RESEARCH REPORT

Evaluating the potential of microfinance for sanitation in India

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Contents

Abbreviations and acronyms

APL	Above Poverty Line
BPL	Below Poverty Line
CGAP	Consultative Group to Assist the Poor
CLTS	Community-Led Total Sanitation
GoI	Government of India
GP	Gram Panchayats
EIC	Education Information Communication
HBS	Household Budget Survey
HH	Household
IHHL	Individual Household Latrine
INR	Indian Rupee
JLG	Joint Liability Group
JMP	WHO/UNICEF Joint Monitoring Programme for Water Supply and Sanitation
MDGs	Millennium Development Goals
MFI	Microfinance Institution
NABARD	National Bank for Agriculture and Rural Development
NBFC	Non-Banking Finance Company
NGOs	Non-governmental Organisations
NGP	Nirmal Gram Puruskar
ODF	Open Defecation Free
PRI	Panchayati Raj Institutions
PS	Panchayat Samitis
RBI	Reserve Bank of India (Central Bank)
SHG	Self-Help Group
TSC	Total Sanitation Campaign
UNICEF	United Nations Children's Fund
USD	United States Dollars
VIP	Ventilated Improved Pit latrine
WSP	Water and Sanitation Programme
ZP	Zilla Panchayats

Note: the exchange rate used in this report is 1 USD = 45 INR, as of June 2011.

Executive Summary

This case study investigates how household financing for sanitation can be mobilised via microfinance institutions and commercial banks in order to accelerate sustainable access to sanitation facilities and/or services.

The research (conducted in India between May and June 2011) sought to document existing experiences in providing microfinance services to households to allow them to invest in sanitation solutions that meet their needs. The objective of the research was to map out the existing provision of microfinance for sanitation, identify where opportunities for future market development lie and identify how the development of such a market could be fostered (through the targeted use of public funds or regulatory changes for example).

The research was conducted in three main steps. First, we identified those organisations that have been actively providing microfinance products for sanitation (and water). Second, we interviewed selected microfinance institutions, considered to be the most relevant ones based on the extent of their activities in the water and sanitation sector. Finally, we conducted more detailed interviews and field research for two microfinance institutions offering (water and) sanitation microfinance products and receiving support from external donors, including Guardian and BWDC, which are both operating in the State of Tamil Nadu (albeit in different Districts).

This research has identified that there is potentially high demand for sanitation microfinance in India, due to a combination of factors. Coverage rates remain low (particularly in rural areas) and national policies emphasise household investments (combined with subsidies in some cases, such as in the Total Sanitation Campaign which provide ex-post subsidies once the household has made the investment, hence the need for pre-financing). By 2010, only 31% of India's population had access to improved sanitation facilities (WHO/UNICEF, 2010). This figure hides an urban-rural divide in terms of access to improved facilities (with 54% and 21% in urban and rural areas respectively).

Historically, sanitation activities in India have been carried out based on a grant driven model, with grants provided either by NGOs (e.g. Gram Vikas) or by the Indian Government via the Total Sanitation Campaign. Being grant-based, some NGOs have been unable to scale up their operations to make significant change in the overall sanitation scenario. The subsidy-driven government programme has achieved scale but has suffered from inefficiencies and corruption, which have resulted in a large number of poorly built or unusable toilets.

In parallel, the microfinance sector has experienced rapid growth in India over the last 20 years, which enabled offering sustainable financial services on a large scale for a range of income-generating activities. Microfinance in India started in the late 1980s on the back of the failure of the social banking initiatives of the Government of India through the 1970s and the 1980s. The sector consists of home grown models (mainly the SHG-bank linkage model) and replications of the Grameen model (generally known as the MFI model). Self Help Groups (SHGs) are informal associations of up to 20 women (their average size is 11-14) who meet regularly, usually once a month, to save small amounts (typically Rs 50 to 100 a month). In the framework of a scheme guaranteed by the leading public bank in India (NABARD), commercial banks can lend directly to SHGs (with which they would have established contact with support of an NGO). By contrast, in the case of the so-called "MFI model", microfinance institutions support the creation of Joint Liability Groups (JLGs) which are groups of four to five women set up specifically for the purposes of joint borrowing and extend loans to these JLGs. The MFIs themselves have to borrow the capital from commercial banks, without the guarantee or support of a nationalised bank.

The SHG model was the first one to take off in India and remains the largest in terms of number of borrowers. During the period 2005-2009, however, the MFI model grew at a compounded annual growth rate of 86% in terms of number of borrowers and 96% in terms of outstanding loans, making it one of the fastest growing microfinance markets in the world. This fast growth came to a grinding halt in 2010, however, due to the so-called "Andhra Pradesh crisis", which meant that it has been very difficult for MFIs to access funds from commercial banks, as they deemed such sector too risky. Most recently, lending conditions have started to ease, however, particularly with the perspective of clearer and more stringent regulations imposed by the Reserve Bank of India onto microfinance institutions.

The growth of the overall microfinance market in India and other factors has led a number of organisations, including Water.org, FINISH and the Michael and Susan Dell Foundation to encourage Indian MFIs to offer loans for building toilets and getting water connections. For example, Water Partners International (now Water.org) started supporting BASIX and Gramalaya so that they would start offering water and sanitation loans. These endeavours were supported by both an initial strong demand for "toilet loans" among the population itself and an awareness of micro-finance as potential support to public services activities. Even though these micro loans are not income-generating as traditionally required by an MFI, they are income-enhancing and can be provided to households based on evidence of their revenues and their ability to repay the loans.

Triggered by these different factors, the market for "toilet loans" has been slowly but steadily growing in India, particularly in rural areas, although at a relatively slow pace. As of May 2011, we had identified that at least 146,000 toilet loans had enabled at least 730,000 people in India to build household sanitation facilities. These toilet loans had been provided by a range of institutions, including NGOs, MFIs and non-banking financial companies. Although a number of organisations providing sanitation microfinance started off as water and sanitation NGOs, they have either set up separate microfinance organisations or are in the process of doing so, as a way to facilitate access to commercial bank financing (which is a key constraint on expansion in the wake of the Andhra Pradesh crisis). Loans are usually provided for less than three years (with 12 months being a commonly encountered tenor for MFIs, although longer-term loans are provided as well). The loan amounts were usually around INR 10,000 but could also be higher for larger investments (BWDC provided a loan as high as INR 350,000 for septic tank, toilet and bathroom).

Demand for sanitation loans seems to outpace potential supply and repayment rates have consistently been very high (above 98% and frequently at 100%). However, the research also helped identify a number of factors constraining such demand. A point that was repeatedly stressed was the importance of coordinating sanitation microfinance promotion with hygiene awareness campaigns: in villages where no such campaign had been conducted, demand for sanitation loans appeared to be lower. The market for sanitation loan products is also limited to a certain population group which includes the poor but not the ultra-poor. This group is very large given the scale of the coverage deficit in India, which means that the potential market for sanitation microfinance still outstrips current supply.

A number of external funders and donors have stepped in to help overcome support the development of the market. External funders have provided support in a number of ways, including through grants, guarantees and facilitated access to commercial lending. They have also facilitated the signing of partnerships between microfinance institutions, NGOs, and government institutions so as to ensure that microfinance is offered as one component of an overall package of services that can, taken together, boost access to sanitation in India.

The research develops these findings based on the evaluation of experiences from a small sample of NGOs and MFIs providing sanitation microfinance (identified based on a thorough screening process) and concludes with the identification of future research needs, with respect to the impact that accessing a loan for building a sanitation facility has on households that take on a loan and to ways to influence the behaviour of microfinance institutions so that they start promoting sanitation microfinance products.

1. Introduction

1.1. Case study objectives

The objectives of the research were to investigate how household financing for sanitation can be mobilised via microfinance institutions and commercial banks in order to accelerate sustainable access to sanitation facilities and/or services.

The research (conducted in India between May and June 2011) sought to document existing experiences in providing microfinance services to households to allow them to invest in sanitation solutions that meet their needs. The objective of the research was to map out the existing provision of microfinance for sanitation, identify where opportunities for future market development lie and identify how the development of such a market could be fostered (through the targeted use of public funds or regulatory changes for example).

This case study has fed into broader research about how donors can channel financing for water and sanitation to small-scale actors (Trémolet, 2012). It was also used as a basis for discussion on how to grow the sanitation microfinance sector in Tanzania, during a companion case study conducted in the context of the SHARE research.

The audience for this research comprises microfinance institutions, sanitation sector actors and funders. As a result, it is crucial to define key terms used in this report, such as microfinance and sanitation, as developed in Boxes 1 and 2 below. Additional details on sanitation solutions are also provided throughout the report for the benefit of readers with no prior sanitation sector knowledge.

Box 1: What is microfinance?

Microfinance has been practiced for many years in different forms. It first became prominent in development circles in the 1970s in Bangladesh, with the provision of small loans for income-generating activities with only minimal collateral requirements and at lower interest rates than those available through traditional lenders (although still relatively high). These loans were provided by microfinance institutions (MFIs) with a good knowledge of local communities and therefore a better ability to manage underlying risks and keep costs down.

Microfinance often refers to financial services for low-income people offered by different financial institutions. The concept is commonly used to mean loans by microfinance institutions. However, over time microfinance involved the provision of a broad range of financial services including loans, savings and insurance. Microfinance institutions use various methods, such as joint liability, advance cash deposits and group members' follow-up, to deliver and manage small loans to usually self-employed borrowers.

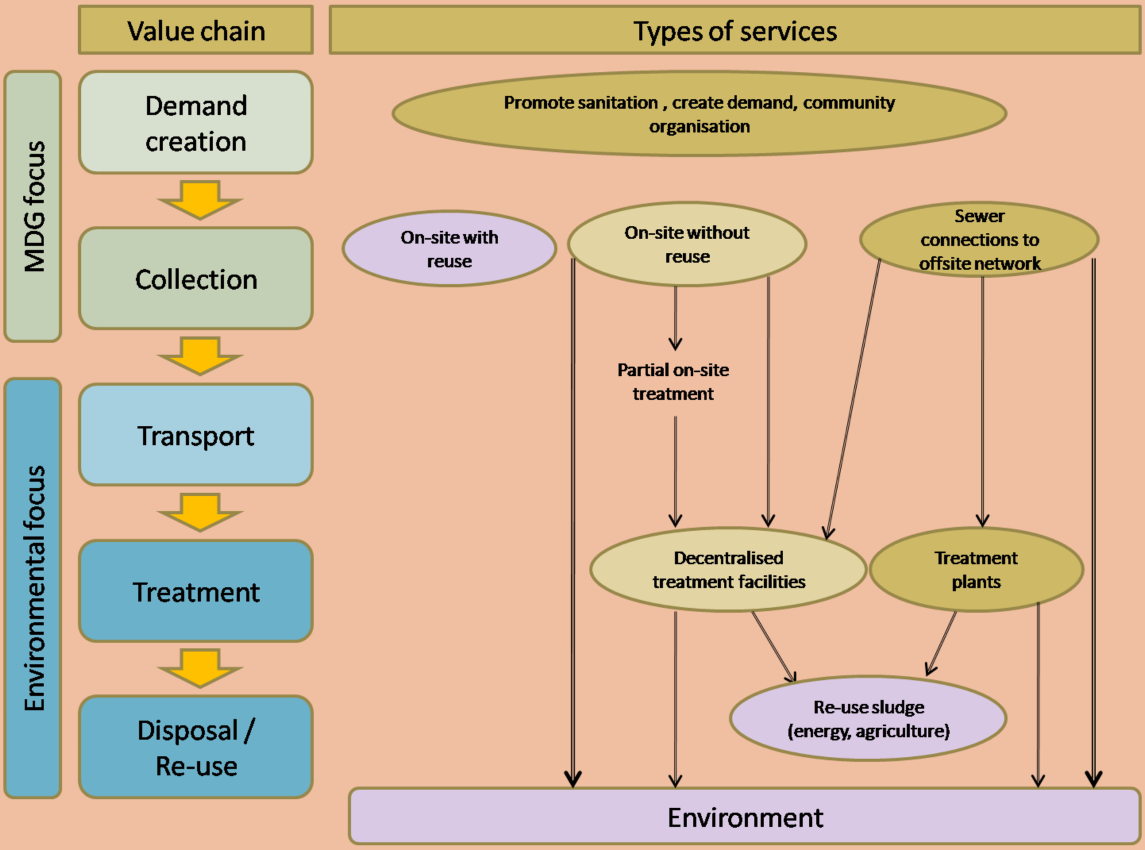
The entities providing such services can include MFIs (for profit or non-profit), but also traditional banks, non-banking financial institutions, SACCOS (Savings and Credit Cooperatives), NGOs and solidarity lending groups, such as Self-Help Groups which are very prevalent in India. The type of institutions providing microfinance services now varies greatly from country to country. In addition, a number of NGOs and microfinance specialists are providing support services to incorporate microfinance products into the design of broader development interventions, which may include development of tailored financial products and/or brokering with financial institutions and training.

See www.microfinancegateway.org for more information.

Box 2: What is sanitation?

Sanitation can be defined as the methods for the safe and sustainable management of human excreta, including the collection, storage, treatment and disposal of faeces and urine. To achieve this objective, a series of services need to be provided alongside the "sanitation value chain", as shown on Figure 1 and detailed below.

Figure 1: The "sanitation value chain"



Demand promotion. Demand for sanitation is often low. Interventions to increase household and community demand for sanitation typically include promotion of sanitation in general, marketing of specific sanitation products, hygiene promotion, social development and mobilization and community triggering.

Collection / access. Human waste needs to be collected and separated from human contact. Collecting the waste can be done either through on-site sanitation solutions (whereby excreta are collected, stored and sometimes treated close to the toilet) and off-site systems, where excreta are removed from the plot, most commonly via waterborne sewerage. In general, as density increases, networked systems are increasingly cost-effective compared to on-site sanitation solutions. Specific services need to be provided to collect the wastes not only from people's homes but also from public spaces (railway stations, markets, etc.), work places and schools.

Transport. When latrines fill up they need to be moved or emptied, while latrines connected to sewers will fail if the sewers themselves fail. In most rapidly-growing cities, emptying is poorly organized and regulated. Householders either empty pits themselves or pay private operators to do so. Pit and tank waste is heavy and costly to transport, and operators often incur additional costs to dump the waste at the official site.

Treatment. Treatment may take place either on-site (some on-site systems allow this, such as septic tanks) or off-site (when the wastes have been collected via sewer networks or pit latrine emptiers and transported to a sewage treatment plant). Treatment of these waste flows is often (although not always) critical to protect downstream water resources, public health and the environment.

Reuse. Suitable treatment can result in waste streams being converted into a valuable resource for reuse, such as fertilizer for agriculture or biogas for energy production.

1.2. Case study methodology

The research was conducted based on interviews with interested water and sanitation organisations, financial institutions and a review of the literature on the subject (see Annexes E and F for more detail). The research was conducted in three stages, as described below.

As a first step, we identified those organisations that have been actively providing microfinance products for sanitation (and water). This initial screening was based on previous literature (including the ground-breaking report on the subject by Meera Mehta for the Gates Foundation) and general knowledge about the microfinance sector in India developed by *MicroSave* over the years.

As a second step, we interviewed selected microfinance institutions, considered to be the most relevant based on the extent of their activities in the water and sanitation sector. As the market for sanitation microfinance is already quite developed in India, it was not possible to carry out interviews with all microfinance institutions offering financial products for household sanitation investments. The results of these interviews are contained in Annex C. These interviews were conducted largely over the phone and email based on a common questionnaire (see Annex D for the interview guide).

Finally, we conducted more detailed interviews and field research for two microfinance institutions offering (water and) sanitation microfinance products and receiving support from external donors. These two institutions are both active in the State of Tamil Nadu:

- ***Guardian*** is the first water-and-sanitation-only microfinance institution in India (and probably in the world). It was selected because of their strong emphasis on the sector and their rapid development in this area, as well as due to the relatively long history of nurturing and support received from the international NGO, Water.org, which allowed us to examine in more detail how donor support can be provided to encourage the development of microfinance for sanitation.
- ***BWDC***, a long-established NGO which has recently established (water and) sanitation microfinance activities was also selected based on its experience in this area. This also gave us the opportunity to evaluate in more detail the type of support provided by FINISH, an internationally funded and supported partnership project promoting microfinance for sanitation as a key way to extend access.

For these two organisations, we conducted extensive interviews with key members of staff (both at headquarters and in the field), sanitation loan customers and some of their funders. This more detailed analysis is presented in Annex A (Guardian) and Annex B (BWDC).

1.3. Report structure

This report is structured as follows:

- ***Section 2*** provides contextual elements for the case studies. The information on the state of sanitation services in India may be most useful to microfinance professionals seeking to understand the sector whilst information on microfinance services in particular can help place sanitation microfinance into a broader context;

- ***Section 3*** presents key findings from the case studies and interviews conducted as part of this research and draws out emerging lessons from these developments, which can be useful not only for India but also for other countries examining the potential of microfinance to boost access to sanitation. It also identifies potential areas to be explored further through more in-depth research.

In addition, a series of Annexes are included, which include the content of the case study research:

- ***Annex A*** includes a detailed write-up of Guardian's experience, the first water and sanitation-only microfinance institution in the world;

- ***Annex B*** contains a write-up of BWDC's activities and the support they have received from the Dutch-funded programme FINISH;

- ***Annex C*** contains a summary presentation of the experience of other financial institutions providing sanitation microfinance products in India;

- ***Annex D*** contains a summary presentation of donor-led programmes supporting the development of sanitation microfinance in India (amongst other activities) and evaluating their fund channelling approaches and experience at channelling funds;

- ***Annex E*** includes the questionnaire used when contacting financial institutions;

- ***Annex F*** includes a list of key references.

2. Contextual elements

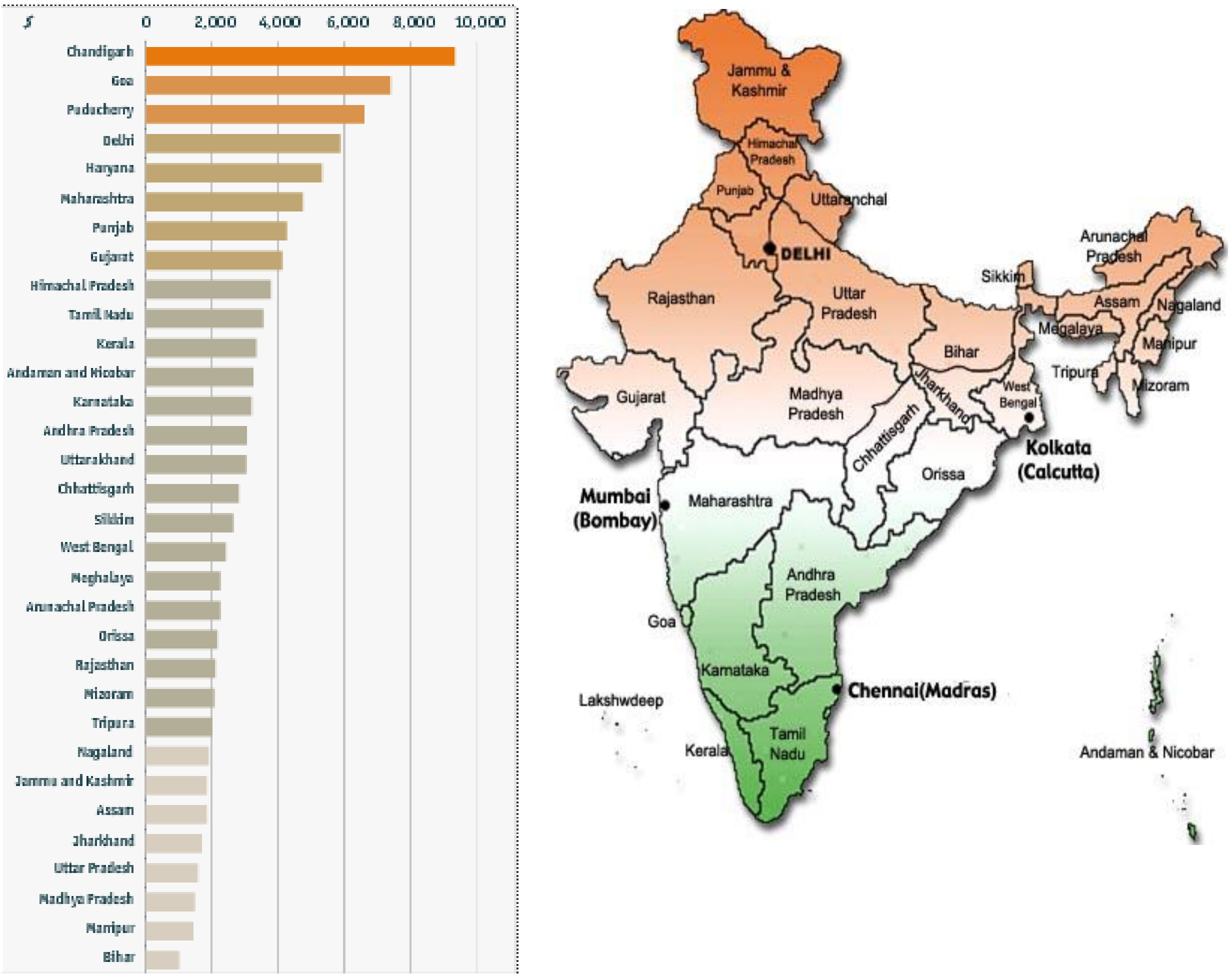
This section sets out contextual elements for the study, including a brief introduction to sanitation services (both urban and rural) and to the microfinance sector in India.

2.1. Country background

Home to more than 1.2 billion people, India has a GDP per capita of USD 3,354/person (PPP$ 2008). The country is recognised as one of the fastest growing economies of the world. The 11th five year plan issued by the Planning Commission of the Government of India (GoI) (2007-2012) began in very favourable circumstances, with the Indian economy having grown at a rate of 7.7% per year in the 10th plan period.

