

Exploratory work in Orissa:

Who is the marginal client for Microfinance? & Why do people repay so well?



**Centre for Micro Finance
Research**

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Institutions analyzed

Gram-Utthan (GU) *Kendrapara District*

- 100% rural
- Nearly 32,000 members
- NGO
- SHG scheme

Swayanshree (SS) *Cuttack*

- Mostly urban
- Nearly 7,800 members
- Federation
- SHG scheme

Variable	Swayanshree	Gram-Utthan
Mandatory savings (monthly)	30	30-100 Defined by the group
Maximum Loan	40,000	15,000
Loans classification (interest and payback period accordingly)	General (consumption and productive, 24%) festivals (18%), Asha loans (0%)	General (18% to SHGs), Poorest of the poor (12%)
Recovery rate on principal	96%-97%	97%-98%

Data collection

Methodology/Source

- Interviews to SHGs' members (individual and group questions) and some interviews to non clients
- Individual questionnaires and group discussion to loan officers and manager staff
- Records from institutions

Some caveats

- No random sample
- People from the same occupation tend to live close and group together
- Records in the institutions are still peccary and few historical disaggregate information is available by electronic means
- For the first institution the questionnaire considerably varied from the beginning to the end

Swayanshree basic client characteristics

SHGs visited	No.	11
Members interviewed (all women)	No.	127
Group's age	Years	3.1
Household (HH) members (2)	No.	5.7
Sons and daughters living in the HH	No.	2.6
At least x people in income generating activities (IGA) in the HH	No.	1.7
HH with 2 or more sources of income		49%
Member's level of education	Years	4.7

(1) Rs 30 is the savings in SS and Rs 10 go to the Emergency Fund. No date on voluntary saving

(2) Members living in the same house

**I. Who is the marginal client
for MF?**

II. Why do people repay so well

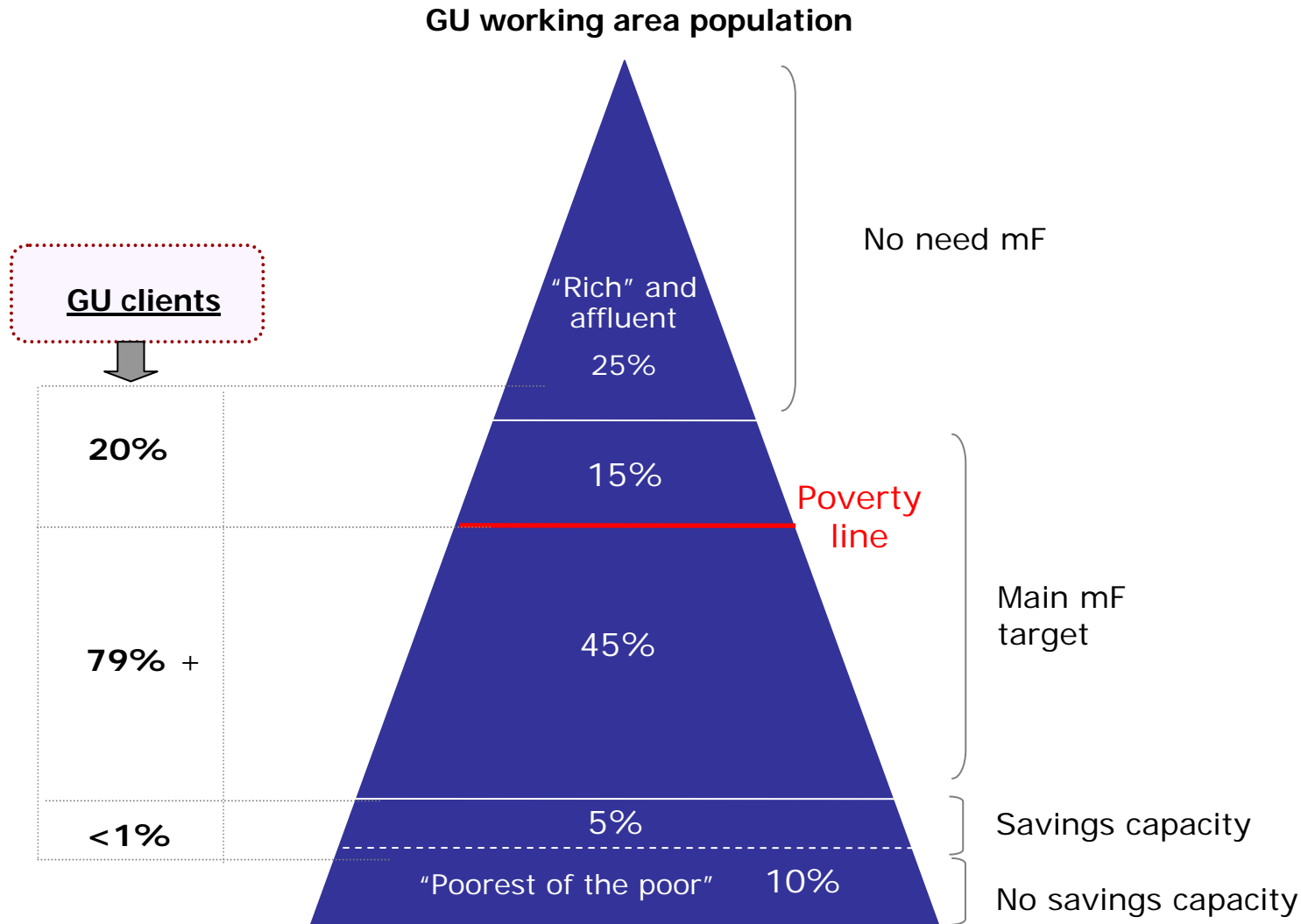
Who is the marginal client for MF?

