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RESEARCH

Assessing financial sustainability as a key indicator for business transformation of microfinance institutions: A study in India

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Access to financing is acknowledged to play a notable role in the development of economy by efficiently allocating resources from excess units to units in need. If microfinance institutions (MFIs) can maintain good financial performance, the positive effects they have on the financial wellbeing of those in need will continue. To promote sustainable global development, sustainable financial practices are essential. Previous studies have been motivated by the economic crisis to highlight the necessity of assessing and managing financial sustainability in business. India is the top borrower in South Asia, and hence, this study is significant for the MFIs in India. This study's goal is to look into the pattern of Indian MFIs' financial (1) success from 2014 to 2017. The result shows that women are consistently being the highest borrowers.

Keywords: financial performance, financial sustainability, India, sustainable financial practices

1. Introduction

According to Singh and Gashayie (2) microfinance institutions (MFIs) that are owned and run by their members, such as rural cooperatives for savings and loans, sustainability refers to their capacity to continue to provide financial services while maximizing member economic benefits. The main goal of these institutions is to sustainably increase the socioeconomic wellbeing of all members while using domestically generated revenue to pay for operating expenses. The significance of deposit mobilizations for establishing financial sustainability has been underlined by several authors (3). The ability of a company to generate more alternative revenue streams to sustainably provide standard services to its clients is referred to as financial sustainability, assessed using metrics like profitability, liquidity, solvency, efficiency, and effectiveness (4). Economic development and growth are greatly influenced by financial access. The main aim of microfinance units is to disseminate the resources from where it is surplus to where it is in need. Financial sustainability is the MFI's ability to meet the current as well as other costs associated with the future development activities. It is advisable to keep in mind that an organization's overall sustainability includes a variety of organizational and human capacities in addition to its financial sustainability, which is important but only one part of sustainability overall (5). About one-sixth of all people on the planet live in India. The lack of bank accounts and a formal credit for 87% of the poor have been predicted, and these MFIs have a greater role to play in financing the villagers. The banks are concerned about the borrower's capacity to pay off the loans, their erratic revenue sources, and their inability to offer collateral services (6).

2. Methodology

In order to evaluate the financial viability of MFIs in India, this study was done using the secondary sources that used a number of ratios, including the proportion of female borrowers to the total number of active borrowers, the total equity to the total asset's ratio, the proportion of deposits to the total assets, the return on equity, and the debt-to-equity ratio (7).

3. Results or finding

Approximately 97 MFIs operate in India (RBI). The return on assets (ROA) ratio is an important profitability index since it shows how well an organization manages its investment in assets and uses them to generate profit. The ROA ratio gauges how much a company makes in profits and about how much it invests in all of its assets. The return on the assets from 2014 to 2017 is not satisfactory because it decreases and it is less than 3%. Return on equity also reveals the institution's profitability. This ratio is especially important for a business that generates profits and has actual human owners. Since it quantifies the return on their investments in the institution, return on equity is for them a metric of utmost significance. The return on equity is greater than 15% only in the years 2014, 2015, and 2017. The year 2016 did not show a satisfactory ratio. In addition to reducing poverty and promoting financial stability, microfinance aids in a series of "worthy spirals" that empower women economically and socially, advancing the cause of gender equality; however, access to credit and other financial services was less common for women. It has been claimed that women make better customers since they are more likely to save than males, borrow less money, and perform better while making repayments. These characteristics of female clientele serve as proof that MFIs are drawn to serving the needs of women. Women make up the largest percentage of borrowers overall (70%), and their share of total borrowing is likewise consistently higher than that of men. Deposit-taking may be the barometer to measure a financial institution's long-term viability. This can be accomplished by giving MFIs a reliable way to finance a rising loan portfolio, which will free them from reliance on outside sources and thus increase the institution's sustainability. The deposits-to-asset ratio (DAR) for microfinance institutions (MFIs) is a financial ratio that measures the proportion of an MFI's total assets that are funded by deposits. It is calculated by dividing the total amount of deposits by the total amount of assets. The deposit to asset ratio was high in the year 2016 and 2017, A higher DAR indicates that a greater proportion of the MFI's assets are funded by deposits, which is generally considered to be a good thing. This is because deposits are a relatively stable and reliable source of funding, compared to other sources such as debt or equity (7) (**Tables 1**, **2**).

TABLE 1 | Trends of MFIs' financial performance over the study period.

Key indicators	2014	2015	2016	2017	Average
Debt to equity ratio	4.5	5.4	4.2	3.7	4.45
Return on assets	3.4%	3.1%	2.6%	1.7%	2.7%
Deposit mobilization	0.00802	0.15792	0.28337	0.29013	0.18486
Deposit to total asset ratio	0.01035	0.15910	0.23232	0.26181	0.16589
Return on equity	19.6%	20.9%	14.3%	8.2%	15.75%
Percentage of women borrowers	96%	97%	98%	97%	97%

Source: by authors.

TABLE 2 | Description of the variables.

Variable name	Variable code	Descriptions
Debt to equity ratio	DTE	Total liabilities/total equity
Return on assets	ROA	Net income/Total assets
Deposit mobilization	DM	Deposit/total loan
Deposit to total asset ratio	DTTA	Deposit/Total Asset
Return on equity	ROE	Net income/shareholders equity
Percentage of women borrowers	PWB	Number of women borrowers/total borrowers

Source: by authors.

4. Discussion

The viability of MFIs is influenced by a wide range of key elements. The present study was conducted based on the secondary data available. The study further needs to be done using primary data. This study has considered only profitability and outreach elements, ignoring other key elements.

5. Conclusion

Microfinance makes a substantial contribution to lowering the failure rate of the credit market by providing financial services to the people with low incomes. However, providing this kind of service to the underprivileged entails high transaction costs, some degree of risk, and a low rate of return. Investigating and keeping an eye on these institutions' financial viability is crucial given these difficulties. Further study must also concentrate on management inefficiency, loan intensity, portfolio at risk, and size and its effect on sustainability.

Author contributions

All authors listed have made a substantial, direct, and intellectual contribution to the work, and approved it for publication.

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