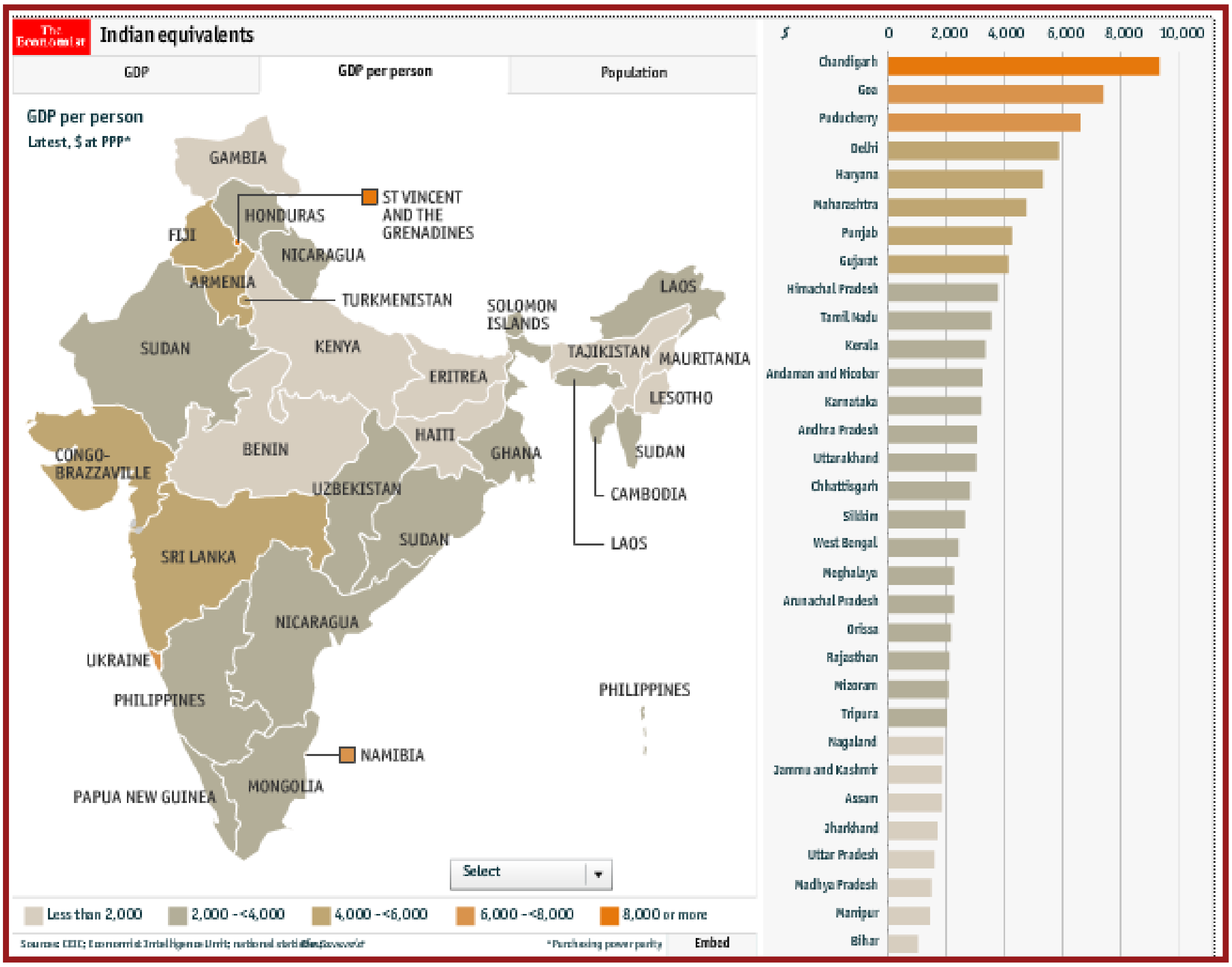
This growth is marred by significant inequalities, however, across states, along rural/urban boundaries as well as across groups. These discrepancies can be observed in recent statistics which show that more than 800 million Indians live on less than INR 20 (less than USD 0.5) per day throughout the country, with the poorest population mostly belonging to socially backward communities concentrated in states such as Orissa, Madhya Pradesh and Bihar (Planning Commission, 2010). Figure 2 below compares GDP per capita throughout the different states of India, whilst Figure 3 makes comparisons with other countries throughout the world.

Figure 2: GDP/capita ($ at PPP)



Source: adapted from www.economist.com/content/indian-summary.

Figure 3: GDP/capita ($ at PPP) across Indian states and comparisons with other countries



Source: adapted from www.economist.com/content/indian-summary

Such inequalities have deepened over the years. From 1960 to 1980, India's focus was on accelerating economic growth. Although poverty was recognised as a possible consequence of this strong emphasis on savings and investments, it was believed to be tackled through the trickle-down effect. In practice, however, several social groups and regions did not benefit at all from this economic growth. During the 1990s, India introduced economic reforms in order to liberalize the economy. Whilst emphasis was mainly on autonomy and competition, it was also recognised that a larger focus was required on human development and as such, sectors such as water supply and sanitation (WSS) slowly became Government priorities.

A pivotal point in the development of India came in 1993, when the GoI passed a series of constitutional reforms which aimed to empower and democratise political bodies known as Panchayats, encouraging local self-rule. India's 28 states and 7 union territories are subdivided into divisions, each comprising several districts. These districts are many times further sub-divided into blocks comprised of village clusters. Although this is the outlining structure, decentralisation in India has been highly variable from one state to another, ranging from village self-rule in Madhya Pradesh to political re-centralisation in Karnataka.

2.2. The state of the Indian sanitation sector

Overall sanitation coverage

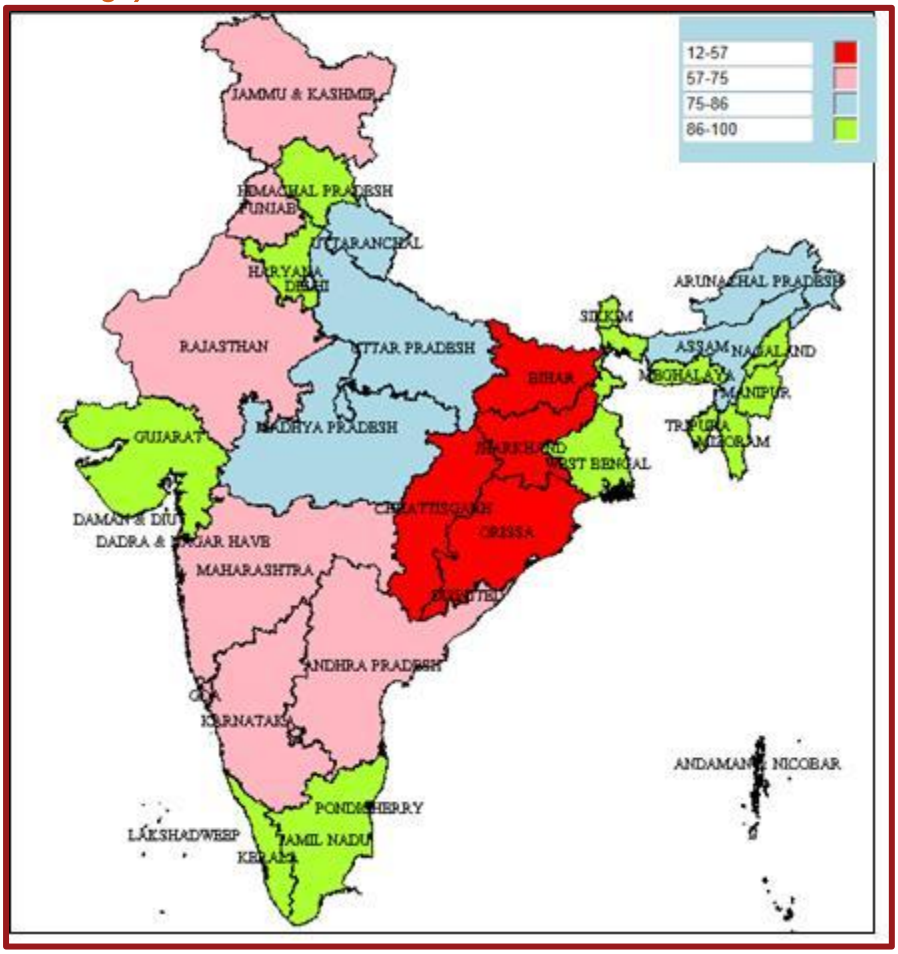
Goal 7 of the MDGs calls on countries to halve the proportion of people without improved sanitation facilities by 2015 compared to 1990 levels. India has complemented this target with one of its own by aiming to provide "sanitation for all" by 2012. In 2010, however, only 31% of India's population had access to improved sanitation facilities (JMP, 2010). Further, this figure hides an urban-rural divide in terms of access to improved facilities (with 54% and 21% in urban and rural areas respectively). At the current pace of progress, given that MDG 7 sets a target of 59% coverage across urban and rural areas in India, the country is unlikely to meet its sanitation target before approximately 2047 (Prüss-Üstün, 2008).

The following sub-sections briefly present the status of sanitation in rural and urban areas.

Rural sanitation

Rural sanitation coverage across India stood at 21% according to the 2010 JMP report. However, this coverage rate varies across the Indian states as shown on Figure 4 below.

Figure 4: Sanitation coverage projected for 2009 (% rural household sanitation coverage)

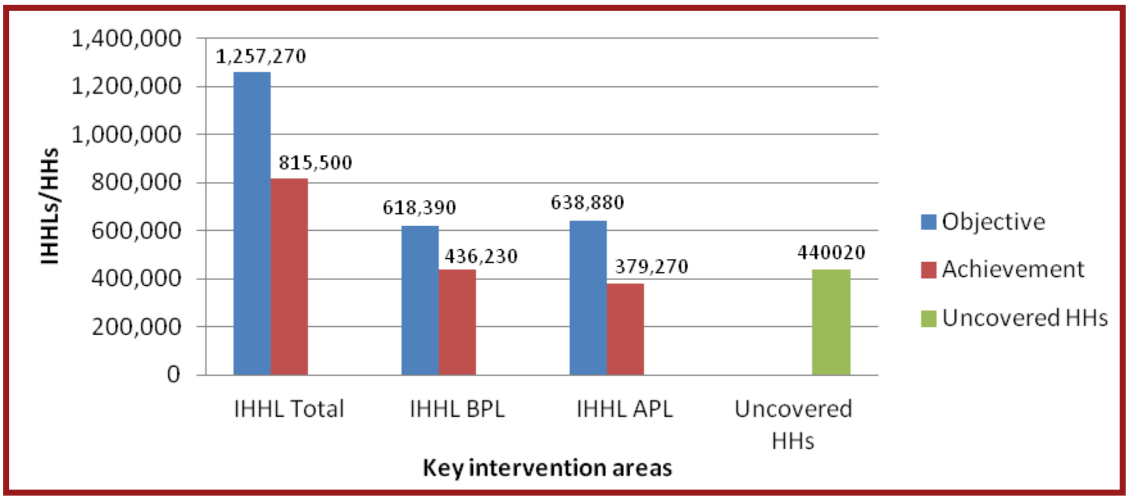


Source: adapted from [*http://gis2.nic.in/tscnew/Default.aspx*](http://gis2.nic.in/tscnew/Default.aspx)

Comprehensive efforts to improve rural sanitation coverage started with the Central Rural Sanitation Program (CRSP) in 1986. This national program mainly relied on hardware subsidies to generate demand from individual households and had only a limited impact on coverage. A new approach was therefore adopted, which advocated a shift from a high-subsidy to a low-subsidy regime, greater household involvement, the importance of education and information of the population and a demand-driven approach.

The Total Sanitation Campaign (TSC) emerged in 1999 as a comprehensive nationwide programme, primarily funded by the Government of India**.** The TSC was designed to take care of both the demand and supply sides of rural sanitation: while IEC (information, education and communication) activities seek to generate demand by creating awareness, Rural Sanitary Marts (RSMs) and Production Centres (PCs) are supported to supply material (such as cement, bricks, foot rest, etc.) for construction of individual household latrines (IHHLs). The "Solid and Liquid Waste Management" component also seeks to achieve general cleanliness of villages.

Figure 5: Objectives vs. achieved results for individual household latrines under the TSC (1999-2011)



Source: adapted from http://tsc.gov.in/RuralSanitationNew/Home.aspx
(BPL = Below Poverty Line; APL = Above Poverty Line)

While policy directions emanate from the national government, the TSC is implemented by the Panchayati Raj Institutions (PRIs). This decision was made as per the 73rd amendment of the Indian Constitution (1992) that contains provision for devolution of powers and responsibilities to local government institutions for preparation of economic and social development plans and their implementation. The PRIs are a 3-tier system of governance that includes the district, the block and the Gram Panchayats (GPs). Since they are the closest level of government to communities, they have been charged with the responsibility of motivating the community to change their behaviour towards better sanitation and facilitating the disbursement of incentives. PRIs often rely on cooperatives, women groups, self-help groups, and NGOs, etc. to bring about desired behavioural change for relevant sanitation practice, construct latrines and run the RSMs and PCs.

Under the TSC, hardware subsidies are provided to below-poverty-line (BPL) households after the latrines have been constructed: since they are outcome-based, they are referred to as "incentives" in the TSC guidelines (Trémolet *et al*, 2010). Although the Government of India has consistently reiterated its commitment to shift from a high to a low or no subsidy approach, the initial capital cost base for subsidies had to be adjusted upwards to reflect cost inflation. From INR 500 (USD 11) at the beginning of the TSC, the amount was raised to INR 1,500 (USD 32) in 2006/07 (USD 54) and to 2,500 in 2008/09.

To add vigour to the TSC, the GoI initiated in 2003 an incentive scheme for fully sanitized and open defecation free Gram Panchayats, called the “Nirmal Gram Puraskar” (NGP) to encourage PRIs as well as individuals and institutions to work towards achieving total sanitation. The NGP provides one-off monetary rewards (which vary in size depending on the population in each community) from the central government to the qualifying GPs based on a set of criteria that include being 100% open defecation free and achieving 100% sanitation coverage of individual households. GPs can use the cash incentive to improve and maintain sanitation facilities in their respective area with a focus on solid and liquid waste disposal and maintenance of sanitation standards.

Although the TSC is a programme designed at federal level, there can be some variations from one State to another with respect to the way in which it is implemented. For example, the state of Maharashtra has been leading the way in terms of achievement under the TSC, with the highest number of NGP awards. The state has ensured that these early achievements be maintained over time through the introduction of a series of additional campaigns, such as the Sant Gadge Baba campaign which monitors achievement of general cleanliness indicators on a yearly basis. Over the course of four years, Maharashtra has seen a 38% increase in coverage throughout the state (Trémolet *et al*, 2010). At the other end of the spectrum, poorer states have not shown such satisfactory results. In Bihar, for example, access remains to be a problem with more than 60% of the rural population without access to an improved latrine. Only a limited number of districts have received the NGP award, and those who have, often received these with delay.

Sanitation in peri-urban and slum areas

Rapid urbanisation has meant an influx of millions of people to urban areas every year. In India, in 2001, the urban population stood at 285 million including 75.26 million people living in slums. Estimates for 2011 indicate that the urban population had grown to 360 million (equivalent to an increase of almost 30% in 10 years), a quarter of them (i.e. 93 million) living in slums. Over the next 20 years, it is expected that India will be home to 250 million new urban dwellers, further increasing the pressure on already stressed services.

Since 1993, the move towards decentralisation made ULBs (Urban Local Bodies), the administrative units providing basic infrastructure and services in towns and cities, in theory responsible for sanitation. However the power to determine the revenue base continues to remain with the state and city planning functions have not been handed over to ULBs in many States. Instead, three broad institutional frameworks exist within Indian states managing the WSS sector. The first of these is the case of an entire WSS system being the responsibility of a department or a parastatal of the state government. Local bodies are thus not directly involved. The second reflects a case where the local bodies such as PRIs and/or ULBs in rural and urban areas respectively take charge of all WSS activities. Lastly, a third case exists in cities, where the responsibility for WSS lays in the hands of a Water Supply and Sewerage Board which is set up for the entire city (Vaidya, 2009).

The government’s role has been prominent in implementing two significant urban policy initiatives. The Jawaharlal Nehru National Urban Renewal Mission (JNNURM) was launched in 2005 with an emphasis on improving the provision of basic services to the urban poor. Under this initiative, the GoI provides 50% of the funds to the States in order for these to undertake infrastructure projects. In return for this, respective state governments, ULBs and parastatal agencies must agree to a set of mandatory reforms. The second initiative, the Rajiv Awas Yojana (RAY) launched in June 2009, has a shorter-term aim: intending to make

India slum-free within 5 years, this approach is centred on pro-poor reforms included in the JNNURM. It includes the provision of basic services to the urban poor and ensuring the delivery of universal services such as health, education and social security.

Public funds alone will not be sufficient to meet the investment required, so financial innovation is likely to be needed to bridge the gap. These include market based funds such as municipal bonds, land-based revenue generation (which capture a portion of the increase in land asset values) and lastly public private partnerships (PPP), when for instance ULBs outsource tasks to other agencies.

Consumers also play a significant role in the provision of efficient WSS services. Before the 1990s, local governments were not involved in the urban development planning process and thus were entirely dependent upon state governments. Residents viewed them as corrupt and inefficient and as a consequence were unwilling to pay for services which were highly unreliable. Due to this, there was a prevalence of informal payments in order to expedite service delivery (Chaplin, 2011).

There has also been admirable progress on participation of communities of the urban poor in the design, construction and maintenance of new community toilets. Empowered communities have greater capacity to make demands upon the state to provide them with basic urban services. For example, Sulabh International Social Service Organization (SISSO) is an NGO which began its operations in the state of Bihar in 1970. Its objectives were based around the restoration of human rights and dignity to scavengers. This was done by substituting manual handling of excreta using bucket privies into Sulabh pourflush toilets. These operated on a pay-and-use basis providing bathing, washing and urinal facilities as well with separate compartments for men and women. Electricity and a continuous water supply are provided in every block and soap is supplied for free to users for handwashing. Trained attendants manage the entire operation, maintenance and collection night and day. Under the public-private partnership model, funds are provided by the government through the local authorities for construction after which the community complex is transferred to private organizations for operations and maintenance.

2.3. Overview of the Indian microfinance sector

The Indian microfinance sector, since its origins over two decades ago, has been on a roller-coaster ride of extremely fast growth interspersed with lean periods, mainly due to external factors (political and financial). Even though it is two decades old, it still faces basic legal questions. The sector has also eulogised and demonised by various stakeholders (including microfinance customers) at various points in time, as explained further in the text below.

Microfinance in India started in the late 1980s on the back of the failure of the social banking initiatives of the Government of India through the 1970s and the 1980s. The sector consists of home grown models (the SHG-bank linkage model and the mutually aided cooperative societies (MACS)[1]) and replications of the Grameen model (generally known as the MFI model).

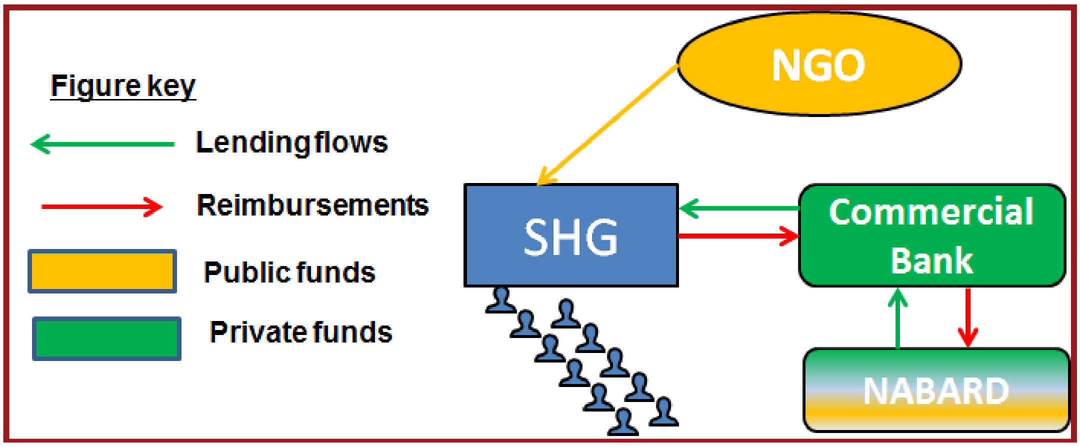
[1] The MACS are a modification of the thrift and credit cooperatives found all over the world and are small in size and restricted to only one state of the country; they are therefore not considered in the present discussion.

Origins and growth of the SHG model

The women-led self-help group model developed in the mid-1980s as an alternative to the credit co-operatives (as the latter was not found suitable for reaching the poor).[2] Self Help Groups (SHGs) are informal associations of up to 20 women (their average size is 11-14) who meet regularly, usually once a month, to save small amounts (typically Rs 50 (USD 1) to 100 (USD 2) a month). While they are formed with the encouragement of NGOs and other self-help promoting agencies (SHPAs) such as government agencies and banks, they are expected to select their own members. They receive basic training from the NGO in financial management skills and book-keeping. After saving regularly for a minimum of six months, and using the funds to lend small amounts to each other for interest, which is ploughed back into group funds, and satisfactorily maintaining prescribed records and accounts, they become eligible to be "linked" by the local bank branch under a NABARD[3]-sponsored programme called the SHG Bank Linkage Programme (SBLP). Norms are laid down for the maximum size of the initial and successive bank loans as an increasing ratio of the group's own-funds. NABARD started lending to women groups on a pilot basis in the late 1980s, in collaboration with MYRADA, an NGO involved in promoting livelihoods and community development in Karnataka.

The success of this project led the Reserve Bank of India (RBI) to allow commercial banks to lend directly to informal groups. This led to the beginning of the SHG-bank linkage programme (SBLP), as represented on Figure 6 below.

Figure 6: The SHG-bank linkage programme (SBLP)



In the SBLP model, the NGOs are involved in mobilising members to form groups, providing capacity building to members on various issues like book-keeping, leadership and governance and conflict resolution in groups. The NGOs are remunerated for groups formed and linked with banks.

The SHG model was the first mover and all the major NGOs started forming SHGs across the country (PRADAN, DHAN Foundation etc.). The model was also considered to be an empowering model for women as they are expected to perform a number of activities like keeping books of accounts, transacting with banks for depositing and withdrawing money and taking loans. All these functions were hitherto handled exclusively by men. The programme got a big push when Andhra Pradesh state started a programme supported by

[2] Fernandes, Aloysius P."Is Microfinance leading to Macro Mess", RMS series, MYRADA. Retrieved from the site: http://www.myrada.org/myrada/rms58.

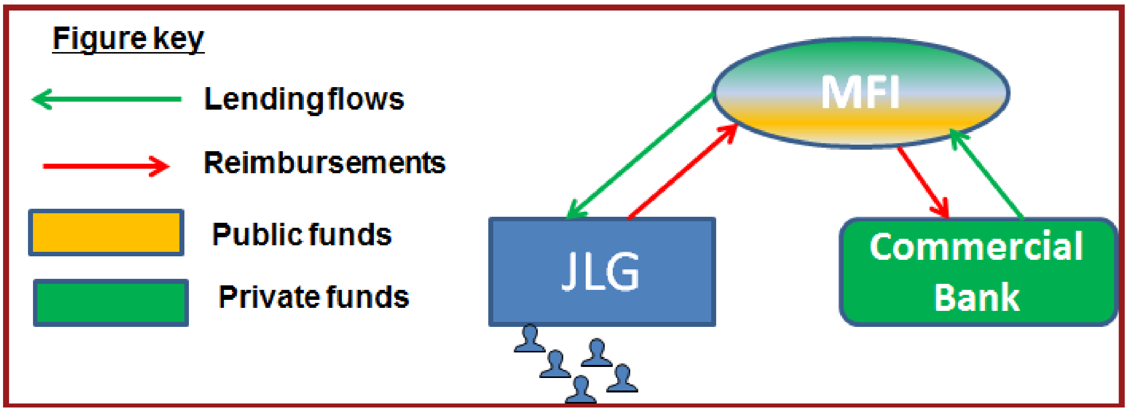
[3] NABARD (National Bank for Agriculture and Rural Development) is the main APEX bank set up by the Government of India to facilitate credit flow for promotion and development of agriculture and integrated rural development. NABARD refinances commercial banks for the loans given to SHGs.

the World Bank in 2000 to create SHGs across the state. As of March 2010, around 60 million clients were linked with banks under the SBLP.