i. Who is the client for mF?

- Income dimension
- Life cycle dimension
- Products

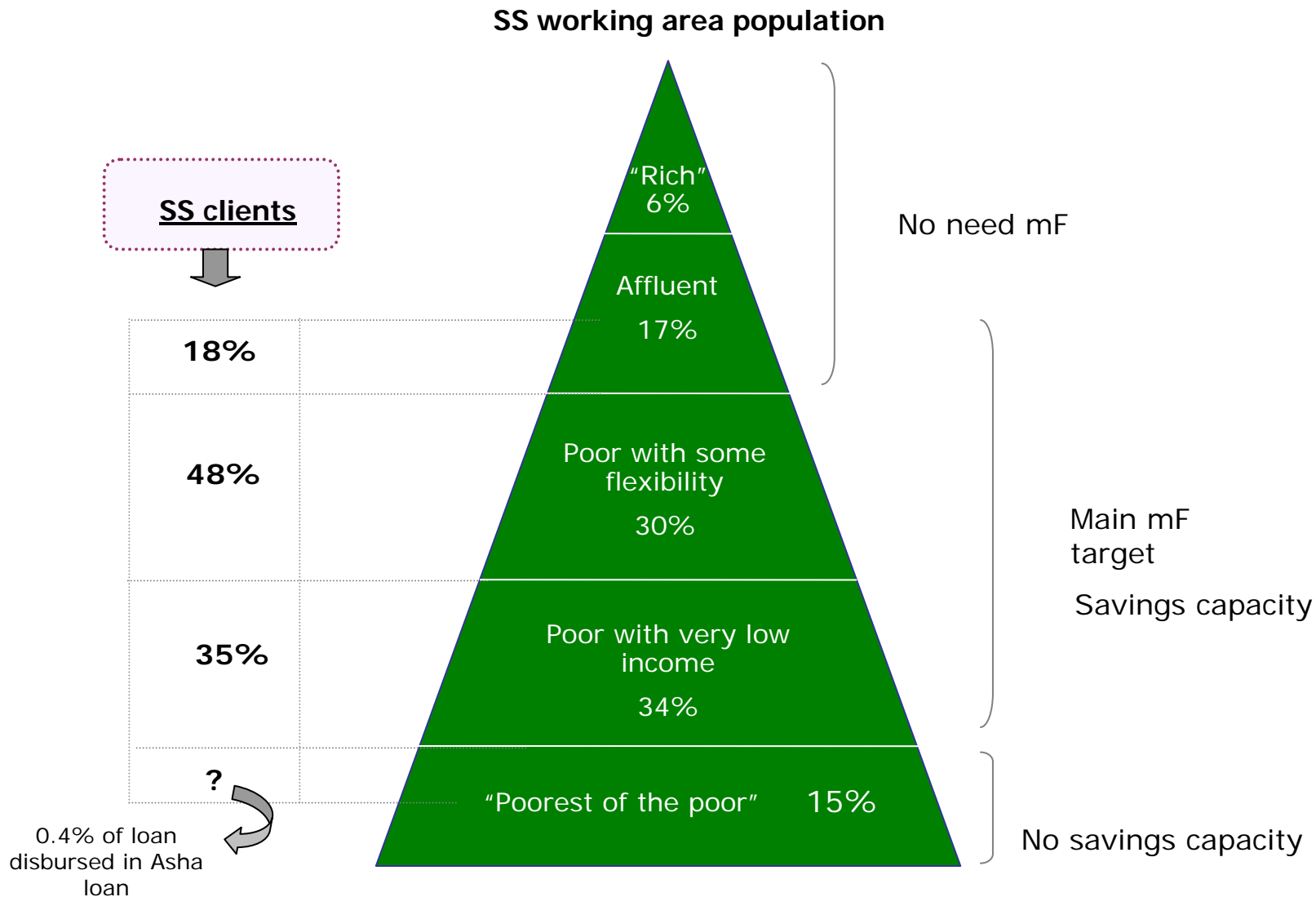
ii. Why do people join?

