EQUITAS HOLDINGS PRIVATE LIMITED
4th ANNUAL REPORT 2011 - 2012

CORPORATE INFORMATION

Board of Directors

1. **Rangachary N**
   Chairman
2. **Arun Ramanathan**
   Director
3. **Gary Ng Jit Meng**
   Nominee Director
4. **Kuppuswamy P T**
   Director
5. **Nanda Y C**
   Director
6. **Paolo Brichetti**
   Nominee Director
7. **Rajaraman P V**
   Director
8. **Raman N**
   Nominee Director
9. **Sampath P B**
   Director
10. **Shankar V**
   Director
11. **Srinivasan N**
   Director
12. **Viswanatha Prasad Subbaraman**
   Nominee Director
13. **Vasudevan P N**
   Managing Director

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Auditors

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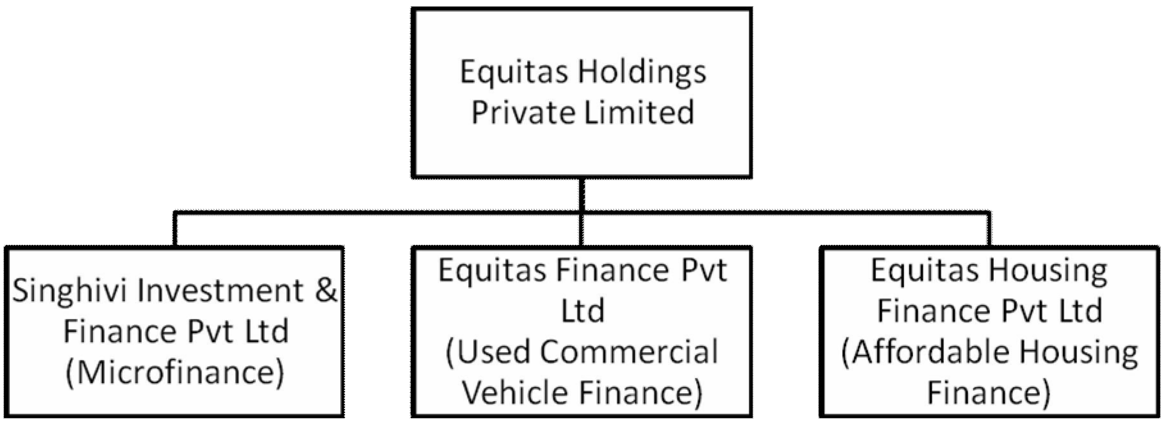
EQUITAS HOLDINGS PRIVATE LIMITED

FROM THE CHAIRMAN'S DESK

Dear Members,

For the third consecutive year, as I sit down to write to you, I cannot help but reminisce on how eventful this year too has turned out to be. This past year has been marked by the evolving regulatory framework in the microfinance sector, the nascent steps taken by our new businesses in vehicle & housing finance and a corporate restructuring exercise of the group. We started this year as a single rose and at the end of the year, I feel, that we have developed a rose garden.

The company has demerged the micro finance assets and related liabilities to its wholly owned subsidiary company M/s. Singhivi Investment & Finance Private Limited through a Scheme of Arrangement (Demerger) sanctioned by the High Court of Judicature at Madras. Subsequent to demerger, the Company ceases to be a NBFC Loan Company and falls under the classification of Core Investment Company. The company has changed its name from Equitas Micro Finance India Private Limited to Equitas Holdings Private Limited. We now have the following corporate structure with all three subsidiaries being wholly owned:



***Microfinance*: Regulatory Evolution Validates Our Model**

Prior to the crisis in micro finance in Andhra Pradesh in Oct 2010, RBI regulated the NBFC players in the microfinance sector at par with any other NBFCs. However, soon after the crisis, RBI had constituted a sub-committee under Shri Malegam to propose regulations for NBFC MFIs and RBI has since notified regulations, broadly in line with the committee's recommendations.

Malegam Committee Echoes Equitas Model!

The Malegam Committee conducted wide-ranging discussions with all stakeholders; and the Company also had an opportunity to present its model to the Committee. It is heartening to note that the comprehensive suggestions spread over 12 key factors, proposed by the Malegam Committee were a complete reflection of the Responsible Model of Micro Finance pursued by Equitas right since its inception from 2007. RBI has accepted the Committee recommendations and through its 2nd Dec 2011 notification created a specific category of NBFCs called NBFC-MFIs. This move towards regulatory clarity portends well for the sector's stability as well as the ability to serve the low-income group clients in a sustainable manner.