Origins and growth of the MFI model

In the early 1990s, some development NGOs inspired by the success of the Grameen bank in Bangladesh started replicating the Grameen model in the country. In this model, NGOs act as microfinance institutions (MFIs) and lend directly to small groups (called Joint Liability Groups, JLGs) or sometimes to SHGs too, as shown on Figure 7 below.

Figure 7: The microfinance model



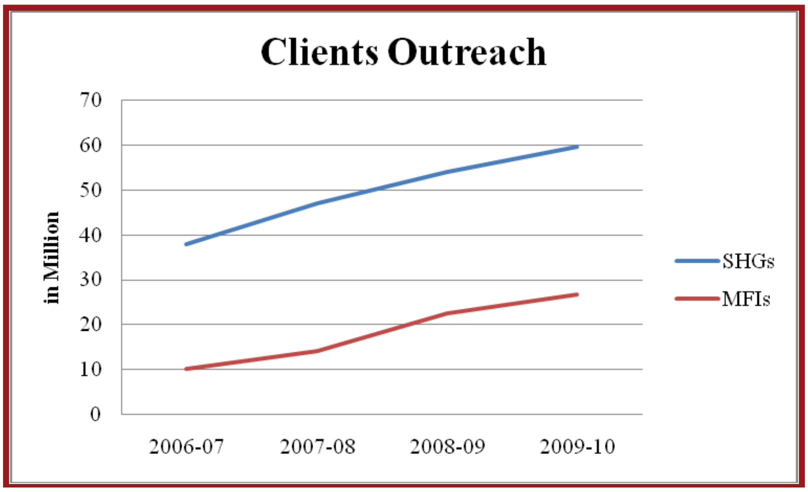
Joint Liability Groups are made up of fewer members (up to 5 members) and are formed solely for the purpose of taking up a loan, which means that members do not perform any book keeping or financial transactions with the banks. Neither SHGs nor JLGs require collateral in the legal or financial sense normally inferred. Instead, the group lending model substitutes the need for collateral by requiring that if one of the members of the SHG or JLG defaults one month on a payment, the rest of the group will pay on their behalf. This can be for whatever reason, for example a family emergency.

The MFI model in India was largely based on the Grameen Bank model of Bangladesh. In the late 1990s, RBI issued a circular making lending to MFIs and SHGs part of the priority sector lending[4] of the banks. This paved the way for the entry of bank funds directly to MFIs. The private sector commercial banks (ICICI) were the first to take the lead and later the government owned-banks (like SBI etc.) followed suit.

The MFI model grew at a compounded annual growth rate (CAGR) of 86% in terms of number of borrowers and 96% in terms of outstanding loans during the period 2005-2009, making it one of the fastest growing microfinance markets in the world till the microfinance crisis hit in late 2010. Since the crisis, however, the market has slowed down considerably. Some MFIs are still growing but a lot of the smaller MFIs are struggling and some have wound up their operations.

[4] Priority sector lending is a policy initiated by the RBI prescribing that a portion of bank lending should go for developmental activities, which include agriculture, small-scale industries, cottage sector, tiny sector, export sector, and other small business (service) firms. With this policy, private banks were assigned an important role in the economical development of the country.

Figure 8: Growth of the Indian microfinance sector



Source: Microfinance Sate of the Sector Report for the years 2006,2007,2008,2009 and 2010

Legal forms for MFIs

The different legal forms under which MFIs are registered are Societies, Trusts, Section 25 (Not-for-Profit) companies, Non-Banking Finance Companies (NBFCs), Cooperative Societies and SHG Federations. Of these, only the NBFCs are for profit, whilst the rest fall under the non-profit category.

From around 2005, there has been a shift in the legal form of the MFIs. Initially, most of the MFIs were registered as societies or trusts and worked as not for profit MFIs. As the MFIs grew, the banks asked for more capital to secure their loans. Societies and trusts, being non-profit entities, could not raise capital from investors who were eager to cash in on the profits available in the sector. This led to the transformation of the large NGO-MFIs into for profit NBFCs. The share of NBFCs in portfolio outstanding has grown from 50.5% (2005) to 71.3% (2007) and 76.0% (2009). The transformation of the sector led to the entrance of private equity to mobilise capital. Initially, this was considered a welcome trend by all as it helped MFIs to leverage more bank capital and in turn increase their outreach. This also helped in drastically reducing dependence on donor funds.

However, private equity also came with demands for high return on equity (in excess of 30%). This pushed MFIs to pursue a high growth strategy which essentially was to offer a single standardised loan product to all the clients with ever increasing loan cycles that had no connection with the business or household cash flows of clients. The focus was no longer on building client relationships but on just lending and recovering the money.[5] Consequently, this led to neglect on important issues of client protection and political risk. The sector had enough warning signs in the form of large scale defaults in Kolar district of Karnataka in 2009 due to local political interference and a similar incident in Uttar Pradesh in 2008 but these were ignored as isolated events.

SKS microfinance, the biggest MFI in the country at the time, issued an IPO in July 2010, which turned out to be a success as SKS was able to raise its targeted amount of financing. But soon after, in Andhra Pradesh (the state that has the maximum penetration of microfinance in the country), a large number of cases of inappropriate behaviour of MFI staff for loan collections surfaced and a number of suicides in the state were attributed to

[5] Wright.G.N and Manoj Sharma, "The Andhra Pradesh Crisis: Three Dress Rehearsals and then the Full Drama", *MicroSave* India Focus Note 55, *MicroSave*.

excessive pressure for repayments and usurious interest rates charged by MFIs. This led to a clampdown on microfinance activities by the state government. Legislation was introduced and greatly restricted the operations of MFIs in the state. The overall loan disbursements reduced significantly across the country with Andhra Pradesh taking the maximum hit. In the first half of FY2011, MFIs in Andhra Pradesh disbursed INR 5,000 crore (USD 1.13 billion) to borrowers; in the second half of FY2011, these same MFIs could only disburse INR 8.5 crore (USD 1.9 million). The repayment rates also reduced drastically for MFIs with portfolio in Andhra Pradesh with most of the MFIs reporting only 10-15% repayment rate.

The repayment rates in some other parts of the country were also affected. The crisis also led to a scarcity of funds for the sector as banks stopped lending to MFIs due to the overall uncertainty on the legal status of the sector. The overall sector shrunk in size during the last quarter of FY 10-11 with all the major MFIs reporting a reduction in portfolio size.

Following this, the RBI set up a committee (known as the Malegam Committee) to look into the charges of misbehaviour of MFIs and excessive interest rates. RBI accepted some of the committee's recommendations and came out with a draft Microfinance Regulation Bill in July 2011.[6] The highlights of the proposed Microfinance Regulation Bill include:

- The Reserve Bank of India will be the sole regulator of the sector and will regulate all the actors including, Societies, Trusts, NBFCs and not for profit Companies;
- Societies and Trusts can carry on with MF activities after registering themselves as MFIs with RBI. NGO-MFIs with portfolio over INR 1000 Million have to be converted into for-profit NBFCs;
- Mandatory membership of credit information bureaus and adherence to codes of conduct & transparency to clients; establishment of advisory councils at the central and state levels;
- The RBI will have sweeping powers to regulate lending rates and margins besides fixing prudential norms. Among other things, the regulator will have a say on how much loans can be disbursed by MFIs, the numbers of borrowers who can avail these loans and the areas where they can operate. The RBI can also delegate an inspecting authority to look into the books of MFIs.

The RBI guidelines, although they are not formal legislation, initially provided a breather to the MFI sector with a number of banks announcing that they would start lending to MFIs again. However, this original announcement was not followed through with actual legislation and a lot of banks remained cautious about lending to MFIs, particularly small NGO-MFIs, and prefer lending to the bigger institutions.

3. Key findings and future research needs

This section provides a summary of key findings from the case studies and draws out emerging lessons on the potential role of microfinance for promoting access to sanitation. It concludes by identifying areas where more in-depth research would be needed in order to strengthen the evidence and design activities to support the provision of microfinance services for sanitation.

[6] As of September 2012, the "Microfinance Institutions (Development and Regulation) Bill, 2012" had been placed in front of Parliament but was still awaiting formal approval.

3.1. Key findings

The development of sanitation microfinance is relatively recent in India

Historically, sanitation activities in India have been carried out based on a grant driven model, with grants provided either by NGOs (for e.g. Gram Vikas) or by the Indian Government (as discussed in Section 2.2). Being grant- based, some NGOs have been unable to scale up their operations to make significant change in the overall sanitation scenario. The subsidy driven government programme has achieved scale but has suffered from inefficiencies and corruption, which have resulted in a large number of poorly built or unusable toilets.[7]

The development of the microfinance model which enabled offering sustainable financial services on a large scale for a range of income-generating activities (see Section 2.3) led a number of organisations to encourage Indian MFIs to offer loans for building toilets and getting water connections. For example, in 2005, Water Partners International (now Water.org) started supporting BASIX and Gramalaya so that they would start offering water and sanitation loans. These endeavours were supported by both an initial strong demand for "toilet loans" among the population itself and an awareness of micro-finance as potential support to public services activities. Even though these micro loans are not income-generating as traditionally required by an MFI, they are income-enhancing and can be provided to households based on evidence of their revenues and their ability to repay the loans. Triggered by these different factors, the market for "toilet loans" has been slowly but steadily growing in India, particularly in rural areas.

Over the last few years, many different financial institutions have expanded their scope to get involved in the "toilet loan" market.

The Andhra Pradesh microfinance crisis considerably limited commercial finance available to microfinance institutions in the second half of 2010 and first half of 2011: commercial banks were reluctant to lend for this type of activities as they estimated that sanitation microfinance was risky, given that the loans do not generate a predictable income stream.

Other types of institutions have expanded into this market segment. Some NGOs with water and sanitation experience have diversified into and then developed their microfinance activities (see for example the case of BWDC, which is reviewed in Annex B). They either operate an internal department which provides microfinance loans (such as BWDC) or set up a separate institution (as done by Gramalaya, an NGO based in Trichy, Tamil Nadu, which set up Guardian with the help of Water.org as a separate microfinance branch, as set out in Box 3 and Annex A). In other cases, well-established MFIs have developed their water and sanitation financing activities, usually with support from external funders.

Maintaining operations both as an NGO and as a microfinance institution can be a constraint on growth as it limits the possibility to mobilise commercial funding or deposits from their customers. As a result, many such organisations are electing to become Non-Banking Finance Companies (NBFC), which gives them better access to capital but also comes with more stringent regulation. However, as NBFCs, they would need to be regulated by the National Reserve Bank of India, which means a series of restrictions on their activities.

[7] Until relatively recently, such subsidy-driven programmes were mostly limited to Below-Poverty Line (BPL) households, although this is likely to change with the recent adoption of the guidelines for the implementation of the NBA (Nirmal Bharat Abhiyan) in July 2012, which aims to provides partial subsidies to a broader range of the population (including all rural households).

Table 1: Summary overview of financial institutions offering sanitation microfinance products

MFI Name	Type	Number toilet loans (05/11)	Sanitation MF out total activities	External support?	Key points
Guardian	New MFI (split from NGO Gramalaya)	10,673	60%	Water.org	• Has grown steadily over 2008-2011 period, but further growth has been limited by availability of commercial bank funding • Has benefited from linkages with sister NGO • 100% repayment rates and strong demand
BWDC	NGO	9,000	9.66% (including water)	FINISH	• 100% repayment rates and strong demand • Institution satisfied with sanitation programme, looking to expand
Grameen Koota	NBFC	5,050	20 branches out of 160	Water.org	• Conducted demand analysis prior to launching products and ex-post evaluation which demonstrated the social impact of the programme • The institution is very satisfied with the sanitation programme and looking to expand • Noted that there are high intermediation costs which need to be covered externally
BASIX	NBFC	3,919	USD 40,500/ USD 248 million (0.16%)	Water.org	• Their sanitation loans have longer term than standard income-generating loans • Conducted an evaluation of the sanitation loan programme which showed positive impact • They identified a potential for expansion but this is limited as households are not always aware the cost of investing in sanitation
ESAF	NBFC	7,400 (including water loans)	3% approx.	Water.org	• They identified a lot of untapped demand for water and sanitation loans. This needs to be stimulated through hygiene and sanitation awareness activities and promotion. This requires working together with a specialised NGO.
FWWB	Apex Organisation	2,000 (including water)	10%	MSDF MOU with Water.org	• Provide grant and loan support to socially orientated MFIs for sanitation • Estimated that their partners use approximately 10% of housing loans for sanitation and estimated that there is strong potential demand.
SEWA Bank	Cooperative Bank	7,000 (including water loans)	15% loan portfolio	MSDF Water.org	• Runs programmes together with municipal governments to provide improved housing (including sanitation) to slum dwellers • High repayment rates (approximately 96%)

Box 3: The example of Guardian: the first MFI only dedicated to water and sanitation

Guardian is the first water-and-sanitation-only microfinance institution in India (and probably in the world). They offer water and sanitation loans (referred to as “toilet loans”), which are targeted at poor households, mostly in rural villages and some urban slums. Although they are still relatively small, they have been rapidly developing since their creation in late 2008 and demonstrate a potential for further growth, backed by strong operational and financial record. During their first three years of operation, they had disbursed close to 20,000 loans to households (60% of which for sanitation) which had attracted a 100% repayment rate.

Guardian (www.guardianmfi.org) was formally established in November 2007 with help and support from Water.org by the board members of an NGO operating in Tamil Nadu, called Gramalaya. This NGO had had a long history of working in water and sanitation, beginning with the installation of hand pumps in 1986. On the sanitation side, they conduct hygiene education campaigns and have also helped with the establishment of community-run toilet blocks in urban slums of Trichy, which are working remarkably well.

Gramalaya was involved early in the pioneering of the WaterCredit concept with the aid of Water.org (formerly known as Water Partners International). In March 2005, Gramalaya decided it did not want to continue with lending activities but preferred to maintain its status as a trust and establish a separate but related organisation, Guardian, to be in charge of micro-lending operations in water and sanitation. Some of Gramalaya’s board members and long-standing staff went off to create Guardian, bringing with them technical expertise in the water and sanitation sector. Guardian was registered as a Section 25 company under the Indian Companies Act 1956, which means that it is a not for profit MFI. As such, it is able to borrow directly from commercial banks (something that Gramalaya, as a charity, was not able to do). Guardian uses the MFI model (represented on Figure 7), which was developed in India based on the experience of the Grameen bank in Bangladesh. The toilet loans they offer have the same conditions in both urban and rural areas, with a principal of INR 10,000 (about USD 222 using a 45 INR to USD exchange rate), repayable over 18 months and attracting an 18% interest rate (reducing balance) plus 3% of financial charges.

To date, Guardian has received commercial loans from the local branch of the Indian Overseas Bank (IOB) for a total of approximately USD 1.6 million. Other banks have not been willing to fund them as they deemed Guardian’s rating insufficient. Gramalaya also provided Guardian with a guarantee, which means that if they default on a loan to IOB, the amount will be taken from Gramalaya without affecting Guardian’s borrowers. However, the operating performance of Guardian has been healthy since the beginning and as of late 2011; the organisation was very much able to stand on its own feet, without the support of its initial supporting NGO.

Guardian received initial and subsequent grant support from Water.org, an NGO based in the USA that focuses on supporting water and sanitation through its WaterCredit initiative, for a total of approximately USD 165,000 by the time of writing. Until May 2011, Guardian received grant support for its operational costs (pre-dominantly salaries and administration expenses) from Water.org. Grant support also covered the costs of technical and institutional support provided by Basix IGS (Indian Grameen Services), the Institutional Development Services branch of a leading Indian MFI based in Hyderabad as well as from ASA, based in Bangladesh. Support from Basix IGS was provided over the course of 6 months and covered activities such as initial training, research, product design and development, preparation of operational policies and definition of collection systems. The MFI is now able to stand on its own feet and operational grants are phased out.

Each USD invested by Water.org in Guardian's activities leveraged approximately USD 16 in commercial funding (a total of USD 2.6 million, mostly from a local commercial bank and including so-called "patient capital" from social investors such as Acumen Fund and Milaap). Guardian has more recently approached social investors in an attempt to diversify their funding sources. They have also obtained funding from Milaap (a small NGO based in Bangalore which functions on the Kiva model[8]) and Acumen Fund, which invests in social enterprises throughout the world and is willing to accept lower (and slower) returns on its investment than private investors.

See Annex A for more information.

As of May 2011, we had identified that at least 146,000 toilet loans had enabled at least 730,000 people in India to build household sanitation facilities. These loans had been provided by the institutions that we interviewed (as listed in Table 1) as well as a few others (as presented in Table 2). The largest number of sanitation loans on record had been provided by BISWA (the Bharat Integrated Social Welfare Agency) which is an NGO and MFI based in Sambalpur Orissa and was one of the initial founder and partner of the FINISH partnership (see Box 5 for more detail). As of May 2011, it had reported to have made 115,000 sanitation loans in 30 districts in the State of Orissa (where it is based).

We were able to identify these financial institutions as providing sanitation microfinance because most of them had received support from international funders such as Water.org, the Dutch-supported FINISH programme or the Michael and Susan Dell Foundation (see Annex D for more information on these external assistance programmes).

Table 2: Number of toilet loans made by a sample of financial institutions

NGO/MFI	Number of toilet loans (as of May 2011)
BISWA	115,000
Guardian	10,673
BWDC	9,000
ESAF	3,600
Grameen Koota	5,050
RDO Trust	700
IIRD	552
SAMBAV	1,710
Sample total	**~ 146,000 loans, reaching ~ 730,000 people**

Identifying financial institutions that are active in sanitation was complicated by the fact that most of them do not track the ultimate use of funds for the financial products that they offer. Therefore, it is likely that financial products provided by other institutions, such as for housing improvements for example, do end up being used by households to acquire sanitation facilities, although there is no evidence on this point at this stage.

[8] Kiva is a non-profit organisation that enables people to lend money via their website kiva.org. Kiva works with "field partners" – these can be microfinance organizations (MFIs), social businesses, schools and non-profit organizations – which disburse the loans and collect repayments.

Most of the institutions consulted operated based on the MFI model (see Section 2.3 setting out the difference between the NGO and the MFI model), whereby the MFI mobilises commercial funding and on-lends to a JLG (Joint-Liability Group).

Details of sanitation loans provided by a sample of institutions are provided in Table 3 below. Loans are usually provided for less than three years (with 12 months being a commonly encountered tenor for MFIs, although longer-term loans are provided as well). The loan amounts were usually around INR 10,000 but could also be higher for larger investments (BWDC provided a loan as high as INR 350,000 for septic tank, toilet and bathroom). Loan sizes tend to be higher for sanitation than for water. In some cases, MFIs charge a lower interest rate for the sanitation loans than for standard loans, with a longer maturity in order to spread the payment over a longer time period (and thereby increase affordability). However, most MFIs charge market rates for these loans. It is important to note that the interest rates shown in Table 3 are indicative for this particular time period, since interest rates would tend to vary depending on local market conditions.

Table 3: Sanitation loans - summary details (as of May 2011)

MFI Name	Typical Loan amount (INR)	Maturity	Interest rate	Other charges?	Repayment rates
Guardian	10,000 (single product)	18 months	18%	3%	~ 100%
BWDC	From 6,000 to 350,000 depending on investment – most common at INR 8,500	12 to 16 months	22%	1%	~ 100%
Grameen Koota	10,000	24 months	20%	1%	100%
BASIX	30,000	36 months	24%	1%	n/a
ESAF	12,000	12 to 24 months	26%	nil	99.2%

Note: Interest rates indicated in the table below are "reducing", which means that they apply to the reducing loan balance.

Based on our case study research, which covered both urban and rural areas, there appeared to be strong demand for "toilet loans" amongst the population.

Microfinance can help households make sanitation investments, i.e. build an on-site sanitation facility or finance a connection to the sewerage network. Obtaining a small loan can help households overcome affordability constraints, as it enables them to spread the cost of the investment over a longer period of time, which reduces the impact of the initial cash outlay. All institutions consulted indicated strong demand for the sanitation products, and this was confirmed during our visits in areas served by BWDC and Guardian.

Experience indicates that helping households invest in water and sanitation facilities can generate a stream of benefits for those households and can be significantly "income-enhancing". Income can be achieved through a reduction in the number of days lost to illness and in medical expenses and an increase in productivity. This can in turn boost revenues and enable loan repayment (in the case of micro-credit). As a result, even though these loans are not income-generating, they are provided to households based on evidence of their revenues and their ability to repay the loans. Repayment rates are consistently very high (consistently above 96% and in most cases close to 100%), which shows that such a strategy, if applied well, can pay off.

However, the research also helped identify a number of factors constraining such demand, as detailed below.

A point that was repeatedly stressed was the importance of coordinating sanitation microfinance promotion with hygiene awareness campaigns. In communities where no hygiene awareness or sanitation promotion campaigns had been conducted, demand for sanitation loans was typically low. When general MFIs (i.e. with no specific sanitation experience) are involved, coordination between sanitation promotion campaigns and the efforts undertaken by credit officers to market sanitation loan products can be enhanced through partnerships between sanitation NGOs and MFIs.

The market for sanitation loan products is limited to a certain population group, which includes the poor but not the ultra-poor. Several of the institutions consulted (including NGOs and NBFCs) thought that microfinance could be a very effective way of helping the poor get access to sanitation, even if it might not be appropriate for the poorest of the poor. For example, the MFI Guardian considers that they would be able to reach 30 to 40% of the population in a given village. These would typically include poor households working in subsistence agriculture (in the case of rural areas) but would not include the destitute (who might be eligible for household subsidies under other types of programmes, including housing programmes). Despite these limitations, it appears that microfinance offers good prospects for improving the quality of life of a substantial portion of the poor population in India, particularly in rural areas, thereby opening up the possibility to better target available subsidy funds on a smaller group of the population. Specific, complementary, strategies may need to be defined for reaching the ultra-poor. As these strategies are typically defined by governmental institutions, this means that the institutions in charge of developing microfinance sanitation (and water) products need to establish strong coordination with the local government institutions so that they can jointly identify which segments of the population within a given community can be served via microfinance and which market segments call for targeted subsidies. In the villages that we visited, for example, households which had a thatched roof house were in some cases eligible for a housing subsidy, which came in the form of a house including a toilet. This would also be important so that the provision of subsidies through parallel programmes does not dampen demand for sanitation microfinance products.

