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www.*MicroSave*.net
info@*MicroSave*.net

Dropouts Amongst Kenyan Microfinance Institutions

David Hulme, John Kashangaki and Harry Mugwanga

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MicroSave

STUDY ON DROPOUTS AMONGST KENYAN MFIS

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List of Acronyms

NCCK	National Council of Churches of Kenya
KREP	Kenya Rural Enterprise Programme
KWFT	Kenya Women's Finance Trust
LIF	Loan Insurance Fund
SHG	Self Help Group

MicroSave

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1 INTRODUCTION

1.1 Background to the Study

As a result of the Africa Conference on "Savings in the context of Micro-finance" held in February 1998 in Kampala, UNDP and DFID have started an initiative to promote savings for poor people in Africa. As a part of this initiative, two action oriented research assignments were commissioned by ***MicroSave*** in East Africa. One would focus on the use and impact of savings by poor people and other would focus on the reasons for high dropout rates in East Africa. This report presents the findings of the study on dropouts in Kenya.

A major assumption guiding the study is that dropout rates in Africa are generally higher than those in Latin America and Asia for similar MicroFinance Institutions (MFIs) in the range of 40-50%. This study attempts to shed light on this as well as to identify reasons why clients exit or dropout.

More specifically, as set out in the Terms of Reference, the study examines the following:

- The socio-economic characteristics of dropouts;
- The reasons for dropouts amongst clients, including those that have switched between MFIs;
- The reasons why poor people eligible to join MFIs in the areas where they are operating choose not to; and
- The reasons why MFI clients join two or more MFIs at the same time.

Prior to examining these issues, we present a brief overview of the MicroFinance sector in Kenya.

1.2 Kenyan MFI Evolution and Nature of the Sector

The Kenyan MicroFinance industry is one of the oldest and most established in Africa. Interest in the informal sector in Kenya started as far back as the early 1970's after the seminal ILO report on employment was issued in Kenya in 1972. This report for the first time identified the informal sector as a potentially important contributor to employment and economic growth in Kenya and other developing countries.

Since then, there has been a gradual shift in interest and resources towards assisting the informal sector in a variety of ways. In the 1970's the main organisations providing credit to the informal sector were church based organisations like the National Council of Churches of Kenya (NCCK) and other smaller church based NGOs. These programmes were heavily subsidised and were ad-hoc additions to other social outreach programmes offered to the poor. Outreach was extremely limited.

In the 1980's other specialised organisations began operating. Two major organisations included KREP which started as a subsidiary of a U.S. based NGO and Kenya Women's Finance Trust (KWFT). These organisations were heavily subsidised at the time and used the integrated (credit and training) approach to assist micro-enterprises. KREP initially had a limited loan portfolio but focused more on lending funds provided by USAID and other donors to smaller organisations like NCCK, KWFT, Tototo among others.

By the early 1990's, interest and knowledge about the microfinance industry had grown substantially and the approach to the industry began to become more focused and sustainability oriented. The "minimalist" Grameen approach was adopted by most MFIs and other ancillary activities like training were either stopped completely or spun off into separate programmes. A few specialised, product based institutions began to emerge in the sector as many church based organisations died out or collapsed due to lack of funding. The most prominent institutions that emerged were KREP, KWFT, PRIDE, FAULU and increasingly other institutions like NCCK and CARE-WEDCO. All of these institutions continued to be reliant on donor funds although KREP has been licensed as a bank and is scheduled to operate as a commercial institution. The focus of these institutions has gradually changed from emphasis on the very poor to the enterprise poor as the demands on these institutions to become financially sustainable has increased.

1.3 The MFIs studied

The consultant obtained information from the following MFIs:
1. Kenya Rural Enterprise Programme
2. Pride Kenya
3. NCCK-Small Scale Enterprise Division
4. CARE-WEDCO
5. Kenya Women Finance Trust

It should be noted that different institutions provide information to varying degrees and this is reflected in the findings presented below. The consultants visited groups from the institutions in the following locations:

Table 1 MFI INTERVIEW LOCATIONS

MFI	GROUP LOCATION
1. KREP	Nairobi, Nyeri
2. KWFT	Nairobi, Nyeri
3. NCCK	Nairobi, Nyeri
4.CARE-WEDCO	Western Kenya
5. PRIDE	Thika

In addition to reviewing secondary data and relevant reports (limited in number), a total of over 25 groups with a current membership of over 500 were visited in various locations around the country. Efforts were made to interview both urban and rural based groups in order to get a varied perspective. In addition, detailed discussions were held with credit officers and other key informants knowledgeable about MFIs. As we only interviewed a few groups per MFI, the results relating to each MFI cannot be taken as statistically significant. However, the overall trends established for the aggregated MFI data is in our view a reasonably accurate reflection of the reality on the ground.

1.4 Financial Services and Poor People in Kenya.

There is ample evidence in various studies carried out in Kenya that poor people have limited or no access to formal financial services. The 1995 GEMINI study for example found that 90% of micro and small enterprises in Kenya have never received credit (see table below). Since 45% of Kenya's population lives at or below the poverty line, this implies that a significant proportion of the population do not have access to formal financial services. They rely largely on informal mechanisms such as merry-go-rounds, family and friends at the lowest end and NGO, church groups and SACCOs at the upper end respectively. Except possibly for the Kenya Post Office Savings Bank, banks in Kenya have not paid much attention to the poor. NGOs have made efforts to act as intermediaries but thus far their outreach is limited to densely populated urban and rural areas.

Table 2 Sources of Credit to Enterprises

Sources of Credit	Percentage
None (no credit received)	
ROSCAs	5.0
Formal Credit Institutions	3.2
Family Members	2.0
Bank Overdraft	0.2
Money Lender	0.1
Other Sources	0.5
Total	100.2

Source: Gemini 1995

As a further indication of the limited penetration of credit services, out of the ten poorest districts, the leading MFIs have a presence in only four (see table below). In some districts like Isiolo, Samburu and Makueni, other organizations like Action Aid and World Vision provide assistance.

Table 3 MFI Presence in Kenya's Poorest Districts

District	% of Absolute Poor (Adult Equivalent)	MFI Presence
1. Marsabit	88	KREP (Pilot)
2. Samburu	84	-
3. Isiolo	82	-
4. Makueni	76	-
5. Turkana	74	-
6. Tana River	72	-
7. Machakos	69	KREP (PRIDE)
8. Mandera	68	
9. Kilifi	67	KWFT, NCCK
10. Embu	63	KREP, KWFT, NCCK

Source: Office of the Vice President: Poverty in Kenya 1997

2 WHO DROPSOUT AND WHY

2.1 Defining Dropouts

Although no distinct definition of dropouts was found, all the MFI credit officers interpreted dropouts as individuals that leave the programme either voluntarily or through coercion. No distinction is made between dropouts that are asked to leave due to illness, migration or other factors. There also appeared to be no distinction between dropouts that leave the programme "to rest" and then return, and those that leave permanently.

The former category is interesting and existed in most of the groups visited. Individuals were either attending meetings on a regular basis to pay their savings but not taking a loan or had dropped out temporarily, withdrawn their savings and were planning to return at a later date. The latter situation often occurs because the MFIs have adopted a fiercely pro-credit policy which discourages members from remaining in the groups if they are not taking out a loan (see box below). As one credit officer reported, "Credit officers are required to maintain 250-300 clients" and to achieve certain loan disbursements targets; there is pressure to encourage clients to take new loans even if they are not absolutely necessary to the client". Members that are not taking on new loans are actually a burden to the organisation and are encouraged to leave and then return when they want a loan.