Income Dimension (*GU example*)



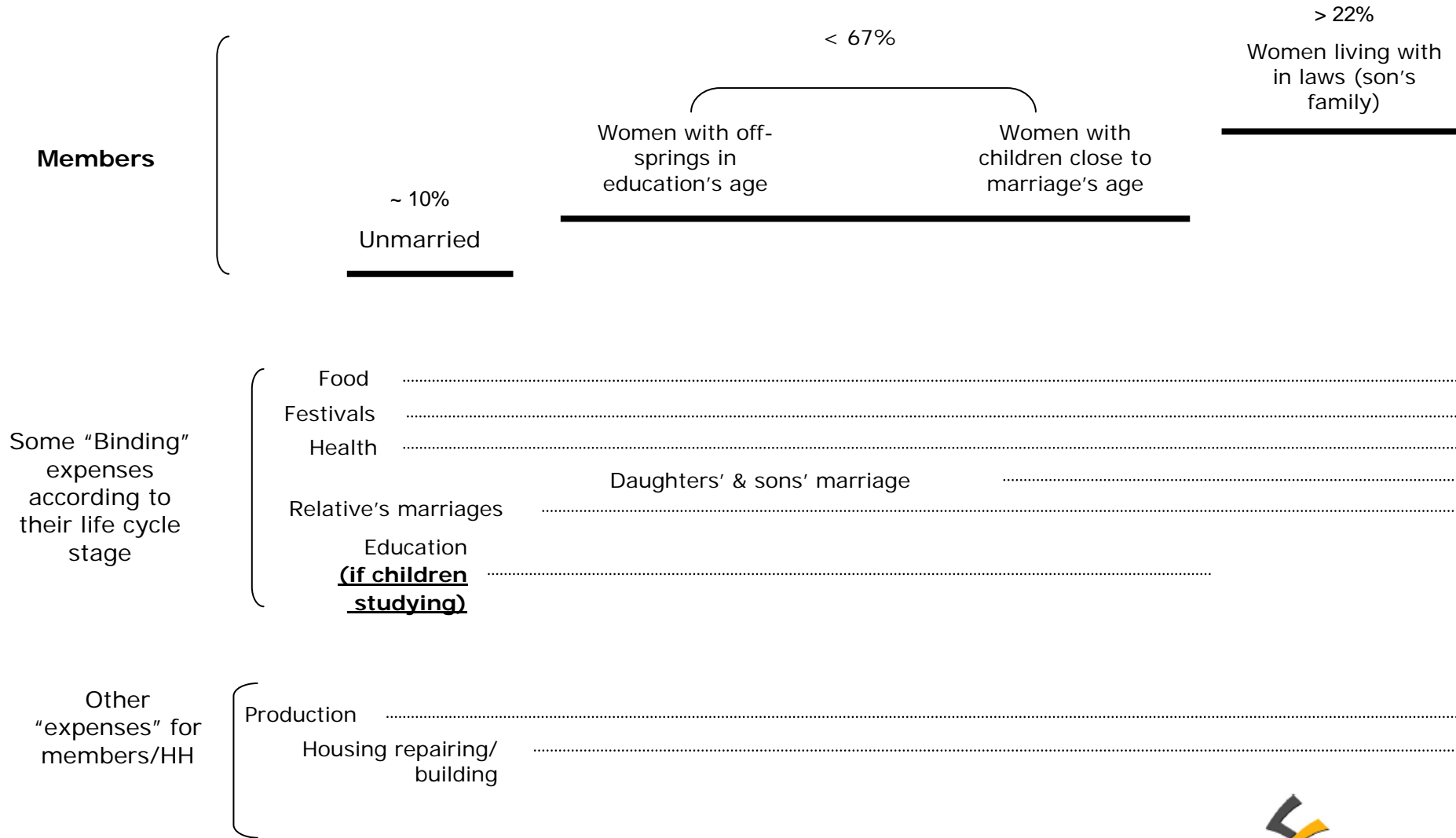
Source: estimations from interviews/questionnaires with management staff and COs (GU)

Income Dimension (SS example)



Life cycle dimension *(SS example)*

Expenditure side



What does influence the demand of different mF services?

- **Income** level determines more the amount rather than need for mF services in the potential segment. Access to mF is determined mainly through:
 - Savings capacity
 - Risk of being able to repay
- **Life cycle** stage determines some of the important expenses. Access to mF is considered risky for:
 - Unmarried women (change of residency when married)
 - Women older than 55 and younger than 18 (GU case)
- **Others** (some determine potential clients join, others what kind of services they demand)
 - Trust on the institution (join/don't join)
 - Social network/neighbors influence (join/don't join, services demand)
 - Risk attitude (taking loans, taking insurance, only savings)
 - Other financial alternatives (join/don't join)

However, the client for mF is mostly the household, not exclusively the women

- The mandatory monthly savings (Rs 30 – Rs 100) comes frequently from the money the women are given to run the HH (around 1% of the HH food expenses)
- But, the repayment of the loan is frequently the husband's responsibility
- An important proportion of women do not have own source of income

Member's level of education	Years	4.7
Members head of the HH (5)		2%
Members working outside of the house		9%
Members with own business or participating in the family business		36%