In some cases, we also observed a misunderstanding on the part of households of the costs of investing in sanitation, which means that households may be less willing to take on a loan to build toilets or build toilets of an insufficient quality (simply because they are cheaper). This can be addressed when technical expertise is at hand and can be provided jointly with loan marketing. This principle is at the core of the FINISH programme, for example, which provides technical expertise alongside marketing of loans. This ensures that the toilets that are built with the loans reach minimum standards and are also durable and cleanable.

On the supply side of the market, all institutions consulted as part of the research indicated that they saw the sanitation microfinance market as attractive, with substantial growth potential.

Developing sanitation microfinance products can be attractive for both NGOs and MFIs looking to scale-up their operations with limited grant funding at their disposal. All institutions consulted indicated that they had had positive experiences. However, several organisations noted the comparatively higher operating costs of making sanitation loans (as compared to standard microfinance loans), due to a high number of visits required prior and after the loan has been made for follow-up (for marketing, sanitation promotion but also monitoring that the toilets built with the loan proceeds are of a satisfying standard). As a result, it is the more “socially-minded” MFIs (and NGOs) that are more likely to get involved in the sanitation loan business rather than the more commercial ones. However, increasingly the NBFCs have also shown an interest, partly because they see entering the sanitation microfinance business as a way to improve their social performance.

A key factor limiting expansion for the supply of sanitation microfinance products has been access to commercial capital rather than demand for their products. The study coincided with a particularly “dark” period for the Indian microfinance sector as it took place the year after the so-called Andhra Pradesh microfinance crisis, which considerably limited commercial finance available to microfinance institutions in the second half of 2010 and first half of 2011. Commercial banks have been particularly cautious to lend for this type of activities (sanitation microfinance), as they estimate that they are riskier because the loans do not generate a predictable income stream and there is still relatively limited experience for this type of lending.

Developing the market for sanitation microfinance often requires external support. There are various ways in which donors can provide their support to market development.[9]

Given the potential of sanitation microfinance to facilitate access to sanitation but the still limited extent of its development, a number of external donors have sought to support the development of a “sanitation microfinance market” in India, via targeted support to institutions that they had identified as potentially promising.

Partners providing external support have been adopting a mix of strategies in order to encourage the development of sanitation microfinance services. Box 4 below reviews the experience of Water.org in India for example, which has experimented with various models and concluded that supporting MFIs to develop water and sanitation microfinance and helping them access commercial finance to scale up this type of products would be the most appropriate (and scalable) option.

Box 4: Evolution of Water.org support to water and sanitation microfinance in India

As part of a diverse portfolio of water and sanitation activities, Water.org started a microcredit programme for water and sanitation in Bangladesh in 2003. They saw this as a way of leveraging additional sources of finance, over and beyond limited amounts of donor funding. They then expanded to South India in 2004 and to Kenya in 2005. In each country, they enter into partnerships with local MFIs and supporting organisations, including for example DSK in Bangladesh, BASIX, Gramalaya in India, and Equity Bank and KWFT in Kenya. In India, Water.org supported the creation of Guardian, the first water and sanitation-only MFI.

When Water.org (US-based international water NGO) decided to support the development of water and sanitation microfinance in India back in the early 2000s, they went through a very thorough process of identifying potential partners. They screened a total of 70 NGOs and other types of organisations and finally identified Gramalaya as a potential partner after 3

[9] This research has fed into a broader research initiative undertaken through SHARE and the European Union Water Initiative that aimed at presenting experiences and lessons from these experiences to external support agencies looking to support the development of the water and sanitation microfinance market (see Trémolet, S. (2012)). As a result, a number of specific lessons extracted from the research have been aimed at this type of audience.

years of intense discussions. They then provided support to Gramalaya (and others, including BASIX) from different sources of funds and through a variety of models. To start with, Water.org (with support from the Michael and Susan Dell Foundation) provided seed financing for a revolving loan programme. They made a grant to the partner NGO which was intended to cover all costs, i.e. the costs of product and systems development as well as seed financing for the revolving loan programme. The main limitation of this model was that they could only provide limited funding, which naturally reduced the degree to which such model could be scaled up.

With funding from the PepsiCo foundation, Water.org also pursued partnerships with MFIs and found that this model works particularly well. In the MFI-led model, Water.org does not provide financing for the loans themselves, but rather provides assistance to the MFI to develop financial products suitable for the water and sanitation needs of their clients. This requires funding market research, product design and in some case, financial system development activities. Each MFI is responsible for mobilising loan capital through existing channels (e.g. internal savings, commercial banks and social investors). This is the model that they eventually used to support the establishment and subsequent operations of Guardian in Tamil Nadu, set up as an MFI spin-off from the parent NGO, Gramalaya (see Box 3 for more detail). They were then able to gradually phase out the support provided to Guardian so that it would cover its own operating costs.

This approach has enabled them to implement much larger programmes. The WaterCredit network now includes 24 partners. The latest programme in India with support of the PepsiCo foundation had a total budget of USD 8 million of grant funding, which is expected to mobilize an additional USD 26 million in commercial and social investments and USD 1 million in in-kind and community contributions. It appears that the funders (and PepsiCo Foundation in particular) are more interested in the MFI model, which they deem to be more scalable, than in the NGO model.

Source: authors.

Based on this experience, it appears preferable to assist the development of the sector by supporting existing MFIs and encouraging them to extend into the sanitation sector, rather than support NGOs and support them to become MFIs. This is because existing MFIs would already have existing systems in place, a network of credit officers and an established client base, which means that they can rapidly roll out sanitation microfinance products. By contrast, NGOs (or former NGOs) need to spend time acquiring financial and microfinance skills and develop a distribution network before they can achieve scale. For example, Water.org has supported a range of organisations to market sanitation microfinance products, including MFIs or NGOs, having supported for example Gramalaya to spin-off Guardian. Although the establishment of Guardian has been a success, the entire process has taken time (and effort). Where established MFIs are willing to expand into sanitation, they would recommend supporting such MFIs to diversify their product offering rather than supporting NGOs developing microfinance activities from scratch.

If supporting an MFI or an NBFC, however, it would be essential to ensure that such organisations have passed agreements with other types of institutions (such as NGOs) for conducting sanitation and hygiene promotion activities in a coordinated manner or also ensuring the technical quality of the latrines built with loan proceeds. This “multi-partner” approach has been favoured by the Dutch-funded programme called FINISH, as reviewed in

Box 5 below, which was designed as a multi-partner initiative and combines a mix of incentives and support services that makes it innovative and scalable to other parts of India with potential for other countries.

Box 5 - The FINISH programme in India: channelling funding to MFIs for "toilet loans"

FINISH (Financial Inclusion Improves Sanitation and Health) was set up as a 5-year programme in 2008 by a number of partners as detailed below. Its main objective is to expand sanitation infrastructure to rural India to cover 1 million households by 2013. They intend to do this not just through the provision of loans to build toilets, but by promoting an overall "sanitation system" that takes a holistic look at the process, from a strong emphasis on hygiene promotion and awareness-raising through to safe excreta treatment and disposal. As of July 2011, FINISH had contributed to the provision of 132,000 "toilet loans" throughout seven Indian states, with the highest number being provided by BISWA in Orissa.

FINISH functions as a partnership between seven organisations that each brings very different types of expertise. It was initiated by SNS REAAL (a Dutch Bank) and BISWA (an Indian NGO and MFI), with others joining later, including TATA-AIG (an Indian insurance company), WASTE (a Dutch NGO specialised in sanitation and solid waste), NABARD (National Bank for Agriculture and Rural Development), NHB (National Housing Bank) and UNU/MERIT (a US-based university).

On the ground, FINISH works through about eight implementing partners who are based in seven states around India. These are well-established NGOs/MFIs with prior experience in microfinance, with some prior experience of sanitation and that are willing to commit 10% of their microfinance portfolio for work in sanitation. The organisations that were selected mainly operate in rural areas because this is where sanitation coverage is lowest (in some rural areas, it is as low as 5% although average coverage is around 25%).

Given that FINISH operates with a number of different MFI/NGO partners, the terms of the loan products on offer vary according to the capacity of each MFI/NGO. For example, BISWA gives smaller loans of 4000 Rupees (USD 80) over 1 year with a rate of 20% reducing to 10%. By contrast, BWDC gives larger loans of up to 350,000 Rupees (USD 7000) for a package of a septic tank latrine and bathroom.

Once they have selected their implementing partners, FINISH provides them with small grants and technological support for awareness-raising. For awareness-raising, they have included some aspects of CLTS and have also made their own media to promote sanitation. They do not provide funds via a revolving fund, however, as all of their partners would be responsible for mobilising funding via commercial banks.

The programme's strategy is to reach 100% sanitation coverage in a few villages before moving to the next ones. One innovative aspect of the programme is the provision of incentive payments to MFIs and their credit offers to improve sanitation coverage. Reaching total sanitation in a village can be a difficult task because coverage lingers at relatively high levels and very rarely reaches 100%. In order to aim for full coverage, FINISH grants incentive payments to MFIs for their staff, as they play the joint roles of animators and loan officers. Through the MFIs, FINISH channels 600 rupees per month (USD 12) to staff members, which is raised to 1200 rupees per month (USD 24) once their initial target is reached. In addition to this, the organisations are granted 75 Rupees (USD 1.5) for each toilet built from a loan over the 50% coverage target, which is raised to 150 Rupees (USD 3) when village coverage reaches 70% and then rose again at 90% coverage. This incentive payment is paid by FINISH to the relevant partner organisation. In some cases, these organisations will chose to share it with their field workers and in others, to add it to the revenue of the organisation as a whole. Currently, 41% of the total FINISH budget has been earmarked for incentive payments (referred to as “output-based aid”).

FINISH is financed only partly from donor grants whilst the vast majority of funds (90%) are leveraged from commercial banks. The grant portion of the programme, estimated at about 9% of the total funding, has been provided by DGIS of the Netherlands.

For more information, see: www.finishsociety.com

Before deciding whether their assistance is needed and how it can be provided, external support agencies should consider very carefully the overall microfinance context in the country, including the regulatory set-up and the structure of the market (on the supply side as well as the demand side). For example, the lack of regulation of the microfinance industry has been a problem in India. This industry grew extremely fast, which led to some issues of a “boom and bust” nature. Recent regulations have been introduced in reaction to the Andhra Pradesh crisis, which has had repercussions much beyond India’s borders. However, at the time of writing, the bill had yet to be passed and lending conditions remained tough. Once the bill is passed, this should be beneficial to the sanitation microfinance market segment in particular. A good understanding of the regulatory framework for microfinance is therefore essential before deciding on how to get involved.

An external donor considering getting involved would need to be particularly attentive at identifying the most appropriate institutions to support. It would be very important to distinguish between “for-profit” institutions (which were largely behind the so-called “microfinance crisis” in India) and the not-for-profit institutions, which may be more socially-minded and therefore more willing to extend financing in the water and sanitation sectors (which might be considered as riskier than other market segments given that they are not directly income-generating). Given the low level of awareness of most MFIs to the needs of the water sector and the fact that (in the case of household loans), financing is not directly for income-generating activities but serves a broader purpose; the “socially-minded” MFIs would typically be more receptive and appropriate. Other MFIs may want to add this type of product to their portfolios in order to increase their social performance, given the increased level of emphasis coming from the microfinance sector as a whole on evaluating social performance. In many cases, such “socially-minded” MFIs would be those that have evolved from an NGO. For example, when Water.org, decided to pilot projects to support microcredit for water and sanitation in India, they identified an existing water and sanitation NGO, Gramalaya, operating in the State of Tamil Nadu as potential recipient for their support. However, a decision was quickly taken to spin-off Guardian as a separate MFI in order to offer microfinance services. This shows that the emphasis placed on a “socially-minded NGO” would need to be balanced against the need for the organisation providing financing to have reliable and scalable access to commercial finance.

3.2. Future research needs

As mentioned above, this preliminary research has been useful in order to identify key trends in the Indian sanitation microfinance sector. However, the level of resources allocated to this research meant that it was not possible to investigate in a detailed and rigorous manner a number of areas that would be worth exploring in more detail, including:

- ***The impact that accessing a loan for building a sanitation facility has on the households that takes on a loan, in terms of access to sanitation, poverty reduction and health impacts.*** This may require conducting a rigorous impact evaluation, possibly in the context of a randomised-controlled trial. One such trial is being considered, for example, as part of the design of a large water and sanitation project in rural areas and small towns of Ghana (with support from the Bill and Melinda Gates Foundation). This type of study could be considered in India, particularly in areas where identified microfinance institutions are active in sanitation microfinance. The RCT could compare the behaviour of randomly selected households to whom a sanitation microfinance loan is either marketed or sold versus others that have not had access to sanitation microfinance.

- ***Ways to influence the behaviour of microfinance institutions so that they start promoting sanitation microfinance products.*** As mentioned, available public data does not indicate the purpose of the loans provided for sanitation microfinance. As a result, it is not possible to rigorously measure with precision the size of the sanitation microfinance market or to identify trends in provision. As a second-best, we have used a mini case study approach to elicit this type of information. It was possible to obtain some information but this information was not always very comprehensive. Emerging learning for scaling-up sanitation microfinance show that ongoing work with microfinance organisations is required to help them identify demand for sanitation microfinance and develop targeted products. This can be done through action research via direct support at the level of a given institution (to help them identify a potential market and develop a product that meets the needs of such a market) or through the setting up of sector-wide groups that identify common issues and propose common solutions. This type of action research is likely to be initiated in Tanzania (where very little experience with sanitation microfinance currently exists) and could be developed in India, where the sanitation microfinance market is currently much more developed and would therefore lend itself for even more active exchanges of experiences.

Annex A:
Guardian, the first water and sanitation-only MFI

Guardian is the first water-and-sanitation-only microfinance institution in India (and probably in the world). As such, they have placed a strong emphasis on providing "toilet loans" targeted at poor households, mostly in rural villages and some slums, which represent the bulk of their portfolio. Although they are still relatively small, they grew rapidly between 2008 and 2011 and demonstrated a potential for further growth, backed by a strong operational and financial record.

Throughout this period, they received nurturing and support from an international NGO (Water.org), which meant that they were able to obtain loan financing from commercial lenders (Indian Overseas Bank) as well as social investors (Acumen Fund). Whereas their ability to obtain further funding was temporarily at risk following the Andhra Pradesh crisis (partly as a result of such a crisis), as of May 2011, they appeared to have good prospects and their operational and financial outlooks looked stable.

This case study is structured as follows:

- Section A.1. provides an overview of Guardian's origins and activities;
- Section A.2. examines the demand for sanitation microfinance in Guardian's operating area;
- Section A.3. analyses the sources of finance that it can draw from to extend sanitation loans;
- Section A.4. evaluates their financial performance; and
- Section A.5. provides a summary of the conclusions and emerging lessons.

A.1 Overview of Guardian's activities

Origins of the organisation

Guardian (www.guardianmfi.org) was formally established in November 2007 by the board members of an NGO operating in Tamil Nadu, called Gramalaya. It is the only MFI in the country solely dedicated to water and sanitation.

Gramalaya had a long history of working in water and sanitation beginning with installation of hand pumps in 1986. On the sanitation side, they conduct hygiene education campaigns and have also helped with the establishment of community-run toilet blocks in urban slums of Trichy, which are working remarkably well.

In the early 2000s, Gramalaya pioneered the water credit concept with the aid of Water Partners International USA, which is now operating as Water.org. In March 2005, Gramalaya decided it did not want to continue with lending activities but preferred to maintain its status as a trust and establish a separate but related organisation, Guardian, to be in charge of micro-lending operations in water and sanitation. Some of Gramalaya's board members and long-standing staff went off to create Guardian, bringing with them technical expertise in the water and sanitation sector. Guardian was registered as a Section 25 company under the Indian Companies Act 1956, which means that it is a not for profit MFI. As such, it is able to borrow directly from commercial banks (something that Gramalaya, as a charity, is not able to do).

According to their Annual Report 2009-10, Guardian 'envisions poorer societies to have easy access to credit for household water and sanitation facilities'. Guardian's stated mission is:

- To promote household water and toilet facilities through water credit;

- To involve likeminded NGOs, MFIs and financial institutions for the cause of water and sanitation promotion;
- To provide technical support for creation of low cost infrastructure in water and sanitation;
- To create a healthy society and safe environment.

Geographical scope of operations

As of June 2011, Guardian worked in 9 blocks of the Tiruchirapally (Trichy) district in the State of Tamil Nadu (rural areas) and in the urban slums of Trichy City.[10] Tamil Nadu is a comparatively wealthy state when compared to the rest of the country (see Section 2.1). In Tamil Nadu, the Government of India estimates that sanitation coverage is high (see Figure 4) and it therefore does not provide subsidies to households or communities as part of the Total Sanitation Campaign (TSC). However, such high coverage rates at State-level hides some intra-State discrepancies, which means that there are still a substantial number of households without access to sanitation that are looking to invest in household latrines.

Type of loan products on offer

Guardian offers loans for a number of water and sanitation investments as shown on Table A1 below. At the time of the research, Guardian did not offer loans for anything else (i.e. for income generation activities) or even for sanitation as part of a housing loan. As shown in the table, the size of the loans on offer can differ between urban and rural areas (to reflect different investment costs). However, the terms of the loans are the same everywhere, with interest rates, loan processing fees, the risk fee and cash security being the same for water and sanitation products across geographical areas.

Table A1: Loan products offered by Guardian

Loan Products	Urban (INR)	Rural (INR)	Interest rate (diminishing)	Loan processi ng fees	Risk fee	Cash security (refundable)
New water Connection	7,000	5,000	18%	2%	1%	5%
New toilet	10,000	10,000	18%	2%	1%	5%
Renovations (Water/Toilet)	5,000	5,000	18%	2%	1%	5%
Rain water harvesting	5,000	5,000	18%	2%	1%	5%
Water purifier	3,000	3,000	18%	2%	1%	5%
Bio-gas plant	10,000	10,000	18%	2%	1%	5%

For the purpose of this research project, particular emphasis was placed on evaluating the performance of the loans for new toilet construction, set at 10,000 Rupees across urban and rural areas. This was equivalent to approximately USD 220 at the time of the research. The loans are repaid over an 18 months period. There is no collateral, no margin amount from the client and no grace period. Collection of loan instalments is on a monthly basis.

The interest rate is 18%, diminishing, which means that the interest rate is applied to a reducing capital balance, taking account of periodic capital repayments. This interest rate is low compared to the interest rates offered by other NGO/MFIs for loans for other purposes, which frequently charge 24 to 25% (note that the recommended maximum rate set by the Reserve Bank of India for NGO/MFIs to charge on micro-loans was 25% in May 2011). They initially received external funding by Water.org which covered part of their operating costs. This support is now being gradually phased out and as they expect comparatively lower

[10] Note that Guardian only operates in government-authorised slum areas.

operating margins. Nevertheless, they have been able to maintain a good operational and financial performance (as discussed in Section A.4. below).

Guardian started off by giving loans to Self Help Groups (SHGs) set up by Gramalaya. They then started giving loans to Joint liability Groups (JLGs) based on the “microfinance model” where the MFI needs to mobilise funds from commercial banks directly (see Section 2.3 for more information on these lending models). For new operations, Guardian now works mostly through JLGs for the disbursement of their loans. Although 93% of total loans had been awarded to SHGs in the first year, this figure had dropped to 22% by the third year of operation.

By mid-2011, Guardian had been operating for three full financial years. It had been growing slowly but steadily over the period, making a total of 18,244 loans, 59% of which had been for sanitation as shown on Table A2 below (i.e. a total of 10,764 sanitation loans). The percentage of sanitation loans has been increasing over the years. According to its funders, availability of external financing has been a major constraint limiting the ability to grow the portfolio further, as opposed to lack of demand.

Table A2: Guardian’s lending performance and share of sanitation loans

	2008/09	2009/10	2010/11	Total
Total number of loans provided	**3,222**	**7,050**	**7,972**	**18,244**
Water loans	518	1597	2756	4,871
Sanitation loans	1266	4573	4834	10,673
Other loans (bio-gas, etc…)	1,438	880	382	2,700
Percentage of sanitation loans out of total loans	**39%**	**65%**	**61%**	**59%**

Source: Guardian’s annual reports.

Type of toilet construction being supported through Guardian loans

In terms of the type of toilet, Guardian does not seek to influence its customers to select a particular model; clients are free to choose whichever model suits their preferences. Guardian provides all potential clients with a booklet outlining potential toilet types to choose from and the price breakdown of materials that go into constructing each model.

They would typically advocate the leach pit model because it is one of the cheapest to install, has a life of up to ten years and does not require as frequent emptying and maintenance as a septic tank would do. However, if clients know that there will be a sewerage connection coming to their area soon, they may for example, opt for a septic tank model. This is because, even if it is more expensive, it can be easily disconnected and the toilet can then be connected to the network when it arrives. Such a change-over would not be possible with a leach pit toilet. It was for this reason that many borrowers in one of the urban slums visited had chosen the septic tank model.

A.2 Demand for sanitation microfinance products in Guardian’s operating area

This section examines the extent to which Guardian developed its sanitation microfinance products in response to a demand that was clearly identified and how such demand has materialised over time.

Demand for Guardian's services in the operating area

In 2009, Guardian conducted a baseline survey to estimate the demand for their sanitation microfinance products. The survey showed that there was a high demand for their services. Of the 453 respondents to the survey, 88% expressed an interest in constructing a toilet whilst 70% said that 'financial constraint' was their reason for not doing so. If they were to construct a toilet, only 1% said they would use their own money whilst 99% said they would want to take a loan from an MFI/NGO. At that time, it appeared that the current supply of sanitation loans did not meet demand, since only 1% of respondents who had ever taken a loan had done so specifically for sanitation. The majority of the borrowers (63%) had taken loans for consumption, however.

According to the baseline survey, demand for the type of toilets also varied depending on the locality. As the 2009 baseline study revealed, for 10% of respondents, the main constraint cited for not building their own toilet was space. In urban areas, this is a potential factor in determining the type of demand. Customers may be more likely to choose a septic tank model in this situation.