The results of this "leaving", "resting" and "returning" is that many dropouts are short-term dropouts and lead to a significant overstatement of the number of dropouts.

Box 1 You Take A loan or Get Out

Most MFI's in Kenya have a very strong emphasis on credit but some are getting into the position where clients are virtually forced to take loans. This is partly because of the MFI's needs to pump out loans to achieve operational sustainability and partly due to a belief that loans are good for small entrepreneurs – even if they don't want them!

At one meeting we attended, of a group of 25 women who had been clients for 10 months, the three women in the group who had not taken loans were asked to stand up by the business development officer and explain why they had not taken loans. The implications were quite clear – they were letting the group down even though they had excellent savings and attendance records.

Another business development officer told us, " once you have savings and don't take a loan then I tell you take a loan or get out". There was even a suggestion that members who do not really need a loan should take a loan of the smallest size available and deposit it in a SACCO (Savings and Credit Cooperative).

This fiercely pro-credit culture may work while levels of competition are low and women place a high value on the benefits of being in a group . If competition develops it will become very vulnerable.

2.2 Data on Dropouts by MFI

Data on dropouts, was provided by two out of the five organizations that we worked with and is presented in Table 4 and 5 below. The consultant did note, however, that although three out of the five MFIs visited collected dropout data systematically, it was not used as an integral part of their management tool to assist in developing new products and services and containing default rates. Although credit officers were supposed to indicate the reason for each dropout in the membership book this was hardly done and even when it was done, there was no indication that senior management were fed with this information or that this information was entirely accurate.[1]

[1] In many cases the reasons cited were simply "voluntary exit" or "indiscipline" without significant probing as to why they leave. In many cases individuals leave due to frustration with the programme requirements or to join other programmes even if they do not explicitly state it.

Table 4 KWFT Dropouts Data

REGION	Dropouts		Members		Dropout rates %	
	97	**98**	**97**	**98**	**97**	**98**
Nairobi	-	75	1283	3107	-	2.4
Coast	255	996	3529	3385	7.2	29.4
Mt. Kenya	335	534	2025	4202	16.5	12.7
Rift Valley	-	107	-	927	-	11.5
Consolidated	590	1712	6837	11621	8.6	14.7

The data for KWFT shows a rise in the dropout rate from 8.6% in 1997 to 14.7% in 1998. The large increase at the Coast can be attributed to the effect of the Likoni clashes in late 1997 and the general economic downturn at the coast. Very low dropout rates in Nairobi can possibly be explained by strict policies introduced in 1997 after a particular branch experienced heavy dropouts in 1996.

Table 5 KREP Dropout Data

	Dropouts	Members	Dropout rates %
1997	1208	10956	11.03
1998	2827	13201	21.42

The data for KREP shows a significant increase in the number of dropouts between 1997 and 1998 with the dropout rate almost doubling from 11% to 21.4%. A major reason for this was the change in policy adopted by KREP to limit increases in loans and loan sizes (See box below). A large number of dropouts occurred in the third quarter of 1998 when dropouts rose considerably in all branches

The data provided by these two institutions appears to suggest that dropout rates are not as high as originally thought for key MFIs in Kenya. These findings however cannot be generalised for all MFIs in the country as we noted significantly higher dropout rates in some of the other MFIs studied (PRIDE, NCCK and CARE-WEDCO). In our discussions with credit officers we got mixed views on the relative importance of dropouts. Some felt that dropouts were not a major problem at present while others felt that there was need to pay much more attention to the issue. Two MFIs in particular have been experiencing a high dropout rate and defections to other MFIs because they are experiencing a cash/credit squeeze and are unable to disburse loans or pay out the LIF to clients quickly and efficiently.

The data from both KWFT and KREP does seem to suggest how naïve it is to discount dropout rates as insignificant as small changes in either policy (KREP) or the economic environment (KWFT) can drastically effect the dropout rate. Dropout rates for both KWFT and KREP increased by over 10% between 1997 and 1998 for different reasons as explained above.

Box 2 KREP - Drifting Up and Shifting Down

In the mid-1990s KREP allowed its clients to rapidly expand their loans by a policy of the automatic doubling of loan size for those who repaid on schedule (or ahead of schedule). This encouraged relatively wealthier people to join and, after a few cycles, take out loans of KSh. 200,000 - 500,000 (US $ 3,200 - 8,000). Poorer group members began to dropout, as they were concerned about guaranteeing such big loans, and so KREP's clientele 'drifted up', to the non-poor, and total client numbers fell. Just as bad, some tricksters joined KREP, took out a series of loans that they rapidly repaid and then defaulted or disappeared once they had a large loan.

To reduce exit rates and re-focus on its target group of micro and small entrepreneurs KREP changed its policy on loan size. First loans are now KSh. 15,000 (US $ 240), second loans KSh. 17,000 (US $ 275) and third loans KSh. 20,000 (US $ 325). In some of the KREP self-help groups (SHGs) we visited clients reported that wealthier SHG members had dropped out now that they could not rapidly develop a credit record that would give them access to large loans.

This experience illustrates the way in which product design influences client bases and dropout/exit structures. Rapid access to large loans encouraged well-established entrepreneurs (and some fraudsters) to join KREP while poorer clients dropped out. Scaling down loan size growth allowed KREP to 'shift down' to its target group but increased the rate at which relatively wealthier members exited.

2.3 Dropout rates and patterns

In order to identify specific patterns in dropout rates, ideally one needs time series data for at least eight to ten years. This was not available to the consultants. Using the data we had for KREP and KWFT for two years, we were not able to establish any specific patterns for dropouts. Credit officers did inform us, however, that dropout rates tend to be highest during the first few loan cycles. One group informed us that "in the past five months 6 members have joined and dropped out ". Another credit officer informed us that "skimming, normally occurs during the first eight weeks of savings … normally during this period some dropout either because they are unwilling to continue or because they are unable to save regularly".

Data from one credit officer with dropout information for four groups over a period of seven loan cycles appears to corroborate these findings. 45% of all the dropouts occurred during the first two loan cycles and 70% during the first three loan cycles (see table below).

Table 6 Dropout Data from 4 KREP Groups

Loan Cycle	**1**	**2**	**3**	**4**	**5**	**6**	**7**
# of Dropouts	23	40	33	15	19	5	2
% of Total	16.7	29.2	24	10.9	14	3.6	1.5

We found this pattern occurring in a number of cases during the course of our discussions with groups and individuals. A group would start off large and very quickly whittle down during the first 2-3 loan cycles until the remaining members were comfortable with each other and "reasonably willing and able to comply with group requirements". In some cases, groups would either completely disintegrate (see box below) or whittle down to a very small number.

Box 3 A Group on the Verge of Disintegration

One group we met was on the verge of disintegration. The group was a rural group based about 15 km. outside of Nyeri. The meeting we attended had only 10 present out of a total of 27 registered members. Three members were defaulting on their loans and had not attended the meeting. None of the present members knew where they were. One member had not been seen for the past three meetings. The group had already paid a significant amount to cover for these members and were finding it difficult to continue paying as the amounts were quite large (Ksh. 20,000). In addition 8 other members were threatening to default on their first loans and wanted to access their savings in order to "balance out their loans". The credit officer was adamant that all the loans had to be fully paid up before these members could access their savings. In addition, the credit officer advised them that if they did not pay back, or get the loanees to pay back, the outstanding loans within the next few weeks, the group would have to stop operating.