The negative backlash against MFIs had largely centred around three counts: usurious lending rates, over lending by multiple MFIs to same borrower and coercive recovery practices. I take pride in stating that Equitas has been setting benchmarks in Responsible Lending on these three key issues and which, now the Regulations are beginning to echo:

Usurious lending rate: When Equitas commenced business in 2007, other MFIs charged between 35 – 45%. However Equitas pioneered the unique concept that the cost of growth should be borne by investors and not clients. Thus a steady state operating cost of 7.5% was projected which was used to arrive at lending rate rather than the actual operating cost. Thus, the first lending rate by the company in 2007 was 25.5% all inclusive reducing balance rate at a time when the market rates were between 35 – 45%. This moderated stance on setting interest rates was also coupled with Equitas' voluntary cap on Return on Equity at 25% in line with the RoE of leading public sector banks. This again is unique amongst MFIs globally.

Curbing multiple borrowing: Within 2 months of commencing business, Equitas engaged MFIs operating in Tamilnadu towards working together on curbing multiple borrowing. And within 10 months of commencing operations, back in 2008, Equitas took the lead in forming a committee of all-India MFIs towards building a common credit bureau database. Since then, consistent improvements have occurred. All NBFC MFIs took an equity stake in Alpha, which became a shareholder of a credit bureau. And today, there is a strong and vibrant credit bureau functioning for the sector with the entire data of all members of MFIN (association of NBFC-MFIs) in it. This entire exercise is a unique feature in the financial sector; and could not have been possible without the leadership of industry stalwarts led by Shri Vijay Mahajan, President of MFIN. Our efforts in this area have been recognised.

Coercive recovery practices: Coercive recovery practices may normally arise only when a borrower has taken loans beyond her repayment capacity. Equitas' efforts to curtail over-lending have helped create an environment conducive to fair recovery practices. Equitas has voluntarily adopted internal guidelines on multiple lending right from inception; and also worked towards establishing a credit bureau across the sector. While there may be instances of individuals involving coercive recovery practices, MFIs have generally trained their employees well to ensure borrowers are treated well. At Equitas, detailed process manuals and guidelines have been issued to train the staff and only after staff is certified they are allowed to interact with clients.

Customer Friendly Repayment Practice (CFRP):

The company has to balance the company's interest of ensuring financial discipline amongst its members with the need of its members that the company be empathetic during times of stress. This is done through the CFRP policy. This policy recognises that clients may fail to repay the loan either due to temporary or permanent inability to repay. In case of temporary issues, the policy allows the branch staff to extend short term holiday to help the client tide over her financial difficulties while in case of long term incapacity the branch can waive the whole or a part of the remaining principal outstanding depending on the nature of the problem. However if the clients' non-repayment is purely due to an unwillingness to pay, the company takes recourse to the normal judicial process available to it. The

CFRP policy has benefited over 1500 members; and the support provided to borrowers under this policy is to the tune of Rs 42 Lakhs.

Margin cap:

The Malegam Committee innovatively proposed a margin cap of 12% (i.e. the difference between the borrowing cost and lending rate of an MFI) to encourage NBFC MFIs to focus on improving operational efficiencies. Now that this cap has become enforceable, MFIs have little choice but to focus on reducing their operating expenses. This is a game-changer in the microfinance sector; and will prove to be a defining period for many of the players in the sector.

Equitas priced its very first loan at 25.5% based on a target operating expense of 7.5% And thus, does not have to change its model in any way to suit the new regulations.

Social Initiatives – Another feather in Equitas' cap

At this juncture, it will be appropriate to highlight the social initiatives undertaken by the company. Equitas' clear focus on social initiatives is borne out by the fact that within 2 months of its inception, Equitas Development Initiatives Trust (EDIT) was formed. Under the able guidance of our Trustees Smt CK Gariyali (IAS – Retd), Shri MB Nirmal (Founder Exnora), Shri SP Mathur (IPS – Retd), Smt Vijayalakshmi (Educationist) and Shri P N Vasudevan, our Trust has rolled out initiatives on the following fronts:

a) **Education**: The Trust operates 4 schools and around 50 tuition centres to provide high quality education to over 4200 children from low-income households.

b) **Health**: In partnership with local health service providers, the Trust has conducted health camps across Equitas branch network for the benefit of borrowers' households. These camps range from general medical check-up or eye check-up to cancer detection camps; and have so far benefited over 8.15 lakh members.

c) **Vocational training**: The Trust conducts short and focused training modules to impart skill development & vocational training to its members; to enable them to augment their income. These programs have benefited more than 2.5 lakh members.

d) **Rehabilitation of pavement dwellers**: Through its Bird's Nest program, the company has rehabilitated 93 families previously living on the pavements of Chennai. This program has been supported by funding from Unitus Inc.

By benefiting more than 1 million members through its social initiatives, Equitas has set another benchmark in terms of holistic approach to clients and their families and has emerged a pioneer in this field.

Vehicle finance & Housing Finance**: New Engines of Growth**

Equitas' vehicle finance, which focuses on financing purchase of used commercial vehicle is enabling first time buyers and drivers to turn owners. We have till now supported over 3500 clients with a total disbursement of about Rs. 100 Crores through 60 branches in 5 States.