In the areas where Guardian works, the alternative methods of borrowing money are the local money lenders and other MFIs. The interest rates charged by the money lenders are very high, typically at around 36-40% per annum. The mode of repayment is daily which makes it very difficult for borrowers to repay. The government advises an interest rate of no more than 25% by MFIs. It is common for MFIs to charge interest rates of 24 -30% and to have a weekly collection frequency. By contrast, Guardian applies a monthly collection frequency, which was considered to be very convenient by clients. Its interest rates are lower than market rates, partly due to initial operating support from Water.org. As a result, 75% of those surveyed in 2009 were either very satisfied or satisfied with the conditions of Guardian loans.

Visits to villages where Guardian operates during our research revealed a mix of demand levels for their products. In most villages, demand was mainly very high, with individual women consulted indicating a strong willingness for taking on a loan. In one rural community, however, hygiene awareness was low, which meant that hygiene and sanitation promotion was going to be necessary to stimulate demand for sanitation loans. This lack of hygiene awareness was one of the obstacles that Guardian identified to the expansion of its services. Initially, Guardian only promoted its products in communities where Gramalaya had first promoted sanitation, which meant that the up-front behaviour change activities had already been conducted and that demand for their loans was high.

Later on, Guardian started working in communities where there had been no awareness-raising campaigns, either because Gramalaya has not yet been involved or due to a lack of coordination between the two in terms of the timing of their activities, which made it comparatively more difficult to promote toilet loans. In sum, Guardian staff estimated that the major challenges for making their loans attractive to the local population were the need to sensitize communities to sanitation and hygiene up-front, prior to any initiative to promote sanitation loans to facilitate toilet construction.

A factor that has driven strong demand for toilets in recent years, however, has been more stringent enforcement of the rule (applicable in Tamil Nadu) which states that the local Panchayat can only grant permission for building a new house if that house has a toilet. Although this rule has been in existence for some time, it has recently started to be enforced, thereby driving the demand for toilet construction.

Methods used to select borrowers and verify ability to repay

Guardian has attempted to collect information on the economic position of its customers and potential customers, both in the 2009 baseline survey previously mentioned and in the application forms that each new loan applicant needs to fill in before obtaining a loan. However, it has not set strict criteria that would lead them to reject loan applications. For example, Guardian does not encourage loan applicants to have multiple other debt obligations, but there are no bright-line restrictions in this regard. It works in both rural and urban areas and does not restrict itself to any particular community.

Guardian uses the ration card status of new JLG members as a simple needs assessment methodology. Whether the ration card is white, rose or yellow indicates whether people are Above or Below Poverty Line status. However, they appear to use it to monitor the status of their clients rather than using it to select recipients. Of all those who have applied since Guardian first started issuing these loans, only two applications have ever been rejected.

Loan eligibility is based on self-assessment and assessment by the group who must trust other members to keep to the loan agreement. Identity documents do need to be provided by applicants. As part of the selection procedure, Guardian does not impose any minimum salary requirement and savings are not assessed. During the loan application process, they simply seek to evaluate the household's revenues and repayment potential. This is based on household's declarations and not verified. The ultimate test of whether or not a household is able to repay is whether loans actually get repaid. Given that Guardian's repayment rate has consistently remained at around 100% repayment, this seems to indicate that Guardian's methods for evaluating repayment capacity have so far been adequate. Group lending also ensures that group members are satisfied that the persons joining the group are able to repay. The group acts as a solidarity mechanism in the event that a group member is affected by an unpredictable event (such as accident, disease, death or unemployment).

Repayment records and sources of funds for repayment

Repayment rates have consistently been above 98% and at 100% over the last two years. In order to repay the loan, 59% of those surveyed in 2009 stated that they used their own sources. Other answers included drawing from a subsidy from the government combined with their own source of finance (16% of respondents) and via a loan from another NGO/MFI (14%). A very small proportion of respondents chose to still use money lenders (3%) or had access to loans from banks (4%). The majority of respondents when asked said that their loan was 'no burden at all' (54%) whilst 34% said it was sometimes a burden. A minority of 12% said it was burdensome.

This result was supported by our 2011 research in which the vast majority of the SHG and JLG group members we met said they repaid their loans from their own funds.

Characteristics of population reached

Of those surveyed as part of the 2009 baseline study, 38% were daily labourers whilst 16% were farmers and 16% not working. Only 5% in 2009 were government sector workers and therefore, only a small proportion had job security. 40% of those surveyed in 2009 had an average monthly income of 3,001 to 5,000 Rupees whilst their monthly expenditure was in the bracket of 1,501 to 3,001 Rupees. The survey also took note of building materials used for respondents houses to assess their income level e.g. thatch or tiled roofing.

Our findings during our 2011 research differed slightly from the above and showed that some of the households that borrowed had an even lower monthly income. From the 2011 interviews, the vast majority of SHG and JLG members were employed as agricultural labourers earning between 100 and 150 Rupees per day (2,000-3,000 Rupees per month which was equivalent to between USD 45 and 65 per month). One group we visited was a weaving community who would earn 600 Rupees per item produced and no more than 2000 Rupees per month. So the average monthly income of those currently receiving Guardian loans was lower than for those who had been considered as potential customers in 2009. This may be due to a variety of reasons, such as the possibility for households to access other sources of funds for repayment of the fact that Guardian felt able to take on more financial risk once better established.

Guardian estimated that of those poor households that did not have a toilet, they could aim to reach between 30 and 40% of the population. It was therefore anticipated that the remaining of the population would need to benefit from other types of support, such as the provision of government subsidies. We observed that there was scope for improved coordination between local authorities and Guardian on this front, so that government subsidies could be better targeted to those most in need (and are not able to finance investments themselves).

Overall, Guardian feels there is good demand for water and sanitation loans especially in rural areas. According to them, the reasons for which very few MFIs operate in this space is the non-productive nature of the loan and the fact that efforts to sensitise the population and raise awareness are essential in order to generate demand for this type of loans.

A.3 Sources of finance

Guardian is funded through a mix of grants and loans, as shown on Table A.3. below, with only very limited equity initially brought in by Gramalaya. The vast majority of its funding (94%) has come from commercial lending, with some very limited grant support and some limited contributions from social investors. In addition, the MFI has very limited equity financing.

Table A3: Guardian's external financing sources

Source	Date	INR (Crore = 10 million)	USD	Interest rate	Maturity
Commercial Loans					
IOB	Mar-08	1.75	388,889	10.5%	5 years
IOB	Sep-08	2	444,444	12.25%	5 years
IOB	Mar-09	2.25	500,000	11.75%	5 years
IOB	Mar-10	1.5	333,333	11.75%	5 years
Total loans		***7.5***	***1,666,666***		
Grants					
Water.org	Aug-08	0.44	98,298		
Water.org	Apr-10	0.3	67,594		
Total grants			***165,892***		
Social investors					
Milaap	Dec-10	1 lakh	2,222	Interest free loan	1 ½ years
Acumen Fund	Jul-11*	4.5	1,000,000	6%	6 years
Total social investors			***1,002,222***		

*Source: Guardian. * In the process of being discussed at the time of writing.*

Commercial funding

To date, Guardian has received commercial loans only from the local branch of the Indian Overseas Bank (IOB). Other banks have not been willing to fund them as they deemed Guardian's rating insufficient; this has also partly been as a consequence of the Andhra Pradesh credit crisis.

IOB was established in 1948 and nationalised in 1969, when a series of banks were nationalised by the then Prime Minister Indira Gandhi. It is involved in lending to SHGs in a variety of sectors.

Guardian initially approached the local branch of the IOB in 2008. They were able to provide a deposit from Gramalaya (INR 30 lakhs or USD 66,000) which initially served as collateral. The local branch manager has subsequently become convinced that this was a "noble cause" as well as a good business opportunity, as it has obtained excellent repayment rates. The IOB provided further loans (of an increasing size) although no new loans have been provided since the start of the microfinance crisis in Andhra Pradesh in late 2010. In total, IOB has so far lent USD 1.66 million to Guardian (as shown on Table A.3.), as some of the initial loans have already been repaid.

There are currently 34 lakhs (3.4 million Rupees) outstanding of the loan and this is being repaid effectively. The IOB charges a 12-13% interest rate and a 1% loan processing fee. Guardian reflects these rates in the charges it passes on to customers. Each of Guardian's loans from IOB have the same repayment period of 60 months (5 years). Guardian also has a guarantee as provided by Gramalaya. This guarantee means that if they default on a loan to IOB, the amount will be taken from Gramalaya without affecting Guardian's borrowers.

IOB's regional office has however set a ceiling in terms of maximum lending that can be outstanding with Guardian at any given time (INR 6 crores, equivalent to USD 1.33 million). They have been reluctant to lend more as they deem that Guardian does not have enough equity capital and that their operating margins are low, making them unable to cover all their operational expenses.[11]

Access to loan financing has been a key constraint limiting Guardian's growth to date, especially following the Andhra Pradesh crisis which struck in 2010 and 2011 (see Section 2.3 for details).

Grant support from Water.org

In addition, Guardian has received grant support from Water.org (formerly Water Partners International), an NGO based in the USA that focuses on supporting water and sanitation through its rather unique Water Credit programme. Till May 2011, Guardian had received grant support for its operational costs (pre-dominantly salaries and administration expenses) from Water.org (USA). The focus of Water.org support was initially placed on water: the grant agreement specifically required that the funds should facilitate the construction of 4,160 water connections and 160 toilets.

This grant support covered the costs of technical and institutional support provided by Basix IGS (Indian Grameen Services), the Institutional Development Services (IDS) branch of a leading Indian MFI based in Hyderabad as well as from ASA, based in Bangladesh. Support from Basix IGS was provided over the course of 6 months and covered activities such as initial training, research, product design and development, preparation of operational policies and definition of collection systems.

[11] See next section for an analysis of their financial performance, which is in fact healthier than this assumption.

Because of difficulties in getting the grant funds channelled, part of this funding initially had to go through Gramalaya. According to the Water.org Progress Report for January 2011, Guardian received 4,423,400 Rupees as a first instalment via Gramalaya during March 2010 and 3,041,738 as a second instalment on a time frame agreed between Gramalaya and Guardian.

This meant that each USD brought in by Water.org as a public funder leveraged approximately USD 16 in commercial funding (including so-called "patient capital" from social investors such as Acumen Fund and Milaap).

Social investors

Given the paucity of commercial bank finance, MFIs increasingly have to diversify their sources of funding and consider social investors. Guardian has done so in an attempt to diversify their funding sources. They have been in contact with Milaap and with Acumen Fund, as set out below.

Milaap (www.milaap.org/) is an organisation based in Bangalore (India) which provides small loans to individuals based on the Kiva model (direct lending from internet-users to individual borrowers). In December 2010, they provided 1 lakh (just over USD 2,000) in funding, to test the model with loans to 10 individuals. They were planning to increase this funding to 5 lakhs per month from July 2011.

In addition, in 2010 Guardian obtained a USD 1 million investment from the Acumen Fund (www.acumenfund.org/investment/guardian.html) to support their activities. The Acumen Fund invests in social enterprises throughout the world and is willing to accept lower (and slower) returns on its investment than private investors. They can provide funding in a number of ways, including loans and equity.

A.4. Financial performance assessment

Although Guardian has been growing steadily, it is still a relatively small institution. The total number of staff as of May 31st 2011 was 30, of whom 14 were field staff. The number of outstanding loan borrowers was 14,321 and the total loan portfolio was Rs 5.22 Crore (52.2 million Rupees or USD 1.16 million). Table A4 below presents key figures summarising Guardian's financial performance.

Table A4: Financial analysis of Guardian

Ratio	Unit	2009	2010	2011
Gross Loan Outstanding	INR	14,894,755	36,681,139	52,832,381
Growth rate in gross loan outstanding	USD		146%	44%
Loan repayment rates	%	98.00%	100.00%	100.00%
OSS (Operating Self-Sufficiency ratio)	%	137.89%	116.02%	112.74%
Return on Asset (RoA)	%	8.65%	4.95%	9.21%
Portfolio to Assets	%	84.83%	82.51%	88.61%
Active Borrowers per field staff		364	549	719
Cost of Funds	%	7.78	7.23	13.21
Debt to Equity	%	23.02	20.02	17.41
Operating Expense Ratio	%	2.14%	21.36%	14.32%
Cost per Active Client	INR	90	973	694
Average Loan Outstanding	INR	4090	4774	4899

Source: Audited Financial Statements of Guardian for FY 2008-09, 2009-10 and 2010-11. The ratios have been calculated using the formulas prescribed by SEEEP network. The same exchange

Guardian has undergone a number of external evaluations with respect to its financial standing. In 2009 it was rated by M Cril which gave a positive rating of β+ where the highest rating is α++ and the lowest is ϒ.[12] β++ is two notches above the investment grade average and means that the organization has 'reasonable safety, reasonable systems', and that it comes recommended to investors but needs monitoring. This gives an indication of the financial and operational strength of the organisation and shows the organisation is credit worthy. Below, we evaluate the way in which its financial position has evolved over the period 2009-2011, which is the period for which we were able to obtain full financial data.

Profitability Analysis. Guardian had an OSS (Operating Self-Sufficiency ratio) of 100% between 2009 and 2011, which shows that it has been able to cover all its operational costs. The OSS has decreased from 138% in 2009 to 113% in 2011: this reduction is due to the recognition of some expenses that were previously attributed to Gramalaya onto the Guardian account. In 2009, Guardian had shared its costs with its parent organisation Gramalaya but over the past 2 years it has started recognising its expenses in its financial statements. The "Operating Cost Ratio", which indicates the operations expenses as a percentage of the overall portfolio has increased sharply from 2% in 2009 to 21% in 2010. This was due to the same factor (i.e. full recognition of the operations expenses (staff salaries, administration expenses etc.) under Guardian's financial statements. The OCR has since come down to 14% in the last financial year which shows that the profitability of the organisation is likely to improve.

The return on assets which is a primary measure of the profitability of all financial institutions is at 9.21% which is quite healthy. Based on the financial statements it is evident that Guardian is a profitable institution and can stand on its own feet.

Asset Liability Management Analysis. The "Portfolio to assets ratio" is a measure of the percentage of the total assets invested in the primary revenue earning source of the organisation (in this case it is the loan portfolio). This ratio has increased from 84% to 88%

[12] M-CRIL, which stands for Micro-Credit Ratings International Ltd (www.m-cril.com) is an agency specialised in the rating of microfinance institutions and providing sectoral advisory services.

over the 3 years and is quite healthy. The “Debt to equity” ratio which indicates the leverage of the organisation has improved from 23% to 17%. Guardian is still an overleveraged organisation as it has very little equity and it may face difficulty to raise commercial funds in the future as a result. This improvement is primarily due to the increase in the profits accumulated from previous years. Since Guardian is a not for profit organisation, raising equity will be an issue as it is not legally allowed to do so.

Efficiency and Productivity Ratios. The “Active borrower per field staff ratio” has increased from 364 to 719, which shows a significant improvement in the efficiency of the organisation. The average industry standard for the active borrowers per field staff is 450, which means that Guardian is well above the industry standard in that respect.

Cost of funds. The cost of funds of the organisation has increased from 7% to 13%: this is due to an increase in the proportion of bank debt (from the Indian Overseas Bank) over its overall sources of financing.

Overall, Guardian has shown an impressive financial performance over the 2009-2011 period. It has had good profitability and efficiency ratios. However, being a not for profit, one of the key issues that it faces is to raise commercial funds and equity in order to sustain its growth in the long run.

A.5. Emerging lessons

Overall, Guardian has shown a slow but healthy growth since its inception. It is now looking to expand its range geographically as well as within the areas where it currently operates, thanks to a team of well-trained and dynamic credit officers.

Splitting the microfinance operations away from the NGO’s operations (managed by Gramalaya) was clearly a beneficial decision for both organisations. Guardian benefited in many ways from initial support from Gramalaya (in the form of staff transfers or staff sharing, thereby drawing on extensive sector experience), the provision of a bank guarantee and sharing of some other operational costs in the initial stages. The two organisations have now been fully separated and Guardian is now able to stand on its own feet and to cover all of its “real” operating costs.

Lack of external funding has been a key constraint to Guardian’s growth rather than lack of demand for sanitation loans on the part of the population concerned. Such limits on available commercial financing have been particularly felt following the crisis in the “microfinance model” that was triggered in Andhra Pradesh. By contrast, Guardian has observed strong demand for their sanitation loan products, particularly in villages where behaviour change and sensitisation campaigns had already been conducted (in many cases, with the help of Gramalaya). Going forward, the link with Gramalaya (or other NGOs able to organise community sensitisation and sanitation promotion activities) would need to be strengthened and formalised, so that Guardian can come into a community with its offer of sanitation microfinance products once the “grounds” has been prepared, in a coordinated manner. This type of coordination is being encouraged by the FINISH programme in its support to microfinance institutions (see Annex D for more detail).

We observed that there was also ample scope for improved coordination between local authorities and Guardian. From its own acceptance, Guardian does not aim to reach more than 30 to 40% of the population in a given village, who would be interested in and able to repay a toilet loan. Other population groups, especially the poorest, may need to rely on government subsidies to access sanitation. Even though the Total Sanitation Campaign is not present in the areas where Guardian operates, other types of government subsidies are provided, such as to support housing construction (including construction of a toilet) for households identified as poor (i.e. those who had thatched roof housing). Optimal coordination with the local Panchayat (which decides who is eligible for such government subsidy) is likely to be necessary so as to ensure that the subsidies are well-targeted and do not dampen demand for the loans from those who can afford such loans.

From the point of view of donors (in that specific case, Water.org), providing support to Guardian has proven to be a very cost-effective way of boosting sanitation, thanks to a high leverage ratio. This means that each USD brought in by Water.org as a public funder leveraged approximately USD 16 in commercial funding (including so-called "patient capital" from social investors such as Acumen Fund and Milaap). Support from Water.org has been provided in the form of technical assistance to evaluate the market, develop sanitation microfinance products, build operating systems and train staff. Such support ended early on in the process, so that Guardian would not become dependent on external assistance and be able to stand on its own feet.

Annex B:
BWDC: Bharathi Women's Development Centre

Name of financial institution	BWDC
Name of contact and contact details	Bharathi Women's Development Centre (BWDC) Mr. M. Nagarajan – Chief Executive Officer & Secretary Kattur & Post, Manakkal Ayyempetai-via, Thiruvarur
Activities in water and sanitation	NGO/MFI providing loans for water and sanitation, getting support from FINISH
Website	http://bharathiwomen.org/fore.html

1. Main characteristics of financial institution

Background. Bharathi Women's Development Centre (BWDC) is a non-profit organization registered as a society in 1987 under the Tamil Nadu Societies Registration Act and classified as a charitable trust. The main thrust of BWDC is women's empowerment along with rural development, child care, old age care, education, water and environment sanitation, health and hygiene, bio-diversity, rehabilitation of handicapped and complete development of the rural community. They are one of the institutions that receives financial and technical support from FINISH (Financial Inclusion Improves Sanitation and Health), a Dutch-funded programme reviewed in Annex B.

Legal status. Whilst BWDC is currently classified as a charitable trust, they are planning to convert the microfinance branch of their activities into an NBFC or Non-Deposit taking Non Banking Financial Company (see background section on Indian microfinance sector for further explanation)[13]. BWDC is planning to change the name of its financial arm to "Mahasakthi Micro Credit and Service Limited". However, the name change and the procedure to get a new certificate of registration (COR) from RBI, Chennai is under process. Subsequently, BWDC have plans to strengthen the Board of the NBFC with at least 3 professionals on the Board. Once this process is complete, BWDC plans to transfer its entire microfinance portfolio (with the exception of sanitation) into the NBFC which will operate as an NBFC-MFI. Once the entire transformation is completed, BWDC will focus only on its developmental activities.

Staff. The executive board is governed by seven members with long experience in various developmental activities. As of May 2010, BWDC had a total of 61 staff, of which 38 were field staff and 23 non field staff with 15 newly recruited that year.

Microfinance operations. BWDC has been involved in the SHG-bank linkage programme, especially in rural areas since 1995. They organize the SHGs, then build capacity for their functioning, then link them with banks, government programs and NGO programs. The microfinance operations commenced in October 2006 in Tamil Nadu and direct lending started from November 2007. Microfinance operations are carried out as one of the projects of BWDC.

Rating. SMERA, an Indian rating agency focused on the Micro, Small and Medium Enterprise (MSME) segment, has assigned BWDC an MFI rating of 4 out of 9 which

[13] There has been very little in the way of legislation on MF so far and the government is very cautious about the bill currently going through parliament. The original version of the bill (that has not been passed as yet) indicated that trusts would be allowed to conduct MF activities but at present, the status quo is that banks can only lend to NBFCs because trusts and societies are uncovered by legislation.

indicates average credit strength. Within the FINISH partners, BWDC is one of the smaller MFI partners, put at Tier 3 along with SAMBAV.[14]

Localities. BWDC's microfinance operations are spread over three districts: Thiruvarur, Nagapattinam and Thanjavur with 6 branches in mainly rural areas. As of 31st May 2010, BWDC activities were spread over 429 villages with 11,230 active borrowers. The cumulative amount disbursed in 2009/2010 had been INR 61.4 million Rupees (equivalent to USD 1.364 million).

Financial channelling. BWDC keeps two separate balance sheets: one for microfinance activities and one for non-microfinance activities. This is so as to keep their donations and grant monies separate from their loans. BWDC is currently receiving loans from various banks/financial institutions. Some of these are commercial such as HDFC Bank Limited (a commercial housing bank), City Union Bank. Others are nationalized institutions such as Punjab National Bank, Kadra Bank, Bandar National Bank and Rashtriya Mahila Kosh (RK). One other is a private investor called Manaveeya's Holding & Investment Limited. Most of these financial institutions require 10% cash collateral in order to provide a loan, but BWDC is able to provide this.

Financial support is channelled for microfinance in water and sanitation via grants from FINISH to BWDC for their activities. In the 2010/2011 financial year, 300,000 Rupees (6,570 USD) were given for demand generation, technical capacity building and mason training. Those funds for demand generation were intended for the village animators who are given added incentives for reaching incremental targets in accordance with the conditions given in the FINISH brief.

2. Activities in the sanitation sector

BWDC have a history of providing microfinance products that help households invest in water and sanitation solutions that predates FINISH. Their first involvement was with the Central Rural Sanitation Programme of CAPART during the early 1990s.

When the Total Sanitation Campaign came to BWDC districts, a large number of interested families did not receive its benefits. Whilst some local governments have set norms for providing both APL and BPL families with subsidies, most mainly focus on providing subsidies to those below the poverty line with the perspective that this will motivate above poverty line families to construct their own. During this period, BWDC continued to train masons in the construction of cost effective latrines and creation of awareness and demand. However, they could not implement construction due to lack of available finance.

As a percentage of their overall activities, BWDC's activities in water and sanitation have remained steady at around 10% over the past three years as can be seen from the table below.

[14] The rating system is put together by WASTE and expresses both the scale of the MFI/NGOs operating in microfinance for WATSAN and the length of time for which they have had experience in this sector: Tier 1 institutions are those with the most experience and highest capacity for coverage, Tier 4 is the lowest.