The group explained to us that many of the initial members of the group did not have legitimate businesses. They had been "heavily recruited to join the scheme" without adequately understanding the implications and without even undergoing a proper appraisal by other members. Some members did not even own their own businesses and were actually employees! According to the group many of them did not know each other when the group first formed even though they were "supposed to guarantee" each other. In this case the group solidarity concept broke down and individuals encouraged by credit officers eager to expand their loan portfolio were accepted into the group just to ensure that the "group of 30" requirement was met.

One group encountered had only fifteen members, eight of them had developed a very good rapport with each other and their businesses had all prospered over time. They had found it difficult to recruit new members as the group matured but they were still very keen to remain with the MFI (see box below).

Box 4 A Group of Successful Entrepreneurs in Nyeri, Kenya

KREP group in Nyeri started in 1995. It has shrunk from 30 to 15 (4 women and 11 men) of whom 8 were founder members. These 8 have all prospered: all of them now own cars and most of them are operating two businesses. They are recruiting new members but find it hard as '…we do not want the micros [micro entrepreneurs] as they have problems with repayments…but it is hard to recruit people like us as most of them say the KREP first loan is too small to bother with'.

Why do they stay with KREP? They report that '…getting loans from banks is too hard…you have to pay lawyer's fees, land valuation fees etc. which costs a lot…and it takes a lot of trouble'. They have also set up a merry-go-round with weekly contributions of KSh. 5,000 (US $ 80) each. In addition, there is great camaraderie between the 8 founder members and this creates an opportunity for them to meet each week.

One female member has recently joined KWFT. She wants to '..test it…' and hopes to access more credit by being a member of two MFIs. She and her husband run several businesses and find credit a constraint on business growth'…the repayments are not a problem…our problem is getting enough credit to finance our businesses.'

In addition to ignorance or the desire to exploit the scheme, one major reason why large numbers drop out in the first few cycles clearly relates to the methodology which puts pressure credit officers to maintain a minimum group size and to ensure that their client and loan disbursement levels remain at minimum prescribed levels. This is bound to affect the "quality" of the loan recipients and group cohesiveness. One credit officer informed us for example that for their region, they must reach 6,000 clients by the end of the year (from less than 3,000) with a target disbursement of approximately KSh. 120 million (five times the disbursements in 1997). For individual credit officers this implies that "if they drop 3 clients, they must recruit 3 to ensure zero dropouts and targets for client intakes are met". In other words the "new are supposed to replace the old" without really estimating the cost of losing the old in terms both time and disruption to the group harmony and process.

2.4 Reasons for Dropping out

2.41 General Findings

In order to assess the reasons for dropouts we used a variety sources including: detailed focus group discussions with group leaders where we asked them to provide reasons for each dropout over the past year (or more) and detailed interviews with credit officers, individual group members and actual dropouts themselves.

We found, as might be expected that the reasons for dropouts are varied and complex and depend on a variety of different circumstances and experiences. A significant number of dropouts occur because individuals are either unhappy with or unable to comply with the programme requirements. Dropouts also occur for reasons beyond the individuals' control such as illness or migration. In other cases individuals are forced to leave either because they are unable to keep up with payments or they disagree with credit officers/group members. Reasons for dropouts also vary by socio-economic status, region (urban vs. rural) and by loan cycle as will be highlighted later in this report.

A quantitative analysis of our interview data supports our assessment of the complexity of the reasons for dropouts. The analysis presented below is based on our visits to eleven different groups in Nairobi and Central province. As mentioned earlier, the groups were from four different MFIs - KREP, KWFT, NCCK and PRIDE. Although the policies and procedures vary, all these organisations follow an adapted version of the Grameen Bank methodology and it is therefore possible to analyse them as a group. Because the CARE WEDCO methodology is so different, and detailed interviews were not carried out by the consultant, this institution is not included in the analysis.[2]

Although the data cannot be said to be statistically valid, it does give a reasonable idea of the issues and reasons why dropouts occur. We have also included data from a 1996 study by KREP, which is a useful basis for comparison. See table below:

Table 7 Reasons for Dropouts

Reason (given or derived)	**Number (%) Affected**	
	MicroSave	**KREP**
Business Failure/unable to pay	12 (19.4)	94 (38.7)
Indiscipline (absenteeism, loan diversion)	11 (17.8)	51 (20.8)
Fraud/group conflict	8 (12.9)	24 (7.3)
Programme policies	19 (30.6)	18 (7.3)
Illness	4 (6.5)	11 (4.5)
Migration	3 (4.8)	21 (8.6)
Voluntary/no reason	4 (6.5)	-
Social problems	-	9 (3.7)
Found wage employment	-	7 (2.8)
Legal/ political problems	1 (1.6)	3 (1.2)
Others	-	7 (2.8)
Total	**62**	**245**

[2] Our general finding for CARE WEDCO was that the organization has undergone vast changes in leadership and policies over the past two years. The focus has shifted from building independent sustainable village banks to one that will develop the core institution WEDCO as a sustainable organization. As a result the organization has been keen to shed off poor village banks in remote areas and recruit new ones. The dropout rate has therefore been high particularly in older groups, but it has not been recorded systematically by CARE. CARE state that group sizes averages are 25 and yet the consultant observed that on average groups did not have more than 10-15 members.

The main reasons for dropouts in the ***MicroSave*** data are programme policies, business failure and indiscipline in that order. Surprisingly, our data seems to suggest that a lot of people are leaving the groups due to the structure of the programmes themselves. Out of the 19 that left in this category, 7 left to access their savings and returned to the group, 6 left because the loan size was too small, 4 left because of programme inefficiencies and difficulties accessing their LIF and 2 left because they were employed and therefore ineligible for a loan. In addition, some of the individuals who left because of poor attendance (classified as undisciplined above) actually had good businesses and are able to pay back their loans; they were not however able to attend meetings regularly as one had a bar and slept during the day and the other a transport business and therefore travelled a lot. Their "indiscipline" therefore had more to do with the structure of the programme than their desire not to participate.

These findings are different from KREP findings, which found that programmatic reasons were not a major reason for dropouts. Based on our data, it would appear that improvements or restructuring of programme policies may reduce group turnover. Each MFI however will need to look at the pros and cons of any modification as some of the dropouts are actually occurring due to very clear programmatic changes by some MFIs. KREP for example has reduced its initial loan size and become stricter on the size of loan increments. This has in effect resulted in dropouts by individuals interested in larger loans (see box 2 for example).

Although not adequately captured in the quantitative analysis above, in addition to the reasons cited above, we also found that a significant number dropout to "rest" or access their savings and then return (see box below). In one case, we encountered a group that had been fairly cohesive since they started five years ago (25 of the current 29 members were founder members). Seven of these had actually dropped out at one time or another to access their savings and then returned at a later date (see case study in the appendix).

Box 5 Interview With A Credit Officer in Nyeri

This Credit Officer gave us a number of reasons why individuals dropout based on his experience:

- Some are **forced out** by group members due to bad character or poor loan repayments;
- Dropouts also occur when the individual fails to comply with group requirements; attendance, meeting welfare needs, making merry go round payments etc.
- Some exit voluntarily due to a change in business location;
- There are also exits from individuals that would like to remove their savings and then rejoin the group starting at the smallest loan size again. These individuals leave largely because their businesses cannot absorb a large loan so after a few loan cycles their savings become almost the same or more than the loan and in their view it makes more sense to "balance out" than to borrow and pay interest for "their own money". For example, after four loans, an individual has accumulated Kshs. 17,000, which is more than the original loan size of Kshs. 15,000. .Some individuals prefer to access their savings "rest" and return later .

