Case Study: Financing the unbankable
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Financing perceived high risk customers
An unlectrified marginal community of farmers and low wage earners in Raichur, Karnataka have been facing troubling times with erratic rainfall and inability to invest in irrigation tools. This leaves them in a continuous spiral of poverty as they are unable to find the means to improve their incomes. Another consequence is the inability to open bank accounts. Partially due to the community’s own fears of dealing with banks and the bankers reluctance to lend to such high risk segments. The case story captures a technique used to demonstrate bankability of such customers to main stream financial institutions in the hope that upon seeing the timely repayments the nearby local banks will be encouraged to extend loans to the community to purchase lights and other services as well for their daily needs.

Identification
A local newspaper highlighted the plight of Mangammahatti community, Sindhanur, Karnataka. Following which SELCO’s Sindhanur branch office contacted the community to figure out ways to resolve their energy needs.

Problem Statement
A number of local banks declined to lend to the Mangammahatti community as they were perceived as high risk i.e. mostly those who do not have bank accounts and are perceived to be unable to repay the loans without protective measures of collateral or guarantee funds or any other credit history.

Financial Model
The systems were installed by SELCO on the understanding that the system would be repaid through 2 interest free instalments by the end of one year as it coincided with crop yields. The community put in a downpayment of Rs 1,000, but did not have to offer any collateral or guarantee for the loan.

Manghamahatti is a neglected community of marginal farmers and low wage earners who have no reliable access to basic facilities like lighting, sanitation and water. Located in the Sindhanur taluk of Raichur district the community relies entirely on rainfall as they are unable to invest in irrigation.

The community has no predictable cropping patterns growing different commodities like cotton, and jowar, but this is not sufficient to meet all household requirements. Therefore a few family members typically engage in farming half to one acre piece of dry land they own, while the remaining members undertake wage earning jobs like construction work in order to supplement household income.

The unelectrified community often buys part of its kerosene from the black markets to meet its energy requirements. Lack of basic lighting facilities has security and health implications for the community and also gives little opportunities to work on secondary sources of income at night. Each household purchases about 7-8 litres of kerosene per month at least 50% of which is from the black markets. Black market prices cost upto Rs 70 per litre as compared to govt. subsidized prices (PDS) of Rs 25-40 per litre.

A number of the families in the community are nuclear families. The elders in the family have little educational qualifications or vocational skills, while children’s education is a challenge owing to low income sources. Some children attend government schools to benefit from the mid day meal school.

A range of local banks were unwilling to finance the lighting systems. This is because these communities hold little property to pledge as collateral and have no regular and predictable sources of income. Most members have little or no banking experience.

But SELCO decided to go ahead with the project to demonstrate to the banking community that the poor communities can be prudent borrowers especially when it comes to meeting their essential requirements. The communities reposed this trust that SELCO showed in them by repaying the two loan instalments in a year’s time.
Key aspects

- **Establishing banking ability**: SELCO’s main aim behind the project was to highlight to the banking community that the poor have the capacity to take loans from banks through regular lending channels in a responsible manner.

- **Demonstration effect**: The success of the project impinges upon the other community members adopting the scheme, which is now evident as neighbours have evinced interest in securing solar systems.

- **Needs assessment**: Designing a system based on needs of customers is critical to ensuring that they are satisfied. Equally important is an understanding of cash flows to design a suitable repayment schedule that makes it affordable.

Risks and learnings

- **Scaling up**: High Risk Projects can be used only on a pilot basis to convince bankers and communities to finance and adopt solar systems respectively. It is not an ideal model to be replicated or scaled up as it will consume resources that could otherwise be utilised to reach out to other needy groups.

- **Opportunity cost**: If the financial arrangement was made through a bank, the borrower could have got an easier repayment schedule through longer tenure loans that matches the income of the household. In this case a shorter time frame was also to prove to the bank that repayments were made in a timely manner even in a short period of time.

- **High risk, based on trust**: As the name suggests High Risk Projects are those extreme cases where bank finance is unavailable and SELCO is forced to intervene. One concern with the project is whether bankers will finance similar projects as it relies heavily on trust as opposed to assets that back the lending.

Technical Specifications

The 2 LED light system has a 18 W panel, 15 Ah battery and 5 amps regulator. The cost of investment stood at Rs 9,000 each for the 5 houses.

Project Nuances

Though 8-10 households came forward to participate in the project, only five were chosen as they were willing to put a downpayment of Rs 1,000 towards the systems. It took nearly 6 months of efforts to convince local banks in the region before embarking on this strategy.

Impact

Quality of life – The households now have access to reliable lighting systems which has a positive impact on comfort, safety and lifestyle. Children can also study extended hours.

Savings – The households previously relied on buying expensive kerosene from the black market as the fair price shops could not meet their full requirements. Estimated savings on account of using solar ranges from around Rs 200-300 per month.

Social status – The households enjoy better status in the neighbourhood with others now seeking to install solar lighting themselves.

INNOVATION

- Easy loan terms packaged to ensure that the community worked towards the success of the project
- Demonstration effect that sets an example for bankers and other community members to replicate
Typical rural high risk segments