More extreme towards less participation of women working outside or in an own business

Some examples of expenses/incomes

The SS mean client

	<u>Expenses</u>	<u>Mean (Rs)</u>
Monthly	Food ⁽¹⁾	3,000
	Festivals	past 1,600
		Next 2,600
	Health ⁽²⁾	1,800
	Education (if children studying) ⁽²⁾	380
???	Relative's marriages	5,000
	Housing repairing/building	Depending on the project
	Production	Depending on the kind
	Daughters' marriage	1 – 4 lakhs

Some examples of monthly incomes (Rs)

Daily Laborer	1,840
Contractor	3,860
Housemaid	1,670
Rickshaw puller	2,100
Beggar	3,000

At least ~ 4,250/HH/month

But HIGHLY VARIABLE!



= Excluding the "rich" and affluent segment, the rest of the pyramid are "natural" borrowers and potential clients for mF

The top and bottom are riskier for mF providers

Products analyzed:

- Savings
- Insurance (mostly life insurance)
- Loans

Some data on the savings side:

DATA FROM GROUP QUESTIONS TO SHGS

SHGs' were most people didn't saved before 75%

The three reasons you value the most being part of SS:

	First	Second	Third
Savings scheme	25%	25%	36%

Savings come from the money they receive to run the HH		75%
HH head/member/daughter/son with other savings account/scheme		43%
Savings with Sahara		19%
Average monthly savings if Sahara scheme	Rs	358
If saving with Sahara, daily recovery scheme		67%

Some data on the insurance side:

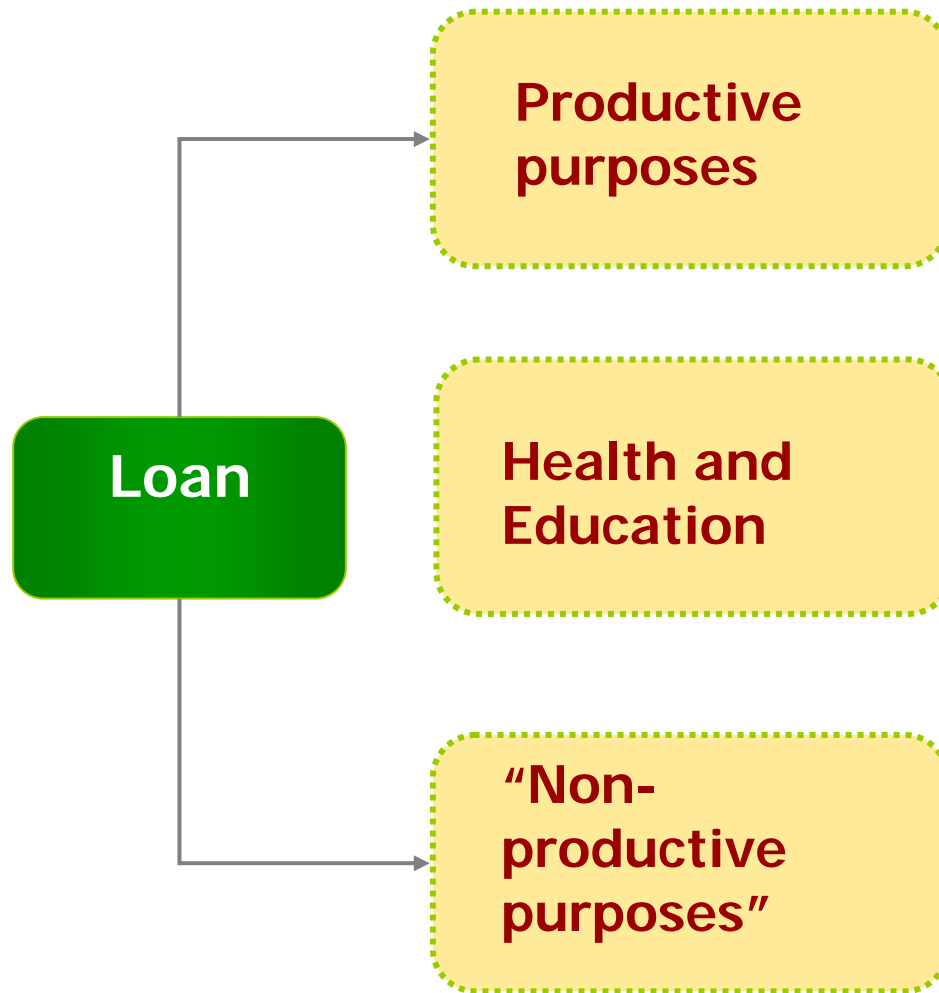
Note that none of the institutions offers life insurance

Swayanshree clients profile

Variable	Mean
At least one has life insurance (Husband/member/sons/daughters)	43%
Husband has life insurance	31%
Member has life insurance	10%
At least one son/daughter has life insurance	13%

Most of them have LIC: if the person doesn't die, after some years can start withdrawing the money (e.g. until the year 15 or 20). Therefore, this is both a way of insurance and savings