2.42 Socio - Economic Position and Dropouts

We did not find any distinct correlation between socio-economic status and dropouts as both the poor, not so poor and upper poor all drop out. Out of thirty recorded cases of the characteristics of dropouts eight (27%) clearly came from lower income members and ten (27.5%) from higher or medium income earners (see table below).

Table 8 Characteristics of Dropouts

REASONS FOR DROPOUTS	SEX	BUSINESS CHARACTERISTICS	INCOME LEVEL DERIVED[3]
1. Business Failure	F	Butchery, single woman	Low
2. Poor Attendance	M	Headmaster, wife running business	Medium
3. Change of Programme Policy	M	Well off hardware	Upper
4. Poor Business	F	Hair salon	Low
5. Poor Attendance	M	Good transport business	Upper
6. Poor Attendance	M	Bar business	Upper
7. Poor Payment	M	Milk bar	Low
8. No Reason	M	Sells clothes-business continues	Medium
9. Illness	M	-	-
10. Illness	M	-	-
11. Business Collapsed	M	-	Low
12. Programme Rules	M	Restaurant, doing well	Upper
13. Business Closed	M	Family business, poor management	Upper
14. Unwilling to pay Municipal License	F	Market trader	Low
15. Employed	F	-	Medium
16. Employed	F	-	Medium
17. Migration	F	-	-
18. Business Failure	F	-	-
19. Distance	F	Hardware, small child, no transport	Medium
20. Fear	M	-	-
21. Unable to Pay	F	Salon	Low
22. Unable to Pay	F	Market sales person	Low
23. No Time	M	Business ongoing	Medium/ Upper
24. Voluntary	M	Barber, business on going	Medium/ Upper
25. Illness	-	-	-
26. Migration	-	-	-
27. Migration	F	-	-
28. Voluntary	F	-	-
29. Illness	F	-	-
30. Business Failure	M	Retail shop, many problems	Low

Source: Field Data

While the data may suggest that dropout behaviours are the same for all groups, our qualitative research, suggested that poorer and wealthier group members find MFI products less attractive than 'average' clients, and are thus more likely to exit. The KREP experience (see box 2) illustrates this well and shows

[3] Please note that these income levels are derived from our assessment of the business and social characteristics of dropouts and our knowledge of the economy. They are to be used as a guide and not seen as 100% accurate.

the way in which product design determines who an MFI works with and who exits. When KREP policy favoured large loans many poorer members voluntarily withdrew from KREP. By contrast, when loan sizes were reduced then wealthier members decided to exit. Interviews also revealed the ways in which personal preferences and circumstances shape exit behaviour. Both relatively wealthy and relatively poor dropouts complained that solidarity group meetings were "a waste of time" when they had better things to do and cited this as a reason for dropping out. By contrast, a small number of other clients, both wealthier and poorer, reported positively on group meetings as an occasion to meet up with friends ... "the best thing that happens each week".

Upper Income Dropouts

Upper/higher income group members largely drop out because they find the meeting requirements onerous or because the loan size is too small to meet their requirements. Some move to other MFIs with larger loans, others try to "straddle " between two MFIs while others dropout out completely. In group after group that we interviewed we heard the same story of people leaving due to frustrations with meetings, small loan sizes and strict programme policies. In one case a client wanted to send his wife because he was too busy, but this was not allowed. In another case we heard of a truck owner in the transport business that was ready, willing and able to meet his weekly payments but unable to attend meetings because the transport business requires a "24 hour commitment" otherwise it collapses. He eventually was asked to leave the group even though his business was doing well.

Medium/Not so Poor Dropouts

These form the bulk of those that remain in the groups and benefit most from the solidarity group methodology. Many of these dropout to "rest" from loans and access their savings. Some drop out in the 2nd, 3rd and the 4th loan cycles as the size of the loans taken cannot be supported by the business. Some eventually return and resume borrowing at significantly lower, more manageable loan levels. It should be noted that many of these business are operating just above the poverty line and when the economy /business is doing well, they are doing well, when there is a downturn or shock such as illness or death, they are liable to slip back into poverty and either dropout or request significant assistance from their solidarity group members. A number of groups visited have established emergency funds to assist members to deal with these kinds of shocks. The fund amounts vary depending on the maturity and income levels of group members and in some cases are liable to abuse. One group we visited was involved in a two hour discussion and eventually resolved not to give out any more funds from the emergency fund until members with amounts due outstanding paid back what they owed. MFIs themselves do not have any direct policies or procedures to deal with individuals facing emergency/crisis situations and those that drop-out as a result have to rejoin the group as new members. For some businesses that left in their 5th or 6th cycle, this is a frustrating experience as the starting loan amount may be significantly less than their business requirements (see box below).

Box 7 Dropout Returnee to a Group

Ephantas is a small market trader in Nyeri town. He has been in a KREP since 1994. He has taken out 5 loans with the group, his highest being KSh. 150,000 (US$ 2,500). When he had about KSh. 8000 left to pay on his 5th loan he fell ill and had to go to hospital. As a result, he was forced to exit the group and use his savings to pay off his loan. He has now rejoined the group, but has to start borrowing again from the minimum balance (KSh. 15,000) and work his way up again. Since KSh. 15,000 is very little for his current business needs, he is frustrated and is thinking of leaving the group. Ephantas recommends that micro credit organizations have an extension or rescheduling policy to facilitate individuals that face major emergencies.

Lower Income Dropouts

Lower income members are most vulnerable to external shocks like illness, death, drought etc. as they have limited other assets or resource bases to turn to for assistance. Their level of exposure to the vagaries of business is also limited and they often lack basic business skills and know-how to turnaround the business in times of difficulty. Many of these businesses exist in rural areas although a substantial number are urban based as well. Most of these dropout after some kind of shock (external or internally induced) affects their sole means of livelihood. They then dropout unable to continue to pay their loans.

(see boxes below). Once the individual recovers they very often return to the group. Many of these individuals are women.

Box 8 Ill Health, Dropping out and Slipping into Poverty

Patricia was a member of PRIDE until 1996. She fell ill and was unable to meet the weekly savings requirements and loan payments. When she left, after taking account for her outstanding loan balance, she was given her savings. These savings helped to tide her over for a short while during her illness. Her business declined completely while she was ill in 1996 and 1997. In 1998 she got KSh. 1,000 ($15) from a friend to restart the business. Her main line of business is rope and basket weaving. Patricia is a single parent with 5 children living in the slum areas of Thika. As her business improves, she is thinking of going back to PRIDE to obtain a loan.

Box 9 Josephine The Vegetable Seller: Dropping out, Moving on, Coming back

Josephine is a successful retail trader in vegetables at Nyeri Market. She is unmarried, has one child and lives in rented accommodation in the town. She is originally from Karatina but by selling small quantities of vegetables and carefully saving at the Equity Building Society she has saved up enough to move to Nyeri and start trading in the market.

She kept her savings in KCB but heard about the KREP Juhudi Credit Scheme and she got together a group of 30 people to join in 1993. "I wanted to improve my business … this meant I could buy goods in larger quantities". She was Chairlady of the group and from an initial loan of KSh. 10,000 (US $ 160) she built up to KSh. 50,000 (US $ 800) in 1996. In that year disaster struck as she fell sick, needed medical treatment and could not do business. She 'balanced out' her loan by repaying with her savings and left the group.