Equitas Housing Finance provides long term housing loans to the self-employed people who are unable to access the same from mainstream financial service providers. Disbursement during the year is about Rs. 9 Crores and has benefited over 150 persons enabling them to own their own homes.

While still at a nascent stage, Equitas' vehicle & housing finance businesses are set to help build a well-diversified portfolio. The used commercial vehicle finance market has only a few players and together with the company's senior management's experience in this market, Equitas is expected great strides in this sector. Housing finance for the self-employed segment presents a large nascent and untested opportunity. While the growth of this business would be relatively slow, the Institutional intelligence on income appraisal of self employed segment is expected to serve as a strong USP and differentiator for the company in this space.

Equitas B2B trading: As part of its endeavour to reach the needy and its social obligation to its clientele, the company had experimented by buying vegetables in aggregate and supplying the same to its micro finance clients who are vendors of vegetables. It was expected that our ability to aggregate would help us offer immediate value to our clients. However due to poor performance of the pilot, the company has ceased this operation and is studying other options.

Equitas: The Way Ahead

The Government of India has introduced the Microfinance Bill in Parliament and once passed, this will further strengthen the regulatory framework by including NGO MFIs within the ambit of microfinance-specific regulations. While we expect a stable regulatory regime to help the sector, the real game-changer would be focus on efficiency towards achieving op-ex levels of 7-7.5% and clear positioning as a holistic support service provider rather than a lender alone. Even before the Company was formed, Equitas had identified these two clear levers and has worked towards these objectives since inception. Equitas has developed and implemented a unique responsible lending framework and has also provided an Ecosystem of not-for-profit services designed to either increase the income or reduce the expenses or facilitate long-term investments of the microfinance borrowers. Continued focus on this approach will help the company emerge as a leading and differentiated model – a model which competitors may seek to emulate and even regulators may seek out as the ideal MFI model.

While on the subject, I will briefly like to touch on a debated subject – the deemed conflicts between self help group (SHG) programmes launched in some States and the micro finance business. It has been argued that MFI business was after all commercial – whatever be the rates of interest offered. It is argued that the structure of the business prima facie converts the MFI into a commercial model dictated and governed by profit motives of its owners and cannot prima facie claim to be a financial inclusion instrument or a social institution as a SHG. While the basic structure of these two institutions remain the same, membership of the institutions being drawn from women members of a household, diversified membership, a spirit of cooperation and help that brings the members of the group together – there is still an unexpressed feeling that MFI's charges are considered very high as compared to a SHG. An additional criticism is about the recovery process that a MFI sets up at the time of failure of repayments.

While I do not at this stage like to enter into an animated discussion on this issue, it remains to be recognised that there is enough space for both SHGs and MFIs to operate in the area of financial inclusion. It is not required that SHG and MFI be treated as adversaries and in constant conflict. Both models have their benefits and drawbacks and if the actions of these Institutions are fair, transparent and responsible, surely they can both serve the common needs of the members of the low-income segment of the population which Banks find difficult to service directly.

I must mention at this stage that when we established Equitas in 2007 and set up our business, we felt the need to be as close to our clientele as possible, serve them in many ways that were socially and economically relevant, act as transparent, responsive and responsible Institution to secure a better life for our clients. I am proud to say that our fundamentals have not changed despite set back in certain geographical areas. We want an Equitasian customer to be holistically served in the most responsible manner possible and the feeling that we have achieved this goal is what has made us unique. It is a matter of great pride to note that the new set of regulations brought in by RBI for the NBFC-MFI sector last year is very similar to the model of Responsible Lending that we, at Equitas have practiced right from our inception in 2007.

We therefore, owe a debt of immense gratitude to our customers, our employees, investors and other stakeholders who have allowed us to practise what we think is right, the financial institutions who have stood by us, regulators and statutory authorities, State Governments and the Centre to practice what we think is the right approach in a dynamic and responsible field of operation. To all these person and bodies and organisations, on behalf of the entire Equitas family and my own behalf, I say “thanks”.

During the course of the year, the company has been fortunate to secure the services of some very committed and distinguished persons to serve on its board and has appointed four new directors to its board – Shri Arun Ramanathan IAS (former Finance Secretary, Government of India), Shri YC Nanda (former Chairman, NABARD), Shri PV Rajaraman (former Finance Secretary & Development Commissioner, Tamilnadu Government) and Shri PT Kuppuswamy (former Chairman & CEO , Karur Vysya Bank). With the addition of these persons, the company’s focus on governance and customer-centricity will be further strengthened.

As exciting as the past few years have been, the future seems just as exciting for Equitas. Keeping aside the operational strengths of the company, I believe its sense of purpose and unique philosophy of “Fair & Transparent” will serve it well in the long run!

N Rangachary
Chairman

Chennai, 9th May 2012