The loan side



The loan side: non productive purposes (smoothing consumption) are as important as productive purposes (income generating activities)

Swayanshree

For the last two loans taken for interviewed members	% of total loan value	% of total number of loans
Loans for productive purposes	45%	29%
Loans for health and education	12%	11%
Loans for "non productive purposes"	43%	60%
<i>Consumption</i>	6%	9%
<i>House repairing/building</i>	18%	17%
<i>Festival</i>	9%	26%
<i>Marriage</i>	7%	5%
<i>Debt Repayment</i>	4%	3%
No. Obs.	131	

Note that SS has special lines for festival and consumption loans while GU doesn't

The loan side (all borrowers):

Swayanshree June 2006

	% Amount	% Borrowers
CONSUMPTION	10%	23%
FESTIVAL	20%	25%
C + FESTIVAL	30%	47%
MIXED LOAN	34%	22%
PRODUCTION	37%	31%
	100%	100%

Gram Utthan loan disbursement in April 2006*

Classification	% Disburs.	% clients
Productive	53%	56%
Education	0.4%	0.4%
Health	5%	6%
NP	41%	38%
Consumption	3%	3%
Debt Repayment	12%	13%
Housing	21%	18%
Marriage	6%	4%
Total	100%	100%

Note: GU is just starting to record the information electronically. For that reason, no historical and unseasoned information is available (that is important for marriages and festivals since April is not a seasonal month for them)

Some data on the loan side

Swayanshree

Variable	Mean	No. Obs.
If loan for productive purpose, it was used for husband's/son's business	66%	38
Clients with loans with the moneylender now	52%	124

Note that the moneylender is the last resort borrower

In Gram-Utthan the No. 33 is more extreme since women are not allowed to work in the field and it's rural area

Why do people join?

SHG's group answers:

The three reasons you value the most being part of SS:

	First	Second	Third
Loan at low interest	42%	42%	18%
Savings scheme	25%	25%	36%
Group cooperation	33%	25%	0%
Financial Independence	0%	8%	0%
Door to door services	0%	0%	27%
Others	0%	0%	18%
Total	100%	100%	100%

Loan officers answers...

The two services people like the most from Swayanshree, in order of importance

	One	Two
<i>Savings</i>	50%	
<i>Loans</i>	13%	63%
<i>Savings and loans</i>	25%	
<i>Group formation</i>	13%	
<i>Training (includes financial literacy, empowerment, group management)</i>		38%
	100%	100%

Why do people join?

- **THE ALTERNATIVE**: They value the mF scheme (saving and borrowing) in a convenient way (doorstep service, fix day and place). ONE OF THE POOL: Most of them continue having one or more additional sources of loans (relatives, friends, societies and moneylenders) that they use according to their necessities (e.g., loan sizes, emergency)
- **THE CHEAPEST**: However, for most of them, mF represents the cheapest source increasing the likelihood to repay the principal of the loans.
- **SAVINGS**: Many clients join SHGs only to save as insurance, even if they are not planning to get a loan yet. *Learning to save/plan.*
- **GROUPING**: Group cooperation (social network improvement) is also an element. Social influence, group identity

People do not join...

- Lacking of trust in the institution
- Unable to save
- Needless of the services
- Influenced from others (e.g. husband, moneylender)
- Not accepted or expelled from the groups for inappropriate behavior

Loan officers answers...

The two most important characteristics of people who show some interest in forming SHGs but do not join

	One	Two
<i>Not needed</i>	38%	13%
<i>No enough/stable income</i>	13%	
<i>Didn't understand the goal of SS</i>	13%	
<i>Forbidden for husband/Outside Influence</i>	25%	
<i>Lack of trust in the organization</i>	13%	88%
	100%	100%

Other elements

- People follow the **leaders** and the crowd (a lot of herding behavior or group influence...)
- **Fears** within the **poorest people** to take loans are not rare (more risk averse? more status quo bias? Their reference point?)
- **The poorer the people are, the more difficult to fit into the scheme.** For instance, for the “poorest of the poor,” to plan or commit to a rigid savings/repayment schedule is more difficult because they are always thinking in the very short run (daily food).
- **The poorest people** have **less alternative** resources since their neighbors and friends hardly have extra-cash to lend them, and they lack collateral for moneylenders (jewelry). The interest burden is also generally too high (double without collateral).
- **The better off the people are** (i.e. having more alternatives), **the longer the time** it typically requires to build trust with the institution and also the less they are typically committed to the scheme.

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II. Why do people repay so well?