In 1997 she was fit again and during 1998 she joined another MFI in Nyeri. She took one loan with this group but soon left as she did not like the way the MFI held the savings, rather than the members. She has now got together another group of 30 people and has arranged for them to join the Juhudi Scheme in the next few weeks.

2.43 Occupation and Dropouts

Based on our interviews and analysis, there did not appear to be any distinct correlation between occupations and dropouts. The businesses that are represented are quite diverse. However, the consultant noted that individuals in certain kinds of businesses particularly transport found it difficult to participate due to the onerous meeting requirements.

2.44 Gender and Dropouts

Again based on our interviews, we did not observe any direct correlation between gender and dropouts. Both men and women are equally likely to drop out. Out of the thirty cases recorded in table 7 above, fifteen were men and thirteen were women.

2.45 Age/Household Lifecycles and Dropouts

The consultant was not able to collect data on the age of dropouts. However, it was generally observed that most participants were aged between 20-40 and this has been corroborated by other studies and MFIs themselves (see Munyakho, 1996). This implies that dropouts are in the same age group.

2.46 Other factors and dropouts

In addition to the factors cited above, other reasons for dropouts came from discussions with credit officers, individuals and in the groups. These include:

- Pressure by the husband to leave or misuse loan
- Seasonality of the business
- Death

Husbands' Influence:
A critical reason, particularly in rural areas relates to the empowerment of women since husbands refuse to support their wives if they perceive that they will become or appear to be more successful than they are. In some cases, husbands, would like to actually misappropriate the loans money received and women dropout either unable to payback or refusing to take a loan afraid that they will not be able to pay it back once the husband takes it. We were told during our discussions with one group on the outskirts of a small rural town about a husband that refused to co-sign his wife's loan because he did not want her to start a business. Since this is a requirement, the woman was unable to get the loan.

Business Seasonality:
Although we did not encounter it a lot in our group interviews, several credit officers reported, that particularly in farming communities, seasonal businesses tend to dropout more often. Businesses are affected differently during different seasons in a rural economy. During droughts or poor rains, some traders in grains thrive as the prices are good. During the rainy season the opposite is true as prices are low. According to one credit officer in the Embu region:

"A lot of dropouts occur between January and September when business is low. Between September and December there is a lot of money in the economy: from coffee sales, payments for those picking tea, bonus from KTDA, Christmas etc. At other times businesses have to make payments largely from saving. Many businesses in rural areas are unable to sustain their loan payments during these slow periods and as a result dropout."

The experience described above probably applies to many rural parts of Kenya. Business incomes and performance fluctuate around the economic performance/activities of that particular region. MFI programmes are not structured to cater for seasonal business requirements.

In addition to seasonal changes in business performance that tend to affect the level of dropouts, we found that in general most rural and urban households are affected by "seasonal lump-sum payment requirements" particularly school-fees. Almost all the credit officers interviewed noted that in January dropouts tended to be high because families face significant school-fees commitments.

Death:
Again, although we did not encounter it a lot in our group interviews, one credit officer reported that 6 of her recent dropouts were all due to death.

3 WHO DOES NOT JOIN AND WHY

3.1 Introduction-Overview

A simple answer to the question, "who does not join MFIs ?" would be "almost everybody !" Despite their relative prominence in the debates about poverty reduction and outreach in Kenya, MFIs' outreach remains tiny. By late 1998 Kenyan MFIs were providing services to around 73,000 clients (see below). Assuming that all are active and poor, have an average household size of 6 and that no household is in more than one MFI, then total population benefiting from MFIs is 438,000. Given that the National Poverty Eradication Action Plan (1999) estimates that there were 12.6 million poor people in Kenya in 1998 then, in the most optimistic scenerio, some 3.5 percent of poor Kenyans are assisted by MFIs.

Table 9 MFIs In Kenya Membership (estimate)

KREP	15,000
WEDCO	9,000
KWFT	11,000
FAULU	7,000
PRIDE	6,000
NCCK	6,000
OTHER NGOs	19,000
TOTAL	73,000

*The KREP directory of MFIs lists 38 other MFIs. Many of these are small or inactive, but if we assume an average outreach of 500 clients this indicated total outreach of 19,000.

3.2 Target group and joining procedures

3.21 Target Group

Kenyan MFIs largely work with micro and small entrepreneurs who are the "upper poor" and often the "non-poor". Their major contributions are to increase competition in urban and rural town markets, help micro and small enterprises remain stable and/or expand. And in addition help entrepreneurs facing a crisis. With their present 'enterprise' focus on short-term loans based products, they have minimal impact on the poverty-reduction agenda.

3.22 Joining procedures

The joining procedures are generally the same for most of the MFIs, although these may be slight variations in the level of detail, documentation and charges required by each organization. Elements of the joining procedures include:

- Group is mobilized by a credit officer: size ranges from 10-50 and is normally constituted in cells of about 5.
- The larger groups are registered with the ministry of Culture and Social Services.
- The group opens a bank account and starts saving.
- The credit officers visits businesses
- Members pay a registration fee, buy a savings passbook
- After a period (3-5 months) more applicants are allowed to apply for loans
- Applicants are required to pledge collateral, which is authenticated by an advocate.

As the target group are generally enterprises the major criteria for joining are:

(i) that you are part of a group that is able to guarantee your loan.
(ii) you have a valid business and premises and
(iii) you are able to pledge some personal or business items as security

3.3 Reasons for not joining

We found that the major reasons for not joining the MFI programmes included:

- Group formation requirements
- Size of loans
- Meeting requirements
- Collateral requirements
- Religious and social reasons
- Fear
- Ignorance

3.31 Group formation requirements

Some individuals interviewed were reluctant to join MFIs as they felt that it was difficult to find at least four other people who they could trust to form a group. This problem occurs in urban areas where people do not necessarily know another well and in also in sparsely populated rural areas, where it is difficult to get large numbers of businesses together due to lack of transport.

3.32 Size of the loan

A number of individuals interviewed felt that the size of the initial loan being given was too low and would not benefit their businesses significantly. Most programmes typically start with an initial loan of between KSh. 10,000 – 20,000. One small KREP group that consisted of 8 fairly well off members has found it very difficult to expand its membership to the required minimum level (20) especially since KREP began its new policy that drastically reduced loan sizes and increments. According to one member " it is difficult to get people to join – the initial loan and subsequent increments are too small. Some members are joining FAULU as the loan facility there can be doubled after the first loan".

3.33 Business requirements

As MFIs target businesses with established locations or premises, this tends to prelude individuals that are either employed[4] or operate in a transient fashion (e.g. hawkers). It also precludes startups with no business premises. A number of hawkers that could actually pay back loans, do not have premises (see case below). Others are reluctant to join as they would have to pay for a business license and they are unable or unwilling to pay the amount for them is quite high (KSh. 2,000).

Box 7: Individual Not Receiving Micro-Credit Loan

Waiganjo is a young man aged between 25 and 30. He is a transient hawker who sells his goods next to the main market in Nyeri town on a very busy road. He sells his goods from a small carton. These goods include matches, handkerchiefs, thread, combs, toothbrushes and other small trinkets. Waiganjo maintains a small stock so that he can escape from the council authorities quickly and easily. Despite the transient nature of his business he has been doing it for several years and is able to make an average of KSh. 400-700 a day or between $2,200 and $3,800 per year. This is between 10 and 15 times Kenya's per capita income. Waiganjo is aware of various micro-credit schemes but is not interested in taking a loan despite his ability to pay.