BWDC's activities : (Percentage of fund deployment)

	2008	2009	2010
Agriculture: (for land improvement, for creation of irrigational facilities, purchase of farm implements & for crop cultivation)	19.45	16.67	18.50
Livestock: Purchase of milk-producing animals & cultivation of fodder	50.21	49.59	48.26
Micro Enterprises : (To meet the working capital and infrastructure requirements)	19.57	24.48	23.58
Water & Sanitation : (To construct and repair water and sanitation facility at home)	10.77	9.26	9.66

The scale of their sanitation micro-lending operations extends to two out of their three districts of operation (Thiruvarur and Nagapattinam) and over 60 Panchayats. According to their website, they have identified 20,000 families as potential targets for sanitation microloans[15]. According to information available as of June 2011, they had covered the needs of 9,000 families.

Loan product. According to their website, the total quantum of loans extended for sanitation has been 46.4 million Rupees (1,010,200 USD) of which 22 million Rupees (482,000 USD) have been recovered so far. These loans have been extended via over 387 SHGs.

The features of the loan product are as follows:

- *Average sanitation loan amount .*The size of the loan amount was different depending on the product constructed.
  - The single leach pit loan = 8,500 INR over one year (186 USD) Single leach pit + bathroom =10,000 INR (219 USD)
  - Septic tank + network connection = 6,000 INR deposit + 2000 INR for connection (130 USD + 43USD)
  - Septic tank + toilet + bathroom =350 000 INR (7,665 USD)

During the field visit, loan recipients commented that 8,000 INR (175USD) was not sufficient to build a toilet as it would cost more like INR 15,000. Loan recipients said they usually raise the difference from their own finances.

- *Interest rate and other charges (Loan processing fee, loan loss insurance etc.)* Currently set at 22% per annum (was 18% till FY 2009) on a reducing balance basis + 1% processing fee[16]. BWDC collects 10% of loan amount as loan security fund (LSF).
- *Loan term:* 15 to 16 months
- *Collateral:* BWDC has adopted the group-lending model i.e. Self Help Group (SHG) approach wherein 12 to 20 members come together to form a group as well as the Joint Liability Group (JLG) model of 5 members in a group.
- *Grace period :* none
- *Time taken to approve and disburse the loan, then construct the toilet* Under normal practice, loans are disbursed within 2 days of sanctioning. However SMERA observed that the loan had been disbursed 2 months after it was

[15] http://www.bharathiwomen.org/development.html#aids
[16] The Royal Bank of India (RBI) had previously imposed a 24% guidance cap on how much interest MFIs should charge but RBI has now raised this to 26%

sanctioned. We were informed by the staff that the process of sanctioning the loan takes one month and the process of constructing the toilet takes one more month.

SMERA observed from their field visits that borrowers would take two loans at a time from BWDC – one for income generating activity and another for construction or maintenance of water and sanitation.

The types of toilets which we observed were twin leech pit latrines. We were informed that septic tanks and single pit latrines have also been constructed with the BWDC loans.

Loan eligibility criteria

- Income of the recipient is below 5000 INR[17] (USD 110 USD) per month
- Recipients should not have more than 50,000 INR (1100 USD) of outstanding debt
- Their source of income, earlier credit track and holding pattern
- Their repayment capacity – this is not decided just by income
- They should have sufficient land for toilet construction
- They must own the land
- They must be married women aged 18 and over
- They do not fix any lower or upper income level

As of mid-2011, they had never rejected any loan requests.

Repayment rates. Of 10,000 loans, only 17 people defaulted, which means that their Portfolio at Risk (PAR) was 0.17% and their repayment rate very high. BWDC have a policy not to use coercion to induce repayment of the loans. The sanitation loan portfolio has been performing well with low default rates.

3. Evaluating demand for MF sanitation products

BWDC have not conducted any structured market research to identify demand but through the process of awareness-raising, demand is created and followed with the process of creation of the SHG/JLG, visit by the loan officer and finally the authorisation of the loan.

4. Measuring the impact of sanitation loans on target population

BWDC target women in rural areas who fit the eligibility criteria outlined for the receipt of their loans. However, they have no systematic means to target particular groups beyond this. The staff reported that sanitation loan products were easier to sell than micro-insurance products which they were having great success with. However, they indicated that a lack of funds to provide the loans limited the growth of the “toilet loan” market.

5. Evaluating donor/government support

The financing received from the FINISH programme to support BWDC’s sanitation activities is in the form of a grant. If they did not have the funding from the FINISH programme, they estimated that they would not be able to conduct their activities in microfinance for sanitation. Therefore the role of FINISH (in turn funded by DGIS) was crucial to initially develop BWDC’s sanitation activities. At the time of writing they were planning to become financially sustainable and setting up an NBFC.

6. Overall assessment of your experience with sanitation

The assessment by the CEO of his experiences in microfinance for sanitation was positive. He commented that whilst he could not speak for the whole of India, his own experiences were good, with sanitation loans showing returns for BWDC and no problems with loan recovery rates. There was scope for expanded activities. The expressed intention of BWDC to become an NBFC are indicative that they intend to continue their microfinance activities and expand them, but their desire to keep microfinance for sanitation under the trust activities indicates that they intend to keep it as primarily a non-commercial activity of the trust.

[17] A loan of above 50,000 INR is not considered microfinance by the Indian government. This is the only legislation that exists today concerning MF.

Annex C:
Other financial institutions – summary information

Name of financial institution	Grameen Koota
Name of contact and contact details	Arun Kumar B Bangalore, e-mail: arunkumar.b@gfspl.in
Activities in water and sanitation	MFI extending loans for water and sanitation. Has received support from Water.org.
Website	www.gfspl.in/Grameen_Koota.html

1. Main characteristics of financial institution

Grameen Koota (GK), a division of Grameen Financial Services, began in May 1999 as a project under the T. Muniswamappa Trust. Working on an adaptation of the Grameen Bank lending methodology, Grameen Koota offers collateral-free loans to women from poor and low-income households. These loans help build livelihoods, raise the standard of living and consequently help beneficiaries break themselves and their families out of poverty. Grameen Koota (GK) is registered as a Non-Bank Finance Company and thus regulated by the Reserve Bank of India (RBI) which is the Central Bank of the country.

For their water and sanitation programme, they operate under a tripartite arrangement between Grameen Koota, Navya Disha and Water.org. Navya Disha, a non-profit organisation, organises social awareness programmes and does community mobilisation under a water and sanitation programme. Water Aid gives grant support for technical and administration support to the programme. There are 36 employees in Navya Disha who are dedicated to the water and sanitation programme. Navya Disha also helps in identifying the beneficiaries and recommending their names to Grameen Koota for credit support. Grameen Koota gives financial services to these BPL (Below Poverty Line) families in the form of loans at concessional terms.

The total employee strength of Grameen Koota is approximately 1700.

2. Activities in the sanitation sector

GK started off with its sanitation activities in August 2009. The initial focus was on creating social awareness programme as it was felt that demand for sanitation can only be generated through awareness programmes. Financial assistance in the form of loans started in February 2010 with support from Water.org. GK gives loans both for water connections and toilet construction.

Its water and sanitation programme is operational in 20 branches out of a total of around 160 branches and its geographical spread is in 20 Taluks (an administrative area which is at sub-district level) of 6 districts in the State of Karnataka. GK has been operating its water and sanitation programme in six districts of Karnataka i.e. Hasan, Tumkur, Mandya, Ramanagara, Chitradurga and Chikamagalur.

GK offers purely a loan product to clients for sanitation (or water) investments. In addition, Navya Disha gives a grant support of up to Rs. 10,000 to the end beneficiary in case s/he constructs an eco sanitation toilet, to cover the cost differential between a standard toilet and an Ecosan toilet. At present, the number of existing borrowers for water loans is 4,100 and sanitation (Toilet construction) loan is 5,050.

Features of the sanitation loan products that GK offers:

- Average loan amount for Toilet – Rs. 10,000
- Average Loan amount for Water Connection – Rs. 5,000
- Interest rate and other charges - 20% reducing interest rate (paid fortnightly)
- Loan processing fee – 1%
- Loan loss insurance: for Rs. 10,000 – Insurance premium is Rs. 80, For Rs. 5,000 – Insurance premium is Rs. 40.
- Loan term – 2 years
- Collateral if any – No Physical collateral but joint liability (group loans)
- No margin amount from client
- No grace period
- Collection frequency depends upon the client choice
- Average periodic instalment size depends upon the collection frequency

For water and sanitation loan, interest rate is charged at the rate of 20% reducing balance while that for other loans it is 24 % reducing balance. The water and Sanitation Loan term is for two years while for other loans, the loan term is 1 year. The LPF is 1% for all kinds of loans. The loan term is longer since it is considered a non-income generating loan. Customers invest in toilet construction/septic tank under sanitation loan. GK also provides housing loans and construction of sanitation infrastructure is a component of it.

3. Evaluating demand for MF sanitation products

Grameen Koota continuous interaction with clients made it realise the great need for water and sanitation programme in the area for improvement in the life standard of the BPL families. Households do not generally take on a loan from a money lender to build sanitation due to very high interest charges and the fact that sanitation is not a top priority.

Before initiating the loan programme, Grameen Koota conducted a market research (funded by Water.org) in 5 districts of Karnataka; this was conducted by an external market research agency. The estimated demand was for 45,000 toilets. Based on the understanding of the demand and gap analysis, the sanitation product was launched in the market.

Grameen Koota sees the programme as a need for social uplift of the low income people and not as a commercial profit programme. It believes there is a big need to promote water and sanitation programme among clients to generate demand for the loans. The awareness and the education of the clients on sanitation issues vary across different geographies and so the demand for the product also varies. In some places, more social awareness campaigns are required in comparison to other areas to make people realise the need of toilet infrastructure and usage. It is also due to local culture and tradition of the place. For example in North Karnataka, the social awareness campaign was carried out three times while in South Karnataka only once for people to realise the importance of toilet. Navya Disha carries out these social awareness campaigns, by showing films on water and sanitation and organising communities.

4. Measuring the impact of sanitation loans on target population

Grameen Koota targets women of BPL family. It operates in urban, semi-urban and rural areas. It does not target any particular community and works both for slum and non-slum dwellers.

Financial eligibility and creditworthiness of potential beneficiaries is checked based on cash flow statements, prepared by Grameen Koota field staff. Loans from other organisations are taken into consideration while making cash flow statements. This is done by oral check with the potential beneficiary but it is impossible to cross-check the information provided by the beneficiary due to the absence of a centralised credit bureau. Grameen Koota conducted a post implementation study to understand the impact of the

Sanitation programme. Major improvements included improvement in social status, more free time to beneficiary and family for income earning, improvement in health and hygiene.

Loan repayment rates of water and sanitation loans have been extremely good at 100%. Clients also see Grameen Koota as a “Toilet building organisation” which differentiates them from other MFIs in the region as none of the others run similar programmes in Karnataka.

5. Evaluating donor/government support

Water.org has provided grant for administration and technical support to the water and sanitation programme. These funds are utilised for social awareness programmes amongst the target population. They also cover the technical assistance to end beneficiary in terms of toilet construction based on the conditions and space available in the house.

Grameen Koota has received loan support from FWWB and other funding organisations to make access to water and sanitation loans available to BPL family. Grameen Koota believes that grant support is required from funding organisations for social awareness and capacity building and concessional funds are required to provide water and sanitation loan to end beneficiary for the success of the programme. The technical support costs if passed on to the end-beneficiary will make the loan unaffordable.

Grameen Koota also helps the borrowers in receiving the benefits of government sanitation programme available in the area. Households falling under the Below Poverty Line (BPL) criteria of the government receive an incentive of INR. 3,000 for toilet infrastructure from the government under Total Sanitation Campaign Scheme. Out of 5,050 Toilet loan borrowers, 2,700 borrowers have received the government incentive (as they qualified for it, although others may actually be below the poverty line but not be eligible for the subsidy).

According to Grameen Koota, accessing public finance is a big challenge for financial institutions. Research agencies have a great role to play in focussing upon the issue and funding agency needs to finance the implementing financial institutions in form of grant and loan. The grants are required as there is a soft component of creating awareness and providing technical support for construction.

6. Overall assessment of your experience with sanitation

Grameen Koota’s experience with sanitation loans has been very positive. The Senior Management team is convinced about the viability of the programme outcome and its social impact. It wants to continue with the water and sanitation programme in future and has a vision to reach to 300,000 families by year 2015 under this programme. To realise this vision Grameen Koota requires a fund of IND 3bn (USD 66 million).

Grameen Koota sees the water and sanitation issue as not just a commercial activity but a social and serious development issue also. The initiative is considered as a non-profit initiative of the organisation to reach low income people. It understands rural areas and urban slums have the highest demand provided social awareness is done in the area. It does not target any community in particular. Only few MFIs are giving loans for sanitation as of now. A workshop was conducted by FWWB for its partners on “Implementation of Water and Sanitation loans for clients”. It was evident in the workshop that MFIs were not aware of the water and sanitation programme and its social impact. Another reason is the high operational cost involved with the programme, because the programme requires financial institutions to do social awareness, technical supervision, loan utilisation check, identification of beneficiary, monitoring visits etc. for the success of the programme. Recent backlash against microfinance has affected the fund flow to MFIs in recent times in the market for general microfinance. For sanitation, the availability of public finance was scarce even before the crisis and it is the same even now. Grameen Koota is changing its loan product features based on the new guidelines of the Reserve Bank of India (RBI).

Name of financial institution	BASIX
Name of contact and contact details	Rama Kandarpa ramak@basixindia.com
Activities in water and sanitation	MFI offering loans for water and sanitation, received support from Water.org
Website	www.basixindia.com

1. Main characteristics of financial institution

Bharatiya Samrudhi Finance Limited (BSFL) is an NBFC created in 1996. BSFL is the first NBFC MFI in the country. The major statistical numbers of the organisation are as follows:

- Number of staff: 8,954
- Number of borrowers: 1,435,476
- Overall size of loan portfolio: Rs 11,173,302,042 (approximately USD 248 million).

BSFL operates through the joint liability group model. It forms groups of 5 women members and offers credit and other services. BSFL promotes itself as a livelihood support organisation as it offers a wide variety of services like business development services to its clients.

2. Activities in the sanitation sector

BSFL offers water and sanitation loans to all its borrowers in all its operating areas. The loans are to construct toilets and bathrooms. The WATSAN loan is a separate loan product and its features are as follows:

- Average sanitation loan amount: INR 30,000 (USD 670)
- Interest rate – 24% (reducing balance)
- Loan processing fee- 1%
- Insurance – Life insurance
- Loan term - 36 months
- Collection frequency (Weekly/Monthly)- Monthly

The loan terms for the water and sanitation loans are different from other income generating loans. WATSAN loans are considered as non-productive loans and clients therefore need a longer term to repay. The outreach of the sanitation loans offered so far (as of July 2011) was:

- Number of sanitation loan borrowers: 3,919
- Size of sanitation loan portfolio: INR 18,229,194 (USD 405,000) – equivalent to an extremely small percentage of their overall portfolio.

BSFL also provides housing loans but it does not track if any portion of these loans is used for construction of toilets.

3. Evaluating demand for MF sanitation products

BSFL has a huge database of its existing clients who had taken a loan/loans in the past. Many of these people do not have sanitation facilities in their houses and are approached for a WATSAN loan. BSFL does not conduct any separate market research to identify its clients but it uses its existing knowledge of its clients to offer this product.

4. Measuring the impact of sanitation loans on target population

BSFL did an impact analysis for water and sanitation pilot programme. The programme had the desired impact of improving the lives of the villagers by achieving better health and sanitation. The average expenditure on medicines had seen significant declines, the incidence of disease like malaria, dysentery and diarrhoea had fallen and in general, the welfare and confidence of the clients had increased. BSFL works with both poor and non-poor clients. It has a mix of both male and female clients and it operates in both urban and rural areas.

BSFL does a cash flow analysis of all its clients to decide on the loan amount. As mentioned it works with both the poor and non-poor clients. Loan appraisal is also done to ensure there is no multiple borrowing among clients.
5. Evaluating donor/government support
External support has mostly been provided by Water.org. Water.org lent BASIX $242,000 at interest in 2007, and it was successfully repaid at maturity. This marked a significant milestone both for Water.org and for BASIX vis-à-vis the WaterCredit model.
6. Overall assessment of your experience with sanitation
The WatSan programme in its pilot phase has been successful in providing sanitation to many households. However, there are factors identified that have inhibited its effectiveness and the ability to scale it up. One of the main challenges was that the households were not exactly sure about the total expenditure incurred for the construction of the toilet cum bathroom. Lack of water supply in the toilet and bathroom is a factor that inhibits the demand for WATSAN loans. BSFL feels there is a good demand for the water and sanitation loan in the semi-urban areas. The WatSan loan needs to be provided along with technical guidance for low cost high quality structures in limiting cost of construction. Awareness programmes are essential to convince the customers to build the exact model specified by the MFI.

Name of financial institution	ESAF Microfinance & Investments (P) Ltd.
Name of contact and contact details	George K John (Bobby) (General Manager, EMFIL – Nagpur) Cell: 09325938383 / 09423104569 e-mail id: zonalhdci@emfil.org
Activities in water and sanitation	MFI providing loans for water and sanitation with some external funding provided by Water.org.
Website	www.emfil.org

1. Main characteristics of financial institution

ESAF is an MFI and registered under NBFC guided by Reserve Bank of India regulations. ESAF channels financial support to the ultimate beneficiaries by providing loans to Self Help Group members. ESAF geographical areas of operation include rural, semi-urban and urban areas.

The total number of staff in ESAF is 1,600. The number of existing borrowers is 400,000 and overall size of loan portfolio is INR 1,980,000,000 (USD 44 million, using USD 1 = INR 45).

2. Activities in the sanitation sector

ESAF provides microfinance products that help households to invest in their individual water and sanitation infrastructure. With a water loan, members can take a water connection from gram panchayat or municipality. It provides sanitation microfinance loan to SHG members in districts of Madhya Pradesh, districts of Chattisgarh and districts of Maharashtra.

Only the existing SHG members can demand a loan from the organisation. So, one must be a member of SHG to avail any kind of loan. SHG members can demand their first loan as water or sanitation loan.

The total number of water and sanitation loan borrowers is 7,400. The average size of water loan is Rs. 5,000 while that of sanitation loan is Rs. 12,000. The total size of the water and sanitation portfolio was unknown but is unlikely to be much above INR 63 million (USD 1.4 million, which is approximately 3% of their total loan portfolio).

Features of the sanitation loan products that ESAF offers:

- Average loan amount for Sanitation – Rs. 12,000
- Average loan amount for Water – Rs. 5,000
- Interest rate – 26% diminishing (The principal amount paid during every instalment is subtracted from the total principal amount. Interest would be charged on the principal balance amount.)
- Loan processing fee – Nil
- Loan loss insurance - Nil
- Loan term: 1 year (For loans less than or equal to Rs. 6,000), 2 years (For loans more than Rs. 6,000)
- Collateral – No physical collateral
- Any margin amount from client - Nil
- Grace period – Loans are disbursed to the members in instalments. Members have the grace period till all loan instalments are disbursed to her
- Collection frequency (Weekly/Monthly) - Weekly
- Average periodic instalment size – For a loan of Rs. 12,000 with a loan term of 2 years the weekly instalment size is Rs. 135 (USD 3).

Members use water loan to take water connection from municipality or gram panchayat. Sometimes they also make a water tank to store water. The loan amount is decided by the technical experts based on the length of water pipes required to take the water connection. With a sanitation loan, members build individual toilet infrastructure. They also need to construct septic tank in case the sewerage system is not present in their area. The cost of constructing toilet infrastructure without Septic tank comes out to be Rs. 10,000 to Rs. 12,000 and including septic tank is Rs.20, 000. ESAF provides housing loan only in the state of Kerala and a portion of such loan is also used by members to build sanitation facilities. Technical supervisor ensure the construction of sanitation infrastructure in house of the beneficiary.
3. Evaluating demand for MF sanitation products
They conducted an informal survey to understand the demand for water and sanitation facilities. It was followed by the Research and Development department of ESAF that conducted a base line survey to get a clear picture of socio economic status and market potential of the area. Then they developed specific water and sanitation loan products to cater to the demands of people. According to them, there is a lot of untapped demand for sanitation microfinance products and it can be created by doing social awareness on health and hygiene amongst the target segment. After social awareness programme in the area, loan applications are being invited. Loan is being disbursed with- in 15 - 30 days of filling the loan application. People's perceptions have been changing fast on the subject of health and hygiene. And, they are becoming more conscious day by day. There has been sanitation demand from people.
4. Measuring the impact of sanitation loans on target population
ESAF targets poor women. It operates in urban and rural areas. It does not target any particular community and works both for slum and non-slum dwellers. Households' potential ability to repay the loan is measured by checking the sources of income. The income of the applicant and spouse and other sources is taken into consideration to calculate house-hold income. Past credit behaviour of member is also checked to check her creditworthiness in case she has taken loan in the past from other organisations. Moreover, the Self Help Group takes the group guarantee for the loan taken by the member. The group is responsible in case the member does not pay the loan. The performance of the loan portfolio in the sanitation sector is very good. The repayment rate is approximately 99.20%. On a regular interval, reports on sanitation related portfolio are also being prepared. The engineer visits the client house three times to check the toilet construction. The first visit is to assess the loan requirement for construction of toilet infrastructure and making a technical report which is submitted to the respective Branch. The second visit is made during the construction of toilet to give advice on technical aspects if required and the third visit is done after completion of construction. Strong monitoring and supervision are carried out to ensure that people use the loan for the purpose they have taken. The Development Executive does the monitoring to find out the status of toilet construction. S/he makes a "Sanitation Follow up report" and sends the same to Head Office. The Development Executive (NGO) reports to the Programme Officer (NGO). The Programme Officer holds monthly meeting of Development Executives every month to assess their sanitation programme targets and past performance.