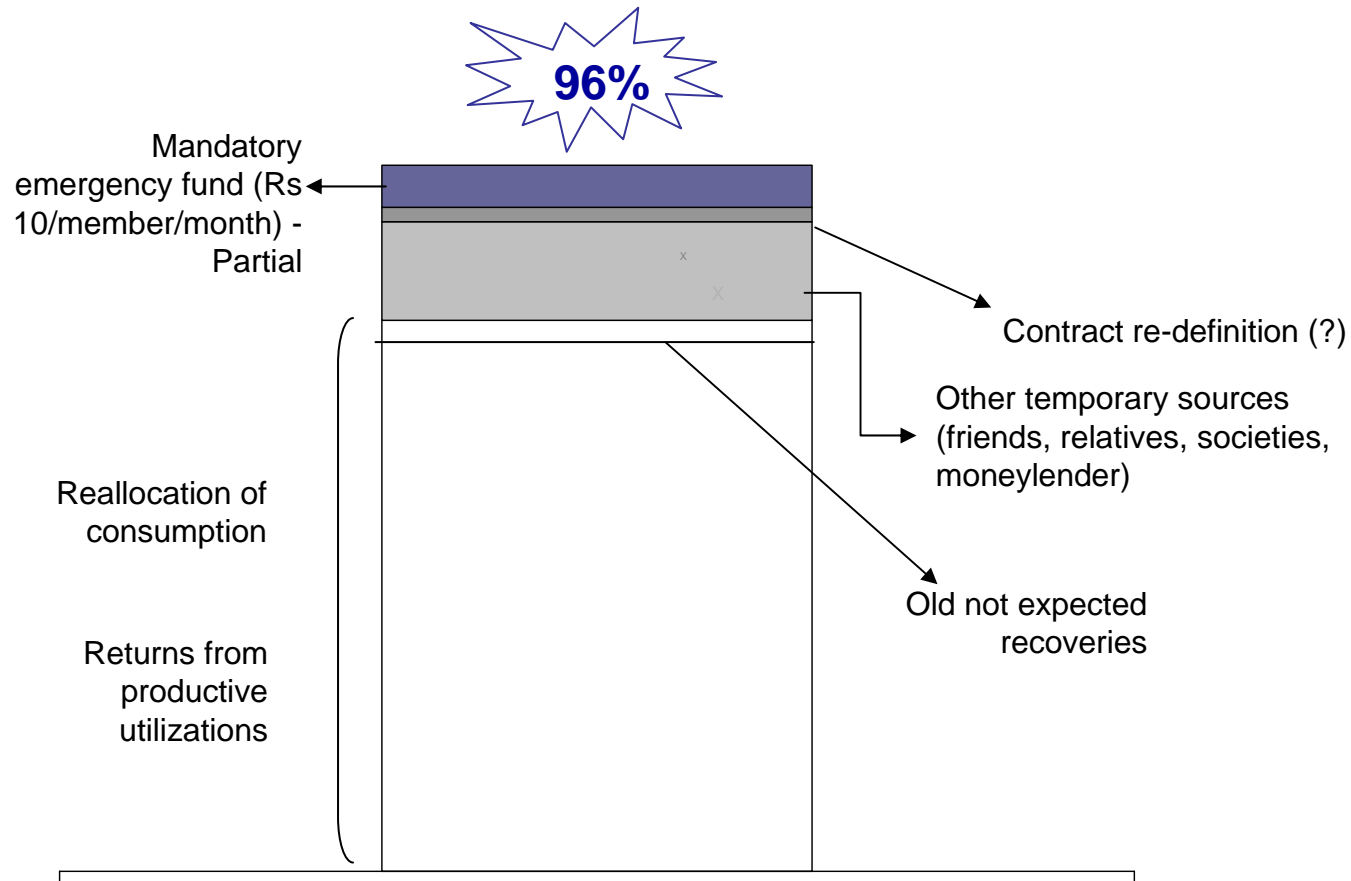
First, what is the repayment that matters?

- The repayment is usually measured based on principal recovery and not income (in the sector)... that is understandable for portfolio quality it wouldn't be when looking long term sustainability
- Cumulative repayment rate
 - Ratio of principal recovered (net of pre-payments) to the principal due since the beginning.
- Current repayment rate
 - Ratio of principal recovered (net of pre-payments) to the principal due during the current period

And more...

- **The concept of defaulter is blurry in practice.** Neither GU, SS nor the groups, treats a person as a defaulter if she pays an incomplete amount. For this reason, explicit peer pressure seems unusual (but it's difficult to observe this as an outsider). Group influence seems to act in indirect ways...
- **When people have additional income, they prefer to prepay** (also to get a bigger loan more quickly). In this way, they are **smoothing their shocks with prepayments or incomplete repayments.** How does much weights each element? In June, the prepaid principal was about 30% of the principal received.