He is afraid to take out a loan and would rather continue as he is. He is also unsure that he will be accepted into the programme as he does not have a permanent stall. He has two children and lives on a farm near his traditional home, about 50 Km from Nyeri town.

3.34 Meeting requirements

A number of individuals do not join because they think that too much time and effort is expended in meetings. Some do not have employees and are therefore unable to leave their businesses unattended. Others, particularly women have other social and family obligations and therefore are unable to attend meetings regularly. It appears, however that men are more reluctant to join as they perceive meetings as a "waste of time". This correlates to our earlier findings where most of the men dropout because they find the meeting requirements onerous.

3.35 Collateral requirements

There appears to be an increasing fear of joining because of the requirement to pledge personal items for security. In rural areas where the main belongings are property (land) and animals, many do not want to risk losing their source of livelihood. In urban areas, this is less of a problem and people pledge

[4] CARE WEDCO is the only organization that has a policy allowing 25% group members to be employed.

electronic items, furniture etc. A problem in urban areas is lack of trust in other group members and fear of losing personal belongings because a group member does not pay.

3.36 Religion and other social reasons

The consultant noted that in various circles, particularly a few years ago, individuals were afraid to join some MFIs on religious grounds. Some MFIs had become associated with devil worshipping and very few individuals joined. The intervention of the church in this area has helped to change this perception although it was still mentioned in some of our interviews.

Other reasons for not joining include, pressure from the family by the husband or wife. Since most MFIs require consent from the spouse on the loan application, if the spouse refuses, then it is not possible to join.

3.37 Fear

A major source of fear is ignorance of the need for and use of loans. In conservative rural communities, many do not really understand the utility and benefits of a loan programme and are therefore reluctant to join.

3.38 Ignorance

Although MFIs are present in many urban areas, there is still a lot of ignorance about MFI programmes and services. In one large slum area served by several MFIs, random interviews with several businesses on a 2 km stretch revealed that almost none of them were aware or knew about KREP, FAULU and other programmes operating in the area. A group of very poor quarry workers interviewed a few miles outside Thika were shocked to hear about credit schemes offered by PRIDE and others. Some were keen to send their wives to the PRIDE office the next day, despite their extreme levels of poverty (incomes of less than Ksh. 100. (US$1.50) per working day. Part of the reason for this could be because MFIs themselves are not keen on attracting large numbers of "undesirable" members; it could also be due to the fact that MFIs still do not have the resources/systems in place to aggressively market their products and services.

To summarise, therefore, most individuals do not join MFIs because of the structure of the programmes and products offered. Either the products exclude the individual or the individuals actually self select themselves out of the programme.

3.4 Socio-Economic position and not joining

Our general findings and observations are that the very poor do not join MFIs. These would include migrant workers, some hawkers and farm labourers among others. The reasons for this are similar to our findings on dropouts cited earlier. Very poor individuals (some hawkers, migrant workers, farm labourers etc.) are unable to meet the minimum requirements for saving, licensing their premises, providing collateral or even being included in a viable solidarity group to apply with. Many therefore choose not to join. Those that join tend to be largely the "poor" and "not so poor" individuals. The wealthy do not join MFIs as they have access to other forms of financing or, as described earlier, they exclude themselves because they do not value the onerous meeting requirements highly enough. We also noted that MFIs did not assist middle and upper income employed and self-employed individuals. MFI assistance is largely focused on the poor and upper poor as very loosely defined categories.[5]

In one group interview, we were able to have a detailed discussion and obtain their perceptions as to who benefited from various institutions. Participants were asked to rank (from 1-10) the importance and frequency of use of various institutions to various individuals based on their socio-economic status. The results are presented in the table and in our view reflect quite well our overall findings described above.

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[5] A study of KWFT clients in 1996 corroborates our observations. Using ACCION International classifications of poorest, very poor, poor, moderately poor, threshold level and non-poor they found that the bulk of KWFT clients can be classified as "poor"; 22% of KWFT borrowers can be classified as "very poor" while very few were classified as "poorest" or "non-poor" using various distinguishing proxy characteristics for income – single status, low level of education and the level and type of business. (Source: IDS, KWFT Borrower Profile, 1996)

Table 10 Socio-economic Status Vs. Institution

	VERY POOR	POOR	NOT SO POOR	WEALTHY
NCCK	0	76	1	1
KWFT	0	26	21	6
KREP	0	21	35	21
KCB	0	0	41	62
SACCO	0	0	22	33
POST BANK	0	2	0	0
BARCLAYS	0	0	38	45
MERRY GO ROUND (MONEY)	33	15	15	0
BALLOTING	1	0	0	0
FUNERAL GROUP	6	1	1	0
MERRY GO ROUND (ITEMS)	54	1	1	0
FRIENDS	31	7	4	2
RELATIVES	5	8	25	4
SHOPKEEPERS	4	2	92	10

Most MFIs are perceived to be assisting the poor and not so poor. The very poor receive assistance from merry-go-rounds, friends and relatives. The wealthy receive assistance from banks and SACCOs.

3.5 Occupations and not joining

As mentioned earlier, our perception is that those occupations that do not join are all employed workers except for CARE WEDCO, which allows a portion of group members to be employed. In the localities in Western Kenyan where WEDCO operates, the majority of employed individuals are civil servants, mainly nurses and teachers.

We did not establish any direct correlation between the kind of business establishment and not joining, although it would appear that businesses with (i) higher capital requirements such as hardware or (ii) extensive travel such as transport businesses have a higher probability of not joining. Businesses at the lower end, particularly those of a transitory nature (hawking) also have a higher probability of not joining.

3.6 Gender and not joining

Similar to our findings for dropouts, we did not find that any particular gender group was more or less inclined not to join MFIs. We did find, however, that the reasons why men do not join fall largely in the realm of dislike for the onerous meeting and saving requirements and in urban areas, scepticism for the group solidarity mechanism (see box). Women are less inclined to join either because of an inherent fear of credit or because their spouses are unwilling to let them join. Poorer women are also less inclined to join if they did not have the necessary collateral or support to take care of domestic affairs – children, daily chores etc. Both men and women at very low income levels are self excluded because of the specific business (premises, licenses etc.) requirements imposed on them by MFIs.

Box 8 Survey carried out at Kenyatta Market.

In a survey carried out at Kenyatta Market, a busy trading centre in Nairobi, we found that most shops visited had employees that did not know about MFI's. Two of the entrepreneurs that we talked to had the following observations:

1. **Occupation: Sweet vendor**
   Gender: Male

3.7 Age/household lifecycle and not joining

The consultants observed that in general, older people (above 40) did not make up and were not a significant proportion of MFI membership. No reason for this was established, however it is most likely that older individuals, either:

(i) live in more remote areas
(ii) are more active in traditional farming related activities that are not sufficiently remunerative to warrant joining an MFI.
(iii) Have reached a stage in their lives when they no longer require credit and rely on their children or other assets for sustenance.
(iv) Are unable to continue active businesses and are therefore self-excluded from MFI programmes even if they want to retain their savings (see box below)

Box 8 James' Story 'Can't I Save with the Group…. I'll Pay'

James is the Chairman of an NCCK group in Nyeri District. By the standards of microfinance in East Africa his group is in the 'rural interior' being 5 kilometres from a tarmac road and on a settlement scheme abutting the Aberdare National Park.