ESAF has sought to measure the impact of sanitation programme on the households that have subscribed to sanitation microfinance product by an external agency. The external agency made field visits and used PRA tools to understand the impact. They also did in-depth individual interview of some of the members, branch managers and development executive. They found that the major challenge is that the organisation needs to do social awareness programmes on health and hygiene to create demand for sanitation infrastructure.
5. Evaluating donor/government support
ESAF has not received any financial support from government to support MF activities in the sanitation sector. But, it believes in working with the local bodies and Gram Panchayat. For example, it helps Gram Panchayat in getting water related infrastructure and support from water department of government. On the other hand, it has received external funding from Water.org, as it has been a WaterCredit partner since 2008. Water.org has financed activities such as a demand survey and product development and provided technical assistance. They identified ESAF as one of their most innovative partners.
6. Overall assessment of your experience with sanitation
ESAF experience with MF for sanitation has been very positive. They believe that sanitation programme should be looked at from a social perspective and not as a pure commercial loan. Though the average loan size under the water and sanitation programme is small, the potential impact on living conditions of the beneficiary is very huge. It has helped them improve the social image and status of their family, to free up time of family members including children. It has also yielded improvements in health (though it has not been evaluated yet) and increases in income because of devoting more time in business. Children are the major drivers as they put pressure to build toilets in the house. There is a market with substantial potential for development provided social awareness is done in the area. It requires a multi-level partnership for success of the sanitation programme. ESAF feels that a combination of an NGO and an MFI is required. The NGO does the community mobilisation and social awareness (supported by grant funds) which will trigger demand. MFI provides the loan to cater to this demand. There should be some institutional arrangement so that members get the proper building material at a subsidised cost. Government should give financial support to NGOs for doing social awareness programmes. Only few MFIs in India are offering MF products for sanitation because the MFIs need to have a social vision to offer sanitation loan products to their clients. Due to the recent backlash against microfinance, funds have slowed down and not coming on time. This has affected the overall microfinance operations of the organisation

Name of financial institution	**Friends of Women's World Banking - India (FWWB)**
Name of contact and contact details	Sireesha Patnaik Email: sireesha.patnaik@fwwbindia.org
Activities in water and sanitation	Umbrella organisation providing support to MFIs providing loans for water and sanitation
Website	www.fwwbindia.org

1. Main characteristics of financial institution

FWWB was established in 1982 by SEWA Bank. It is an Apex Organisation and a regulated entity. At present, there are 17 staff in FWWB I. They have reached approximately 2000 clients under the water and sanitation programme. They have partnered with 30-50 organizations.

FWWB-I channels financial support to the end beneficiaries through partner organisations through: (a) Credit for solar equipment and water & sanitation loans (b) Livelihood support (c) institutional Capacity Building of Microfinance Institutions - strengthening Microfinance Organisations through its various programs on providing technical assistance, training, loan and grant support etc.

The microfinance activity of FWWB was shifted to another entity in 2010. This was done to increase the outreach of the organisation. The new organisation is registered as a Non-Bank Finance Company (NBFC) named as Ananya Finance for Inclusive Growth (AFIG) and supports microfinance institutions for their capacity building and financial assistance. FWWB works in the areas of women's empowerment, need based financial products (energy and water and sanitation) and livelihood services.

The support to MFIs for water and sanitation comes under the purview of FWWB The microfinance support FWWB reaches to the end customers in rural, semi-urban and urban areas through partner organisations.

2. Activities in the sanitation sector

FWWB gives grant and loan support to socially oriented MFIs for sanitation. FWWB has supported six MFIs across the country in states of Orissa, Maharashtra, Madhya Pradesh, and Karnataka. ESAF, Mahashakti, Adhikar, Sambhav are the major MFIs supported for water and sanitation. FWWB selects MFIs that are socially oriented.

Appraisal visits and commitment of MFI to meet the social objectives is looked into before selecting the organisation. FWWB launched the Water and Sanitation 'WATSAN' Program in year 2009 with an objective to improve the overall quality of life of women by facilitating access to Water and Sanitation through credit services and awareness creation on hygiene and sanitation through its Partners.[18]

The sanitation portfolio is Rs. 16,000,000 (USD 355,000). It has also given a grant of Rs1,200,000 (USD 27,000) to its partner organisations. The WATSAN loans given are at lower interest rate as compared to commercial rate. FWWB does not issue any guidelines to MFI but advocates for loans to be made at concessional terms to clients. In addition, FWWB asks its partners to adhere to RBI guidelines. Under sanitation loans, clients make investments in toilet construction and also make septic tank in case sewage line is not available in the area. Water loans are utilised by clients to take water connection from the municipalities in urban areas and Gram Panchayats in rural areas.

[18] http://fwwbindia.org/watsan.html

3. Evaluating demand for MF sanitation products
FWWB experienced through its partner organisations that clients use approximately 10% of the housing loans for toilet construction. This gave them the belief that there is a demand for sanitation infrastructure in the area. FWWB helped its partner organisations in doing pilot survey and understand the client demand in the area. FWWB feels doing pilot surveys to understand the demand is a challenge since client interest or preference changes as per the context. The initial pilot surveys done by the partner organisations shows a good demand for sanitation MF products in urban as well as rural areas. Urban areas are relatively more challenging to work in for water and sanitation due to issues of migration, space available to the family in slum houses and legal status of the slums. By contrast, in rural areas there is sufficient space available to the family to build sanitation infrastructure and adequate legal documents are available with clients.
4. Measuring the impact of sanitation loans on target population
FWWB targets especially women whose household income does not exceed INR 15,000 per month (USD 333). It reaches to urban, semi-urban and rural areas through its partner organisations. It does not target any particular community. It targets those low income people who have creditworthiness to repay the loan. Performance of the loan portfolio in the sanitation sector is very good. Partner MFIs are registering an excellent repayment rate. FWWB is also planning to do the impact study for water and sanitation loan. It wants to do three levels of assessment to understand the impact of the programme. 1) Base line Assessment 2) Midline Assessment 3) End line Assessment.
5. Evaluating donor/government support
FWWB has not received any financial support from government. But, FWWB received funds from the Michael & Susan Dell Foundation as an interest free loan. FWWB disburses this as a loan to its partner organisations on concessional terms. The same loan would be recycled by FWWB for 5 years. FWWB believes that sanitation products should be given at concessional terms to the end beneficiaries. The grant fund could be utilised for conducting training programmes, developing training materials, community mobilisation, social awareness campaign on health and hygiene, monitoring visits to client location, technical support to the programme, identification of right beneficiary etc. Today a number of government schemes have been coming under sanitation programme. But, there is not much grant support available from the government or international organisations. FWWB advocates to its partners to remain aware of state sanitation programmes for the benefits of end beneficiary. Partner organisations support the end beneficiaries in making them aware of the state sanitation programme and eligibility conditions required to get the benefit, filling up the forms, completing the required documents etc. There is not enough public financing available in order to encourage financial institutions to provide microfinance for sanitation.
6. Overall assessment of your experience with sanitation
FWWB experience with MF for sanitation has been very positive. It believes that there is substantial potential in the market. But social awareness is required to make the target group aware of the importance of health and hygiene and thereby create demand in the market. Many clients realise the need but it is not their priority.

There is demand for microfinance products for water and sanitation in urban as well as rural areas. But only few MFIs in India are offering MF products for sanitation. One of the major reason is that operations cost is high in case of sanitation as compared to other loans. MFIs are required to do a number of other activities for success of the sanitation programme. Social awareness of the target group on health and hygiene, identification of the right beneficiary, regular monitoring of the client, technical supervision by technical experts are some of the reasons for the high operation costs. These activities are in addition to other normal credit activities which increases the operational cost of the programme.

Recent backlash against microfinance in India has also affected FWWB funding activity. It has slowed down funding to its partner organisations.

Name of financial institution	SEWA Bank
Website	www.sewabank.com
1. Main characteristics of financial institution	
SEWA Bank is the bank of SEWA (Self-Employed Women's Association). SEWA Bank is a separate entity from SEWA itself, which is in fact a trade union. It is registered as a cooperative bank in 1974 under the dual control of The Reserve Bank of India and the State Government. Since then, it has been providing banking services to poor, illiterate self-employed women and has become a viable financial venture. SEWA Bank tends to emphasise the savings part of their microfinance model. In 1974 SEWA Bank was established with 4,000 depositors. Today, over 125,000 poor women are depositors. The Banks' total working capital is currently 210 million INR. Mahila Housing SEWA Trust (MHT), a sister organisation, gets involved as a technical agency. It ensures that the women residents of the slums are involved in the decisions made by the Ahmedabad Municipal Corporation, thus building their own capacities. MHT facilitates access to services such as shelter finance, legal advice, technical assistance, information on the housing market, and shelter-related income opportunities for poor working women. Through its advocacy activities, MHT also attempts to influence housing and infrastructure related urban and rural development policies and programs to meet the needs of its membership	
2. Activities in the sanitation sector	
Since 1976 and in response to demand, SEWA started providing housing and infrastructure finance activities, providing both individual and collective loans for various purposes including installation of a private or community source of drinking water, toilets, drainage, electricity etc. As a rule, SEWA provides loans for housing where the house is required to be bought in the name of the women borrower, thereby creating an asset for the woman. Loan amounts vary from Rs. 3,000-3,500. The technical supervision for building the toilets is provided by engineers from Manila Housing SEWA Trust. The repayment rates of the loan are as high as 96% (www.sewa.org/images/pdf/new/product.pdf) p7 *Parivartan Housing Programme.* The "Parivartan" housing program is designed to upgrade the slums in the city. Slums located on municipal land are first identified; then SEWA mobilizes the women slum dwellers to form a residents' association. Every household deposits 2,100 rupees with the municipal corporation, which entitles them to a toilet, a sewage system, water supply, and electricity in their new pucca house. The women may borrow the amount from SEWA Bank if they are unable to pay with savings. The title to the house is issued in the SEWA member's name, and it is entered into the official municipal record. Local SEWA leaders play a significant role in making this happen. Once the project is completed, the neighbourhood tends to acquire a more respectable name – such and such colony or so and so Nagar. However, working in collaboration with outside agencies, especially a government of any sort is not without problems. *'Target areas' within India.* SEWA operates in Ahmedabad city as well as a few other districts in the state of Gujarat in India. The loan initiative for infrastructure upgrading is provided to Panna Lal ki Chali in Saraspur area of Ahmedabad (slum). There are many instances throughout Ahmedabad, where the poor have begun to pay voluntarily to install drinking water and/or sanitation facilities. SEWA Bank has actively facilitated this process by disbursing loans to individual women, who wish to upgrade their existing infrastructure facilities. Of the 151 families that live in this area, 75 per cent have built their own toilets with help from Mahila Housing SEWA Trust and SEWA Bank. As Panna Lal ki Chali is	

connected with the main city sewer line, all of the toilets that have been built here are hooked to the city grid and are the pour-flush model.

Financial instruments employed. Loans in the model used in Panna Lai ki Chali. But as an MFI they provide a range of other services including savings and insurance. They work in urban and rural areas. There is an emphasis on self-help groups particularly in rural areas.

According to (Mehta, 2008), they have provided individual loans to their members with a 17% per annum interest rates and tenor from 12 months to three years and a maximum size of USD 650. Two guarantors serve as collateral and adequate savings performance is a precondition. Bank's regular loans to members are tracked for end use. About 50% are classified as "building" and "building repairs" and of these, 60% are estimated to be used for water connection, bathroom or toilet. Over the past five years, there were total 7000 water and sanitation loans of about USD 4.1 million, which accounted for about 15% of total loan portfolio and nearly 12% of total borrowers. SEWA Bank's sister organization the Mahila Housing Trust (MHT) is currently doing a more detailed end use tracking of SEWA Bank's loans.

3. Measuring the impact of sanitation loans on target population

SEWA Bank account holders are made up of approximately 70% urban and 30% rural self-employed women. It is estimated that 40% of SEWA Bank's overall housing/shelter related loans are for infrastructure upgrading. This means that approximately 15% of total loans disbursed by SEWA Bank are for infrastructure-related needs.

4. Evaluating donor/government support

The origins of SEWA Bank's Credit Fund has evolved over time, as follows:

- 1974-1997: savings from own depositors;
- 1998: Additional funds of Rs 28.8 million from HUDCO, a mainstream Indian housing bank, for longer term housing and infrastructure loans (sanctioned but yet to be fully released);
- 1999: Additional refinance of Rs 27 million from HDFC, a commercial bank, for longer term housing and infrastructure loans (sanctioned but yet to be fully released).

SEWA Bank acts as a financial intermediary and provides a loan of up to Rs 1,600 to each family, if they require it, in order to meet their cash contribution. Currently, SEWA Bank has an average loan repayment rate of 94 percent. SEWA Bank charges its clients 17 percent interest per annum on loans from its own depositors' credit fund, and 13 percent interest per annum on loans accessed from mainstream housing finance institutions such as HUDCO and HDFC (the interest rate on loans from HUDCO to SEWA Bank is 9% whereas it is 10% on loans from HDFC to SEWA Bank).

The domestic government has played an important supporting role for the programme. The Ahmedabad Municipal Corporation provides the connection of each of these services up to the city mains and pays the full cost of off-site infrastructure connections. In addition, the Corporation has also provided written land tenure security for a period of 10 years to all the slum participants of Parivartan. In addition, SEWA has been a WaterCredit partner since 2011.

5. Overall assessment of your experience with sanitation

The municipality is quick in collecting funds, but slow to start the building process. Meanwhile, the women are impatient – they are paying interest on a loan that has yet to see any results. They feel frustrated and turn to the Bank for help, even though the Bank has no control over the government and other power structures. The overlap in the roles of SEWA and SEWA Bank also causes some confusion at times. By intervening on behalf of the women in dealing with the government, the municipality, or with insurance companies, the Bank often bears the brunt of the women's frustration.

When, for example, an insurance company makes a low assessment of the damage to a riot victim's house, she is devastated. While the insurance company takes a limited view of what constitutes damage and how it occurred, for the woman, the loss continues to haunt her for years after the incident. Rebuilding a life, regaining trust, and recovering one's livelihood against overwhelming odds is a daunting task; while the Bank can play a crucial supportive role in recovery, it can by no means solve all problems. The client's needs are greater than what an economic entity like a bank can provide. Yet the women see the Bank as “our bank,” a provider, a sort of “mother” that provides shelter, is caring, understanding, forgiving, trusting, and “all-powerful.” While admittedly SEWA Bank has tried to “mother” its clients, it is not its mission. Its mission is to empower the women themselves. For a formal financial body, serving clients who have grown in the traditional, non-formal culture of unwritten mutual trust, this can be a challenge.

Annex D:
Donor-led programmes supporting sanitation microfinance

Name of supporting institution	FINISH
Name of contacts and contact details	Sadanand Bhave, sadanand8bhave@finishsociety.com Valentin Post, vpost@waste.nl Vijay Athreye, vijayathreye@gmail.com
Activities in water and sanitation	Umbrella support organisation to MFIs providing microfinance for sanitation
Website	www.finishsociety.com/

1. Main characteristics of the institution

FINISH (Financial Inclusion Improves Sanitation and Health) was set up as a 5-year programme in 2008. FINISH operates as a partnership of international donors, APEX banks and NGO/MFIs. The FINISH society, set up subsequently as a charitable trust, is an emanation of that programme.

The main objective of FINISH is to expand sanitation infrastructure to rural India to cover 1 million households by 2013. They intend to do this not just through the building of toilets, but promoting an overall 'sanitation system' that takes a holistic look at the process, with a strong emphasis on hygiene promotion and awareness-raising, through to safe excreta treatment and disposal. For example, they promote solutions that do not involve the contamination of underground water or putting the health of the individual at a detriment.

Origins of the programme. At the end of 2007, SNS-REAAL (a Dutch Bank) was negotiating with BISWA (Bharat Integrated Social Welfare Agency, Sambalpur Orissa), an Indian NGO and MFI the conditions of a USD 2 million loan to support BISWA sanitation activities. The two organisations that facilitated the negotiations (TATA-AIG and WASTE) saw it as an opportunity for integrating sanitation, micro finance and micro health insurance. TATA-AIG is an insurance company and WASTE is a Dutch NGO with expert knowledge and consulting experience in sanitation. Integrating micro-finance and micro health insurance was something over which a common understanding was easy to reach. There was also a need to link financial inclusion with sanitation and health, which was rather difficult in the absence of authentic academic or scientific data to back this concept. The United Nations University (UNU)/MERIT saw the opportunity to scientifically identify the possible correlation between financial inclusion, health and sanitation and became a partner as well.

The 5 parties (TATA-AIG, UNU/MERIT, SNS-REAAL, BISWA and WASTE) prepared the basic concept for the programme with the ambitious goal of providing 1 million sanitation systems (i.e. basically latrines) in 5 years in India. On 18 March 2008, the Programme Partners signed an agreement to develop the partnership further. The concept caught the eye of the Partners for Water (a Dutch platform supporting commercial and non-profit organisations that work together to realise their international objectives in the field of water) who supported the initiative through a development grant in May 2008. During the latter part of 2008, meetings were held in India and the Netherlands on the details, implementation partners, application criteria, insurance scheme, the financial engineering, monitoring and impact evaluation mechanisms and the cooperation structure, culminating in a programme document.

DGIS (Department of International Cooperation, Government of Netherlands) recognized the high potential of the partnership and its highly innovative character and provided useful suggestions, such as involving the Indian government. To the programme partners, it was not immediately obvious who would be the most logical choice. State governments would be difficult as, from a risk mitigation point of view; FINISH was going to be implemented in different areas and states. Following high-level discussions with all relevant organisations and a consultant, a focus on Development Finance Institutions, often nicknamed “State Banks”, was decided upon.

Among the various Banks approached, the National Housing Bank (NHB) was very responsive. A MoU between NH Bank and WASTE was signed in early 2009. Further, a draft MoU was agreed upon with the National Bank for Agriculture and Rural Development (NABARD) too. Reportedly the necessary government clearances have been obtained by NABARD recently and the MoU is likely to be signed shortly.

How does the programme work? FINISH works through implementing partners (i.e. NGOs or MFIs) who are based in seven states around India. The selection criteria for NGO/MFIs who would receive FINISH funds are as follows:

- The NGO/MFI needs to have prior experience in microfinance;
- The NGO/MFI is willing to commit 10% of its microfinance portfolio for work in sanitation;
- The NGO/MFI needs to have previous experience in sanitation;
- The NGO/MFI has a microfinance rating as provided by one of the various agencies;
- The NGO/MFI has annual reports dating back three years and is willing to sign a memorandum of understanding with FINISH.

FINISH has various MFI partners in different states as listed in the Table below.

Table – List of FINISH partners by State and number of sanitation loans (as of July 2011)

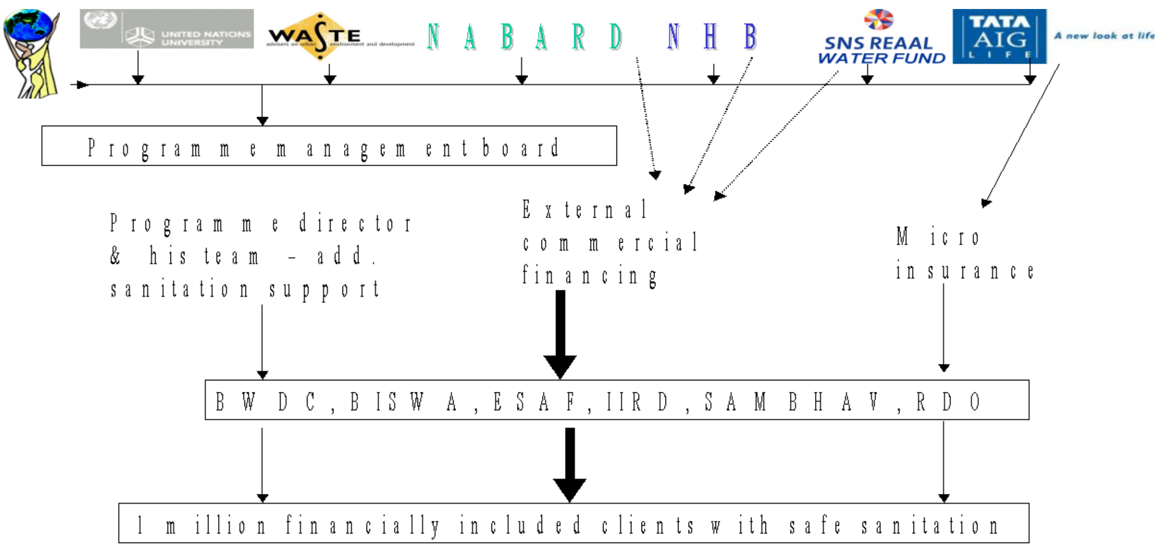
State in India	**Partner Organization**	**Recorded number of sanitation loans (July 2011)**
Tamil Nadu	BWDC, RDO Trust	9,000 (BWDC), 700 (RDO Trust)
Orissa	BISWA (Bharat Integrated Social Welfare Agency)	Operates in 30 districts 115,000 in the last two years
Nagpur	ESAF, Nageshwara Charitable Trust	3,600 in total, across the two states
New Delhi	ESAF	
Rajsthan	IIRD (Indian Institute for Rural Development)	552
Madya Pradesh	SAMBHAV Social Service Organization	1710
Gujarat	Setu Seva Trust	n/a
Total number of loans disbursed & toilets built		**132,000**

These partners include a wide range of organisations. These organisations mainly operate in rural areas because this is where sanitation coverage is lowest (in some rural areas, it is as low as 5% although average coverage is around 25%). However, SAMBHAV also operates in urban areas.

The components of the programme are as follows:

- Improving financial literacy;
- Providing microcredit for toilet loans via partner organizations;
- Providing micro insurance. This is currently active for life insurance (whereby discounts on insurance premiums are given to those who have toilets) but not yet for health insurance;
- Providing small grants for innovative sanitation initiatives at SME level;
- Promotion of hygiene, awareness raising on sanitation issues including safe excreta treatment and disposal;
- Provision of technical support in the form of training to animators and training of masons from experts they are connected to.

Figure 1 FINISH's institutional set-up



2. Activities in the sanitation sector

Once they have selected their implementing partners, FINISH provides them with small grants and technological support for awareness-raising. For awareness-raising, they have included some aspects of CLTS and have also made their own media to promote sanitation (viewable here). They are in the process of making a new video for the promotion of the two pit latrine. Their strategy is to reach 100% sanitation coverage in a few villages before moving to the next ones.