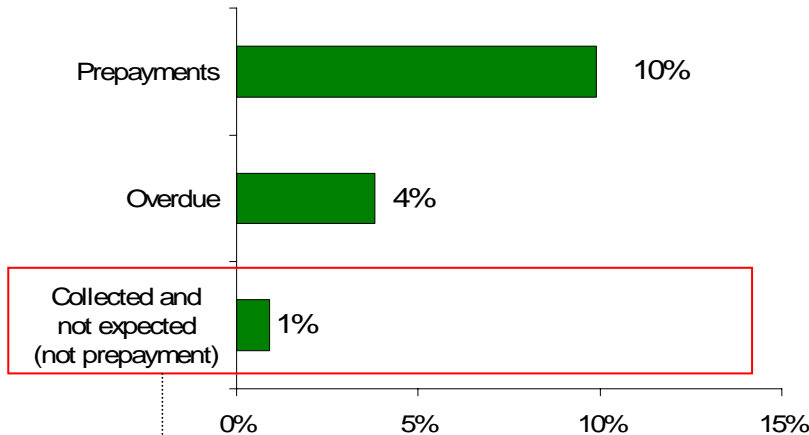
What can explain the high repayment rate? - Principal recovery (SS)



Prepayment and underpayments reflect how clients smooth their shocks

Value (as % of schedule principal recovery) - SS

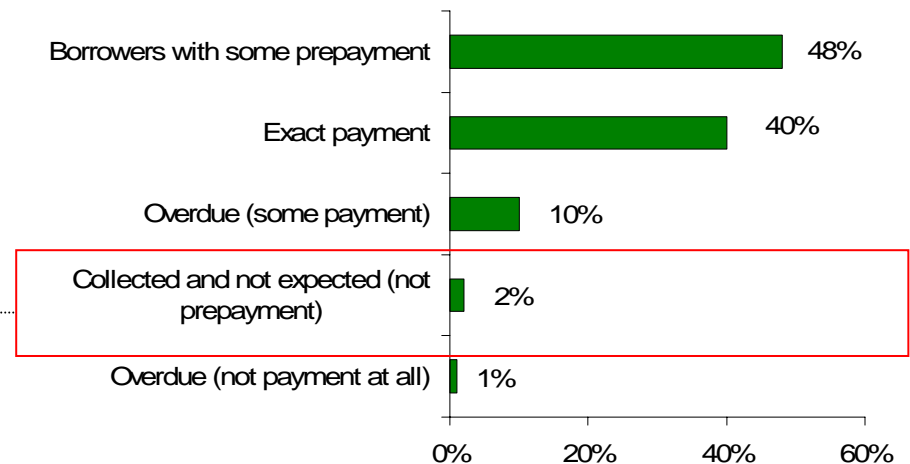
As on June 30-06



Are these past overdue?

Borrowers (as % total borrowers) -SS

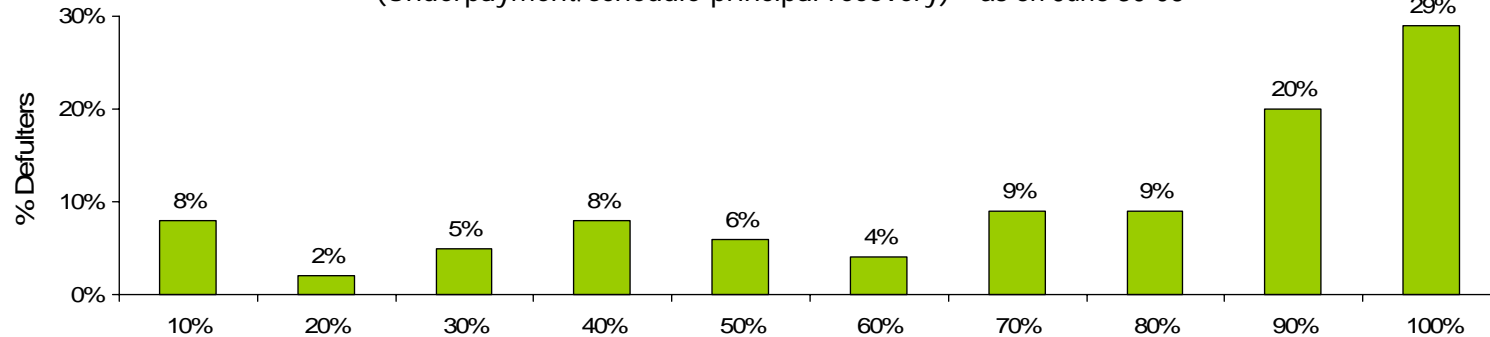
As on June 30-06



How deep is the individual default/ prepayment practices?