James is a retired teacher whose energies have helped to pull together this group of relatively poor micro-scale traders, dressmakers, mechanics and shoe repairers. However, last month he was evicted from the small shop that he runs in a nearby rural trading centre as the owner wished to redevelop the site. As he is old and has a pension he does not wish to establish a new microenterprise. The NCCK has told him that he will have to resign from the group as this is a microenterprise scheme and clients must have a business. Besides, as with virtually all East African MFIs, NCCK can only recover operational costs from loan products.

At the group meeting James made an eloquent plea to the NCCK credit officer - he wants to continue being a member, providing voluntary management services and making regular savings. In his own words '…can't I stay with the group I shall pay you to keep my savings'. Unless things change dramatically the answer is almost certainly going to be 'no'.

It is likely that if MFIs had other "non-business" products such as insurance or savings instruments, they might attract a larger number of elderly clients than at present.

4 WHO JOINS MORE THAN ONE MFI AND WHY

Although we did not meet a significant number of individuals with multiple membership in MFIs, several credit officers and MFI clients admitted that individuals were joining more than one MFI. The main reason was to expand the individual's capital base. According to one credit officer, "to get more capital, some don't have security to borrow large amounts from one so they take small amounts from two groups." In other cases, firms with adequate security joined more than one MFI, because the individual MFIs loan ceilings were too low to meet the firm's capital requirements.

We also found that some individuals, tempted by potential access to easy credit, joined more than one MFI. One credit officer interviewed cited this as a big problem; very often the individual ends up defaulting on at least one or both of the loans. Credit officers in several locations actively discourage individuals from taking up multiple loans and when they do, follow up closely with them to ensure that the loans (at least theirs) are paid back. In some cases informal credit reference checks between credit officers of different MFIs have been started to reduce the number of multiple memberships. This is not widespread however and in fact the consultant did not observe a significant amount of collaboration between MFIs in the areas visited.

In all cases it was reported that taking out multiple membership was a very stressful exercise for clients and one that credit officers actively seek to discourage.[6] We were told of one client who had taken out loans with two MFIs, struggled to repay and after completing payments withdrew from both groups to "rest" clearly fatigued. Evidence suggests that if individuals found an MFI that met all their needs they would prefer not to join more than one given the onerous requirements. The challenge for MFIs is to continuously monitor and adapt to the needs of their client base to allow for more of them to be **fully satisfied** with the services provided

4.1 Switching from one MFI to another

Although we did not encounter many individuals that had multiple MFI membership, we did encounter many cases where individuals switched from one MFI to another. There is increasing competition for clients particularly in Nairobi, Central Province and some parts of the coast. Clients are also becoming

[6] Clearly this is partly due to their own self interest in not assisting the "competition" but also to protect their loan portfolio as the chances for default are higher with multiple membership.

more and more demanding and (service oriented) as their choices increase. Although we have mentioned some before in the dropouts section, in principle, some of the main reasons clients switch are identified below:

- **Loan Sizes and Increments are too low:** MFIs have different policies on the initial loan amount and increases in the loan size. KREP for example has a starting loan size of KSh. 15,000 with incrementals of 25% after that, meaning that it would take a client six or seven loans to obtain a loan of more than KSh. 100,000. This might take up to three years if repayment is consistent and loans are taken continuously. Other MFIs such as FAULU have similar starting loan sizes, but have a much more liberal incremental loan policy; loan size can double from one loan to the next in the FAULU programme for example. Clients that are interested in larger loan sizes prefer to go to FAULU instead of KREP and we did find evidence of some clients leaving KREP to join FAULU. KREP believe, however, that in the long run, the best interests of the client are served by having a much more gradual incremental loan policy as it does not put pressure on the group guarantee system. They have learned this by experience as their previous policy allowed for much larger loans in a relatively quick period which adversely affected their default rates.

- **Meeting Requirements**: Most of MFIs require that groups meet weekly, however some are beginning to experiment with a slightly more liberal meeting schedule. KWFT in Nyeri requires clients to meet only once a month and has found that it is a very popular change that has attracted some clients from other MFIs. Other MFIs are also contemplating making these changes as well in the region in order to retain clients.

- **Slow Loan Disbursements**: Some MFIs have less access to capital and have been unable to meet the demand for loans from other members. This has resulted in them losing clients to other MFIs.

- **Degree of Access to the LIF/Savings**: The consultants were informed by some groups that clients were leaving to join other MFIs when they discovered that it was taking long to access their Loan Insurance Fund. One MFI in particular holds the LIF in its own account which is different from other MFIs that allow groups to bank the LIF in their own accounts and access it upon approval by an MFI credit officer.

- **Preference for Women Only Schemes**: According to one credit officer interviewed, women preferred to be members of "all women" groups and have actually left one MFI to join another that targets women only. The main reason for this is that women enjoy other intangible social and companionship benefits when they are in groups of their own. They are also less intimidated and able to express themselves more freely. This occurrence may be more of a rural phenomenon than an urban one where societal norms and values regarding the participation of women in business activities is more conservative.

The fact that there are so many programmatic reasons why people switch from one MFI to another implies that there is potential for MFIs to establish clear niches and develop programmes and policies to meet the needs of particular clientele. It also implies that as competition increases, MFIs that are not increasingly attentive to their client needs will lose more and more clients.

5 SUMMARY ANALYSIS AND RECOMMENDATIONS

5.1 Summary Analysis

In summary therefore, we can conclude the following:

- Based on the information received, the drop-out rate in Kenya is still quite high and has the potential to grow even more as it is sensitive to both programme changes and the performance of the economy at large. Although most of the MFIs are collecting data on dropouts it does not appear that it is being used at a policy level to influence changes in products and policies.

- At the field level there have been efforts by credit officers to innovate and improvise methodologies to attract clients albeit at a limited level. The pressure on credit officers to achieve sustainability via high loan disbursements is forcing them to push endlessly to expand their client and loan portfolio base. This implies a certain "ruthlessness" towards members that are not borrowing and therefore a bias towards "new" clients that will borrow as they push out older clients interested more in saving. There is almost a "laissez faire" attitude towards dropouts amongst credit officers as long as they can recruit new ones. The implicit cost of allowing members to dropout in terms of lost time and disruption to the groups has not been registered effectively by many MFIs.
- The consultants did establish that dropouts tend to be highest during the first few loan cycles; we also found that seasonal patterns in rural areas do affect the performance of businesses and the level of dropouts during particular months.
- The reasons why drop-outs occur vary, however, the main ones identified include programme policies, business failure, indiscipline, fraud/group conflict, voluntary exit and illness among others. In our analysis it appears that the structure of various programmes has influenced the drop out rate significantly.
- Different socio-economic groups drop out for different reasons. Wealthier participants dropout either to access more funds or because they are tired of the onerous meeting requirements. Poorer members drop-out largely because they are unable to cope with business or personal shocks such as illness or death and as a result are unable to continue to meet the loan requirements. Average members tend to dropout either to access their savings built up over a period of time or to "rest" and return at a late date. Others are tempted into taking larger loans which they find difficult to pay back resulting in them being forced to dropout.
- Those that don't join MFI programmes include the very poor, employed workers at all levels and the elderly.
- Individuals join more than one MFI for various reasons, but the main ones include to expand their capital base, or switch to other MFIs to take advantage of various aspects of a particular MFIs programmes and policies such as larger loan sizes, less frequent meetings, women only groups, easy access to the LIF etc.