Incentive payments to improve sanitation coverage. Reaching total sanitation in a village can be a difficult task because coverage can for example reach 95% but then struggle to reach the last 5%. In order to reach the target, FINISH has adopted a strategy of granting incentive payments to MFIs for their staff, as those play the joint roles of animators and loan officers. FINISH provides these staff with incentive payments to improve their performance and focus their attentions on sanitation. Through the MFIs, FINISH channel 600 rupees per month to staff members, which is raised to 1200 rupees per month once their initial target is reached. In addition to this, the organisation are granted 75 Rupees for each toilet built from a loan over the 50% coverage target, which is raised to 150 Rupees when village coverage reaches 70% coverage, and then raised again at 90% coverage. This incentive payment is paid by FINISH to the relevant partner organisation. In some cases, these organisations will chose to share it with their field workers and in others, to add it to the revenue of the organisation as a whole. Currently, 41% of the total FINISH

budget has been earmarked for incentive payments (which can be described as output-based aid). *Features of the sanitation loan product offered by FINISH partners.* From a technical point of view, FINISH is promoting twin leach pit latrines. These are always used unless the water table is high, or a village is soon to be connected to a sewerage network, in which case septic tanks are recommended. Given that FINISH operates with a number of different NGO partners, the terms of the loan products on offer vary according to the capacity of each MFI/NGO. For example, BISWA gives smaller loans of 4000 Rupees over 1 year with a rate of 20% reducing to 10% by the end of the year. By contrast, BWDC gives larger loans of up to 350,000 Rupees for a package of a septic tank latrine and bathroom. One of their other products of a single leech pit and bathroom at 10,000 Rupees, at a rate of 21% declining over 15 or 16 months.
3. Measuring the impact of sanitation loans on target population
FINISH tries to obtain data on the composition of the population of villages targeted in one of two ways so as to measure the impact of sanitation loans on the target population: • Either they will contact the Gran Panchayat (the head of 4-5 hamlets) who will provide data on the composition of the population in the area. About 10% of Gran Panchayats are willing or able to provide such information; • If the local authorities cannot be contacted, FINISH will provide training to partners so that their staff conducts their own village censuses. Animators will go door to door collecting information whilst accumulating information on the local population. FINISH partners get in touch with block officers and link up with local panchayats wherever possible in order to find out about where BPL residents are. However, the FINISH project believes in achieving high sanitation densities and therefore does not have a specific pro-poor focus.
4. Evaluating donor/government support
FINISH is financed only partly from donor grants (about 9% of total funds), whilst the vast majority of funds (90%) are leveraged from commercial banks. The grant portion of the programme, estimated at about 9% of the totals funding was expected from two main interested parties namely, DGIS of the Netherlands and the Bill and Melinda Gates Foundation (BMGF, USA). While the DGIS came through on 1 May 2009, the BMGF grant is under review.
5. Overall assessment of your experience with sanitation
The director of FINISH did express some concern over the current microfinance crisis affecting FINISH activities. They are considering moving towards a model that links SHGs directly to banks. However, as one of the FINISH partners (BWDC) makes clear, there does continue to be demand for microfinance loan products in sanitation.

Name of supporting institution	Michael and Susan Dell Foundation (MSDF)
Name of contact and contact details	Ms. Urvashi Prasad Programme Officer, Microfinance and Health, MSDF Email: Urvashi.Prasad@msdf.org
Activities in water and sanitation	Supporting partner organisations providing microfinance for sanitation with mostly grants (and zero-interest loans)
Website	www.msdf.org

1. Main characteristics of the financial institution

MSDF is a private foundation set up in 1999 by Michael Dell, the founder of Dell corporation, and his wife Susan. It operates in the United States, South Africa and India. MSDF supports organisations in three prime areas: education, child health, and microfinance with a stated mission of "*Transforming the lives of children living in urban poverty through better health and education".* They focus on developing sustainable and scalable models for addressing the issues of child health and education development.

MSDF has a staff of 60 professionals globally with 15 of them in India. MSDF operates through partner organisations like NGOs, MFIs, Societies and Trusts which are involved in the three prime areas mentioned above. MSDF supports these partner organisations through equity investment, grant support and loans.

MSDF's strategy for working in water and sanitation sector is stated in their website: "*Our aim is to effectively combine microfinance and the provision of basic services to improve the health, quality of life, disposable income levels and child literacy rates of urban poor families".*

2. Activities in the sanitation sector

Based on past experience, MSDF believes that best usage of water and sanitation facilities can be ensured if beneficiaries have a sense of ownership of water and sanitation infrastructure. Traditionally, usage of the toilets provided for free by NGOs and Government has been low because of lack of sense of ownership by beneficiaries. Therefore, MSDF does not believe in free grants to end customers for building water and sanitation infrastructure.

Rather, MSDF financial support reaches end beneficiaries in two ways : a) In the form of a loan through microfinance at concessional terms for building water and sanitation infrastructure, such as individual toilet construction, individual water connection, individual sewage line/septic tank (Individual Toilet Construction, Individual Water connection, Individual Sewage line/Septic Tank) (b) Community mobilisation and linking beneficiary to government water and sanitation programmes through partner organisations (e.g. Mahila Housing Sewa Trust) providing information to slum residents, and motivating and mobilizing them.

MSDF provides grant and loan support to MFIs to develop scalable and sustainable models to deliver access to water and sanitation facilities to the poor. Currently, MSDF supports water and sanitation programmes in 7 cities in India including Nagpur, Ahmedabad, Surat, Delhi, Jaipur, Hyderabad and Bangalore. Approximately 17% of MSDF microfinance dollar commitments in India are towards water and sanitation. MSDF supports WATSAN in two ways:

1. Providing grants for awareness building and monitoring support to NGOs;
2. Loan support to FWWB, for on-lending to its partner organisations for WATSAN (in FWWB the split between water and sanitation is approximately 50-50%).

MSDF essentially focuses on urban areas and to some extent on semi urban areas. The reason that MSDF quoted for focusing on urban areas are as follows: 1) High population density in urban areas results in very poor water and sanitation conditions. Slum sanitation conditions are pathetic; 2) The pace of urbanisation has not kept pace with water and sanitation provision; 3) there is less Public/Government support for water and sanitation in urban areas.

Grant support is the major form of support that MSDF provides to its partner organisations in the water and sanitation space. The major grantees are Mahila Housing SEWA Trust and Andhra Pradesh's Mahila Abhivruddhi Society.

Friends of Women's World Banking (FWWB) has received both grant and loan support and is the only organisation which has received a sanitation loan support from MSDF till now. The major characteristic of this sanitation loan component is that it is interest free and the loan term is for 5 years. At the end of five years, FWWB will return the principal loan amount to MSDF without any interest.

MSDF has issued some broad guidelines to FWWB and its partners on how the loan should be utilised. These are as follows:

a. Loans should be disbursed to end customers on concessional terms;
b. The interest rate should be lower and the loan tenure should be typically little longer compared to other loans, since sanitation loans are non-income generating

The loan amounts would vary from one implementing organization to another and may not cover the entire cost of the facility. For a water connection, the average loan amount is INR 5,000. For toilet construction without septic tank, the average loan is INR 10,000 and INR 20,000 if a septic tank is included.

3. Evaluating demand for MF sanitation products

MSDF has not carried out any demand estimation exercise. But the experience of its partners and field interactions with the end-beneficiaries have revealed that: a) the water and sanitation situation in urban areas has deteriorated with time b) Access to finance is a major challenge for low income people in constructing water and sanitation infrastructure.

Keeping this in view, MSDF believes that microcredit can play a major role in providing financial access at concessional terms to the target group. For sanitation, the other major sources of finance are the local money lenders who charge very high interest rates. The level of awareness of people is higher in urban areas than in rural areas, although community mobilisation is very much required to boost the demand in urban areas. For example, people may not know how to get a water connection approval from the city Municipality Corporation or they may not know how to access the various government sanitation schemes. MSDF through its partner organisation does community mobilisation mainly to create social awareness on water and sanitation.

4. Measuring the impact of sanitation loans on target population

As mentioned MSDF focuses on the urban poor, and specifically slum dwellers are a key target group for the Foundation. Partner organisations do a baseline survey to collect basic information on the households in the area e.g. household income, primary occupation, house condition.

Repayment rates of the sanitation microfinance loan programmes have been very good (for example, for ESAF, repayment rate has been closer to 100%).

Conducting impact assessments is an integral part of the water and sanitation programme of MSDF. To partners other than FWWB, MSDF has offered only grant support since they can mobilize credit for families from other sources (microfinance institutions or banks in the case of self-help groups). MSDF does a detailed impact assessment for every partner

(involving a baseline and end-line). In addition, MSDF has started doing annual “customer satisfaction surveys” (for a period of two years after construction of the infrastructure) to assess the functionality of the infrastructure provided under the project and whether the families continue to use it/are satisfied with its functioning. For their programme with FWWB (water and sanitation loan and grant support), three assessments have to be done: 1) Base line Assessment 2) Midline Assessment 3) End line Assessment A detailed impact evaluation was done by an independent research team for a programme conducted by Mahila Housing Sewa Trust (MSDF partner), which included a sanitation component. The results of the impact evaluation were as follows. Over 60% of the families had access to properly functioning water, sewage and toilet connections. The major benefits found were time savings, the ability to go to work on time, safety, convenience (especially for women) and reduction in disputes with neighbours over water-related issues. The respondents also reported that there had been an increase in the levels of awareness about hygienic practices, technical aspects of construction, and the procedure for lodging complaints with the relevant government authorities if the basic services infrastructure does not function properly. The research also showed a reduction of more than 30% in the incidence of water-related diseases including typhoid, jaundice, stomach problems, diarrhoea and cholera in the target communities.
5. Evaluating donor/government support
MSDF does not raise funds from any other international donor or government. Based on the experience sharing with partner organisation, MSDF identified that there is less public finance support in urban areas and there seem to be funding gaps at two levels – a) Lack of adequate loan funds for on-lending to clients b) Lack of adequate grant support for the “softer” costs of community mobilization, government liaison, technical assistance provision etc. This is where they decided to place their emphasis.
6. Overall assessment of your experience with sanitation
MSDF feels their experience with microfinance for sanitation has been very positive. MSDF believes that low income families do not have ready funds available to them. They need microcredit at concessional terms (low interest rate, little longer loan tenure) in the range of INR 10, 000 – 15,000 to meet those infrastructure costs. Microfinance is an efficient and effective approach to make the financial support available to this target group. MSDF believes that sanitation loans are different from income generating loans. An MFI requires other capacities and need to provide more services to clients to make sanitation microfinance programmes successful. It requires technical expertise, community mobilisation, regular monitoring of the client etc. to ensure the right usage of the loans. So, it becomes a higher risk product for a MFI. This is the reason why only MFIs which are capable of providing these support services give loans for sanitation. Moreover, sanitation loans should be provided at concessional terms in the form of lower interest rates or / and longer loan tenures as compared to income generating loans, so that overall the regular instalment amount remains low. Not all MFIs can offer these sanitation loans at concessional terms.

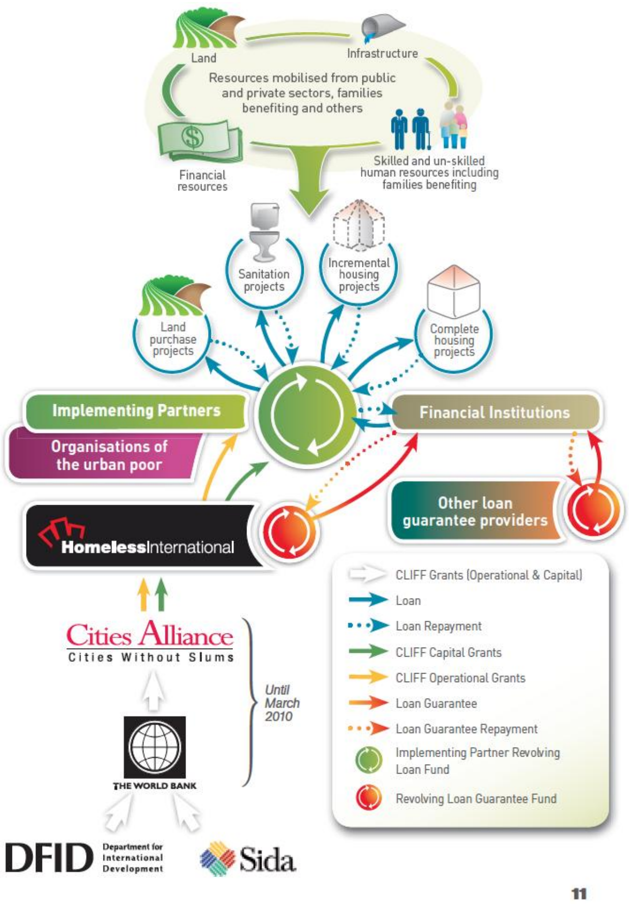
Name of financial institution	Community Led Infrastructure Finance Facility (CLIFF)
Name of contact and contact details	Sarah Stravrakakis, SarahS@homeless-international.org Rémi Kaupp, Remi@homeless-international.org
Website	www.dfid.gov.uk/working-with-dfid/funding-opportunities/countries-and-regions/cliff/ and www.homeless-international.org/cliff

1. Main characteristics of the programme

Background. The Community Led Infrastructure Facility (CLIFF) is a programme started in 2002 by a British based charity called Homeless International with the support of DFID and SIDA. CLIFF is a venture capital facility which enables organisations of the urban poor to access greater public, private and civil society sector resources. These resources are used for sustainable housing and basic services projects for slum dwellers, which have the potential of being scaled-up to benefit even more people. These projects result in improved housing and sanitation for significant numbers of people. In addition, they can be used to influence the policy and practice of banks, governments, international development agencies and others. The programme was initially piloted in India in 2002 and later expanded to Kenya and the Philippines (this write-up is focused on their activities in India).

Channelling financial resources to ultimate beneficiaries. As explained in the diagram below, donors provide financing to CLIFF in the form of grants. These grants are received by Homeless international and channelled into a revolving fund in the form of operational and capital grants.

Figure D1.1: Overview of CLIFF activities



With support from this fund, implementing partners and organizations of the urban poor (such as the Indian Alliance organizations SPARC, Mahila Milan and NDSF) take out loans through local financial institutions – increasingly commercial banks such as the Bank of India or UTI Bank. Often the implementing partner lack the collateral to take out a loan, which is where Homeless International can provide support in the form of the guarantee provision. In sum, CLIFF provides: • The bulk of the funding (75%) is provided as capital grants to enable local partners to provide loans to the projects (these funds are later revolved to finance new projects); • Operational grants to cover the costs of project preparation and management; • Loan guarantees through Homeless International guarantee fund. This financial support is provided to secure infrastructure upgrades in urban and peri-urban slums through the scale up of community-based projects. These projects include sanitation as part of housing upgrade schemes, or can be directed towards sanitation in the form of community sanitation blocks or household sanitation projects.
2. Activities in the sanitation sector
Sanitation is included in CLIFF partners' projects, either directly or indirectly as part of housing upgrade schemes (which always include household sanitation facilities). Between 2002-2010, CLIFF implemented 29 projects, 4 of which had a sanitation component. For example, in India, community sanitation blocks were built in Mumbai, Pune and Tiruppur with CLIFF support. In Nirmal Mumbai Metropolitan Region for example, there have been 7,627 units commissioned in the latest project as of 2010. The blocks are built as the bottom floor of a community centre. The caretaker is given a room rent free to fulfil his duties with the idea that he or she will not want to live above a sanitation block that is poorly maintained. Those sanitation blocks have been financed using a mix of capital grants, funds provided by the municipality and a monthly fee paid by the community. Operation and maintenance of the toilets is paid for by its users. Each family will pay for a pass costing 20 INR per month. This is much cheaper than the 1INR per use charge, the fee that applies to passers-by. For Phase 2 of the Mumbai sewerage disposal project, the projected peak finance at £1,015,815 was all provided by UTI bank but with the aid of a 10% guarantee from Homeless International. Projected total cost recovery for this project was £2,365,835 – the profit from which is recycled into the revolving loan and guarantee funds. In 2007 CLIFF reached a significant milestone in India when the level of finance negotiated from the banking sector by the Indian Alliance exceeded the finance approved from CLIFF for the first time. This direction helped secure future funding for the programme.
3. Measuring the impact of sanitation loans on target population
The target populations are the urban slum dwellers who are living mainly in informal settlements and have come together under community organization brackets. The members of the savings and credit groups are females.
4. Evaluating donor/government support
CLIFF was established with support from DFID and SIDA. During the first phase of the programme (2002-2010), DFID provided about USD 11.2 million and SIDA provided about USD 4.6. million. These grants were used as seed funding for revolving funds and leverage commercial funding. Until March 2010, donor funds were channelled via the World Bank's Cities Alliance. CLIFF estimated that these donor funds leveraged about USD 87 million in commercial funding, which gives a leverage ratio of about 5. From March 2010, funds have been flowing directly from donors to Homeless International. Both DFID and SIDA have raised their contributions for the second phase of CLIFF (2010-2015), to USD24 million and USD6.15 million respectively. During that second phase, CLIFF will expand the range of implementing partners and the number of countries where it works.

Annex E:
Interview guide for microfinance institutions

This interview guide is for Stage 1 of the India research: survey of organisations providing microfinance products for sanitation in India

Guidance about conducting the interviews

Interviews are to be carried out over the phone (or in person wherever possible by combining this with MicroSave's other pieces of work or with the field work in Tamil Nadu). Plan to organise several interviews:

- *First generic interview - to go through the generic questions as detailed below. This should take no longer than about an hour. During that interview ask for as much documentation as possible from the respondents and whether it is possible to follow up with another more targeted phone call based on a review of their documentation.*
- *Subsequent targeted interview – to go through a more detailed list of questions about their programs based on review of documentation and comments by Trémolet Consulting on your initial write-up.*

Interview objectives: the objectives of the interviews are to assess what sanitation financing the financial institution in question has been providing, how this fit within their broader range of products on offer, whether they have received any public support for their activities and what the estimated impact of their services on recipients (e.g. borrowers) has been.

Upstream work prior to conducting the interview

Overview of the institution *[we will aim for most of that to be done based on previous knowledge / internet searches, data gathered via mixmarket – i.e. compile short description in the "financial institution fiche" (as per Annex D) and prepare more detailed questions for each. If you have more detail on each institution that does not fit into the fiche, then feel free to write some additional text as well which may be used in the overall India report]*

Reporting on each MFI/ microfinance actor contacted

Please keep a file per MFI with all the relevant documentation in each file. If possible, we would like you to create a "dropbox" account so that we can share documentation between us over the internet – with regular email updates about what has been done. If you already have a dropbox account, please let us know which email address it is attached to so that we can "share" our existing folder with you.

On each MFI / microlending organisation, we would like to fill in a table such as what appears in Annex D. For other types of organisations (such as APEX institution or MFI institutions, the information requested will be more general in nature and can focus on Sections 4 and 5 of the interview guide.

Interview guide

1. Characteristics of the financial institution

- When was your organisation created?
- What is the main purpose of your institution? [*e.g. providing financial services to poor consumers, association of microfinance organisations, APEX institution, etc, etc*]
- What is the size of your organisation: number of staff, number of existing borrowers, and overall size of loan portfolio?
- What type of organisation is your institution (MFI/NGO/APEX/ associations, etc) and are you unregulated/ regulated (if so under which regime)?
- How do you channel financial support to the ultimate beneficiaries?
- Geographical areas of operation [*specify if rural, peri-urban or urban*]

2. Understand the extent to which the financial institution has been active in sanitation

- Are you providing microfinance products that help households invest in their own water and sanitation solutions? *[If so, specify whether it is water or sanitation]*
- If you are considering doing so in the near future but not yet launched, have you carried out research/evaluation to consider how to get involved?
- In which "target area" are you providing such sanitation loans? [*indicate, for example, the number of wards or districts or whether these loans are provided throughout a given State*]
- What type of MF products do you offer that can be used for sanitation (or water) investments?
    - Loan products
    - Are loans combined with savings [*this might apply to commercial banks, not to MFIs as they are not allowed to take deposits*]?
    - If so, how: do borrowers need to join a savings and loan group or ROSCA?
- What is the size of your "sanitation" related portfolio: number of sanitation loan borrowers, size of sanitation loan portfolio?
- What are the features of the sanitation loan products that you offer?
  - Average loan amount for Sanitation and for water
  - Interest rate and other charges (Loan processing fee, loan loss insurance etc.)
  - Loan term
  - Collateral if any
  - Any margin amount from client
  - Grace period
  - Collection frequency (Weekly/Monthly)
  - Average periodic instalment size
- How do these features differ from those of other loan products you may be offering?
- What type of water/sanitation investments are made by your customers (e.g. on-site latrine, septic tank, water tank, etc)?
- Did you develop specific sanitation-related products or were you able to use existing products to respond to a demand from customers for sanitation-related products?
- Do you provide housing loans and if so, do you know whether a portion of such loans is also used to build sanitation facilities?

- Do you provide any other type of general MF products that you know households are using to finance the costs of sanitation facilities (even if it was not their original purpose)?

3. Evaluating demand for their MF sanitation products

- How did you identify the demand for MF sanitation products in the first place? Did you conduct market research prior to launching your sanitation products?
- In the geographic areas where you do provide MF products for sanitation, do you know how households usually finance their sanitation investments? If they borrow from traditional sources (i.e. local money-lenders), what are the terms at which they would borrow?
- Have you sought to estimate the “untapped” demand for sanitation MF products: do you think that there is a high potential for market development? How do you plan to capitalise on this: are you planning to extend your activities in the area?

4. Measuring the impact of sanitation loans on target population

- Which population groups do you target with these sanitation MF products?
    - Poor/non poor
    - Women/men/both
    - Slum dwellers / non-slum dwellers/both
    - Urban/rural
    - Any particular community?
- If you target a particular group, how did you make sure that you reach those groups in particular? In particular, how do you measure the income of the targeted household (if at all)?
- If providing a loan, how do you evaluate household’s potential ability to repay the loan? Do you check whether they have subscribed to loans from other organisations?
- What has been the performance of your loan portfolio in the sanitation sector? Is it better (or worse) than for other types of MF products?
- Have you sought to measure the impact of your programme on the households that have subscribed to your MF products: in terms of access to sanitation? In terms of freeing up time for income-generation activities? In terms of overall poverty reduction?
- How easy or difficult it is in delivering the Sanitation loan product as compared to other Microfinance products? What are the major challenges if any?

5. Evaluating donor/Government support

- Did you receive any public financing to support your MF activities in the sanitation sector? [*by public we mean government subsidies, grants or concessional loans from international organisations or charitable organisations, NGOs, etc.*]
- If you did, what role did such support play in improving the financial viability of the scheme? Can sanitation products be sustainable using commercial funds? If no, for what purposes are public funding required?
- In which form was public support provided:
    - Grant (for what: to cover the initial costs of market research, product development, marketing costs, seed financing for a revolving fund, other type of technical assistance?)
    - Loan (for on-lending)

    - Guarantees?
- Would you have considered other type of support necessary?
- Do you think there is enough public financing available in order to encourage financial institutions to provide microfinance for sanitation?

6. Overall assessment of your experience with microfinance for sanitation

- Would you say that your experience with MF for sanitation has been positive/negative?
- Do you think that this is a market with substantial potential for development?
- Where do you think is the highest demand for microfinance products for sanitation: in rural vs. areas? From what kind of population groups, for what types of investment?
- What, in your opinion, are the main factors that explain that only few MFIs (in India and throughout the world) are offering MF products for sanitation?
- Have your activities in general and in sanitation in particular been affected by the recent backlash against microfinance in South Asia?
- *[Finally, if they are willing to participate, send them the list of MFIs that we know are providing (or contemplating providing) microfinance products for sanitation and ask them whether this list reflects the entire market or whether others are also involved in the market (which we do not know about)*]

Annex F: Indicative sources

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