Underpayments Frequency

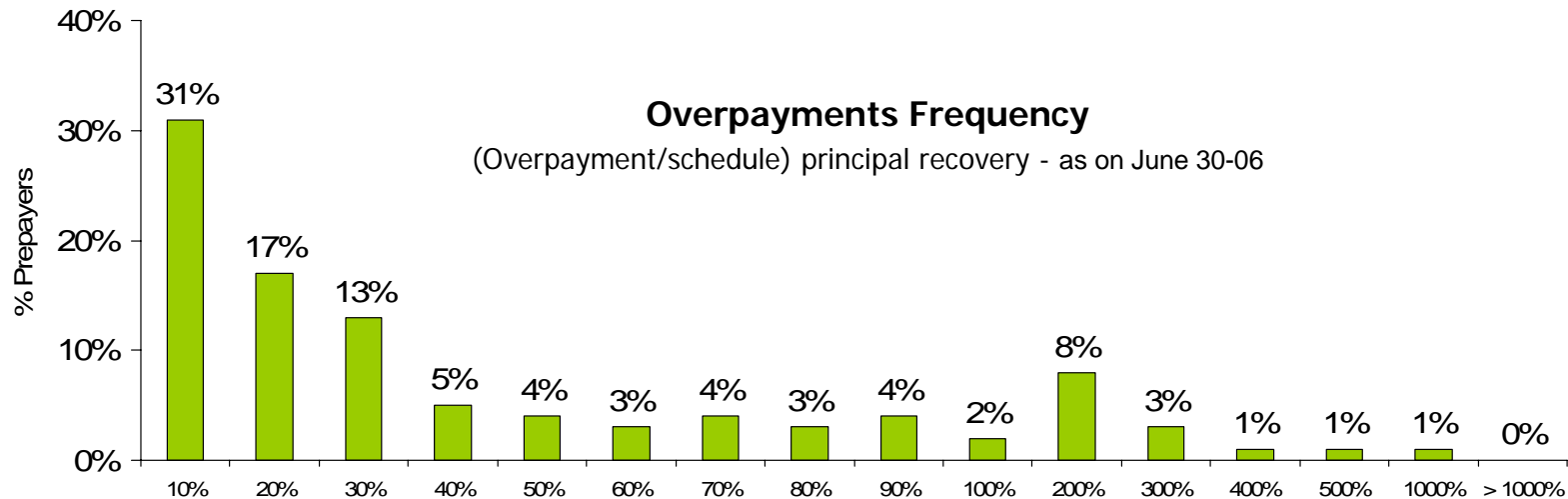
(Underpayment/schedule principal recovery) - as on June 30-06



Underpayment (% schedule principal recovery)

Overpayments Frequency

(Overpayment/schedule) principal recovery - as on June 30-06



Overpayment (% schedule principal recovery)

Why is so important to repay?

DATA FROM GROUP QUESTIONS TO SHGS

Why is so important for you to repay on time?... come to your mind when you cannot complete the money

	One	Two	Three
Group will suffer otherwise	42%	8%	27%
Less burden	25%	17%	0%
Moral duty	17%	17%	0%
Get another loan	8%	50%	27%
Don't want group pressure	8%	0%	27%
Financial Independence	0%	0%	18%
Total	100%	92%	100%

Have your group had problems of default?

Never	56%
Very few times (1 or 2)	44%

Loan officers answers ...

Why do you think people repay so well?	One	Two
<i>Group accountability</i>	25%	25%
<i>Proper investment of loan amount</i>	25%	50%
<i>Getting another/bigger loan</i>	13%	13%
<i>Regularly attend the meetings/understand the regulations</i>	38%	
<i>Loan suitable for the members</i>		13%
	100%	100%

How many other institutions offer micro finance services in the area you work?

4.6

Loan officers answers ...

) The main element you use to determine that a member can pay the loan she is asking for

<i>Regular savings, attendance, previous recovery practice</i>	50%
<i>Proper use of the loan</i>	25%
<i>The ratio according to the savings amount</i>	13%
<i>Family income source</i>	13%

100%

) Your two most successful strategies to encourage on-time repayment

	One	Two
<i>Getting another loan</i>	25%	38%
<i>Strictly attend schedule date of repayment</i>	13%	13%
<i>Say they'll have more financial burden if they don't pay on time</i>	25%	13%
<i>Stop loans to the group</i>	25%	25%
<i>Fine</i>	13%	
<i>Group pressure</i>		13%

The group members usually do when another member pays something but not the whole amount she should pay

<i>Support her from the emergency fund / if she is a good member</i>	25%
<i>Group decides</i>	13%
<i>Use the Emergency Fund</i>	25%
<i>Pressure to make her pay</i>	38%

100%

Loan officers answers ...

What does the group members usually do when a member doesn't repay anything at all?	Some examples of actions
Fine/pay from EF/peer pressure	Group memebers it in front of the delinquent house till recovery (directors also visit)
Pay the whole amount from the EF, then colect the remaining amount and then through her out of the group	Individual visit to the loanee and her family members
	In the group meeting all the members will be informed about the default person and then leave to the rest to the group
Group pressure and they say they will take the savings from the defaulter...	Office will take steps against them
She should be out of the group and another person can join	Visits with SS office support/Action taked by the office.

Final points

- Given the importance of consumption smoothing for mF clients, they would be better off (from a simple financial perspective) if they can have better instruments to save. Besides, many of the “binding” expenses are predictable. However, the poorest the people the higher the inter-temporal discount seems to be...
- What seems clear is that after developing a discipline to save, they are able to value the benefits of a better planning
- A system based on trust... the trust on what the other does
- in the absence of mF, this reallocation would entail a higher cost. For this reason, reduced consumption to meet loan payments does not imply a decrease in the HH welfare since the counter-factual would likely be taking loans with other more expensive sources, such as moneylenders

Thank you!