5.2 Recommendations

Based on the assessment above, we recommend the following:

MFIs should develop new products to meet clients needs: The fact that so many dropouts occur for programmatic reasons implies that there are significant opportunities for MFIs to redefine their current programmes and policies to meet client needs. In addition, there are also opportunities for product development in a variety of areas to meet specific client needs. Consideration should be given to the following areas:

- Meeting requirements
- Schemes to cater for seasonal businesses
- The size of the loan and increments to subsequent loans;
- Gender segregated groups;
- Emergency loan provisions; rescheduling options;
- Loans for 'employed ' persons with businesses;
- Group size requirements reconstituted to suit varying urban and rural needs;
- Easier access to the LIF without having to exit the programme;
- Insurance and emergency schemes

MFIs should Develop Long-term institutional capacity for product development: In line with the recommendation above, we also noted that none of the MFIs have well integrated system for tracking for tracking the number of dropouts, the reasons for dropouts and relating that new product development. At present MFIs appear not to be too concerned about loosing clients as the perception among credit officers is that they can go out and recruit another one. The cost and benefits of this appear no to have been analysed in detail. As competition increases it will be increasingly important to RETAIN clients and to have a very keen understanding on the demands and needs of clients**. MFIs are also not taking advantage of the significant knowledge and resource base already existing with the credit officers. They need to be consulted more and given more leeway to develop programmes**

and policies that will facilitate greater client retention. Several quotes from Bill Gates manager of one of the most successful companies in the world, on the importance of tracking bad news is illustrative of how even the best companies are forced to understand the needs of their clients.

"an important measure of a company's digital nervous system is how quickly people in the company find out about bad news and respond to it."

"learning from mistakes and constantly improving products is key in all successful companies. Listening to customers is a bigger big part of that effort."

"focus on your most unhappy customers."

"gather rich information on their unhappy experiences with your product and find out what they want you to put into their product."

Although it may appear that there is still significantly room in the market for all players, the speed at which this can change can be quite dramatic. The implications and impact of KREP entering into the market as a fully fledged financial institution has yet to be analysed in detail and yet they are likely to have the wherewithal and resources to draw away a significant client base from other MFIs unless these MFIs also begin to think about ways to maintain a competitive edge in certain market niches.

- ***MicroSave*** should fund practical product development pilot activities for MFIs in Kenya. MFIs assisted should be those that may not necessarily have the resources to develop long term product capability.
- Given that so many of the very poor and even upper poor do not have access to financial services, there is need for donors, practitioners and others interested in poverty eradication to think about additional methodologies and approaches to reach the poor. Contrary to the experience in Bangladesh, the Grameen approach which has been applied in Kenya has not been sufficient to reach the vast numbers of poor and very poor in need of assistance.

APPENDIX 1 LIST OF PERSONS AND GROUPS INTERVIWED

1.	Aleke Dondo	KREP
2	Ben Nkungi	NCCK
3.	Dagoretti Amani Group	KREP
4.	Hapa Kwa Hapa group	KREP
5.	Jikaze Group	PRIDE
6.	Mwitamania Group	PRIDE
7.	Hawkers Group Member	KREP
8.	United Group	KREP
9.	Amboni Group	NCCK
10.	Urumwe Self Help Group	NCCK
11.	Abundant Faith Group	KWFT
12.	Mongozo Self Help Group	NCCK
13.	Border Self Help Group	KREP
14.	Mathena Vision	KREP
15.	Christine Midia	Credit Officer, KREP West Nairobi Area Office
16.	George Odhiambo	Branch Manager, PRIDE Thika
17.	Juliana Muthoka	Credit Officer, KREP Nyeri
18.	Mr. Kariuki	Branch Manager, NCCK Nyeri
19.	Peninah Mwangi	Regional Credit Officer, KWFT
20.	Martha Murage	Nyeri Credit Officer, KWFT
21.	Lucy Kavinda	Nyeri Credit Officer, KWFT
22.	Rosemary Macharia	KWFT, Nairobi
23.	Thenya Mule	KREP
24.	Kimondo Karanu	PRIDE
25.	Mrs. Bungu	KWFT
26.	Mr. Harry Mugwanga	Micro-finance Consultant; visited up to 20 Care-WEDCO groups in Western Kenya

APPENDIX 2

METHODS USED

The research team used a variety of quantitative and qualitative methods to carry out the study.

Quantitative Methods

- The team entered drop-out records from MFIs into the computer and analysed them to look for trends, seasonal variations, variations by cycle, etc.
- In addition the team analysed some of the field data collected quantitatively in order to assist in our overall assessment and to substantiate qualitative data where possible.

Qualitative Methods

- Key informant interviews were conducted with the managers and front-line staff of the participating MFIs.
- In-depth interviews were conducted with clients, dropouts and non-clients of the MFIs in the catchment areas where the participating MFIs were operating.
- The team conducted extensive focus group discussions with clients and non-clients of the MFIs in the catchment areas where the participating MFIs were operating.
- Participatory Rapid Appraisal techniques were also used.

Approximately 500 people were interviewed.

APPENDIX 3 CASE STUDIES

GROUP CASE STUDY:1

Name of Group: Hapa Kwa Hapa Group

Funding Agency: Kenya Rural Enterprise programme (K'REP)

Year Group Started: 1993

Starting Membership: 36 **Current Membership**: 23

Characteristics of the Group
The group since inception has been predominantly male. Current membership includes 20 men and 3 women. The group is located in an urban slum area in Nairobi called Kawangware. Members of the group can be classified as upper poor.

Dropouts: Since April 1998 the group has lost 7 members. The reasons for dropping out are presented in the table below:

Member Characteristics	Reasons for Dropout
1. Single woman , butchery	Business failure
2. Headmaster, poor attendance	Voluntary
3.Good business hardware ,male	Needed larger loans
4. Woman, hair salon	Business failure
5. Man, good transport business	Unable to attend
6. Male, bar	Unable to attend
7.Milk bar, male	Unable to pay

Other Issues:

- According to the group no defaulter left with a loan balance to pay. The group encourages members to pay their loans until the savings are enough to offset the loan balance.
- Members are requested that grace period to be introduced and the duration for paying of large loans be introduced. The current maximum period is one year.

GROUP CASE STUDY 2

Name of Group: United Group, Nyeri

Funding Agency: KREP

Starting Membership: 30 **Current Membership:** 15

Characteristics of the Group
The group consists of small formal businesses in established locations. Businesses include electronic shop, clothe boutique, laundry, spare parts business, transport business among others. There are still 8 founder members in the group. These have established quite a strong bond. Group members could not be considered as poor although some may have graduated from upper poor. Almost all members of the group owned a car.

Dropouts: Over the past year there have been 2 dropouts: one member left voluntarily as he could not get along with other members and another member's business failed so he left the group.

Since the groups inception it has experienced significant turbulence at one time loosing 22 members and leaving only 8. Reasons for leaving include default, fraud, business closure and indiscipline. A major reason for this is that at group formation, many members did not know each other. Many original members were employed and did not understand fully the terms and conditions.

Other Issues:

- The group is finding it difficult to get people to join as the initial loan size is too small and the increments are also small. FAULU for example allows the loan to be doubled.
- Between Dec. 98 and April 1999, 6 individuals have joined and left the group for the reasons cited above.
- The group has significant savings in the bank (KShs.440,000). The largest amount held by an individual is KShs. 85,000.
- The group merry-go-round is able to give loans of KShs. 25,000. K'REP's starting loan is 15,000. Members would rather take advantage of the merry go-round's better terms then the KREP loan.

Group Case Study 3-Uhuru Self Help Group, NCCK

Date Formed: 1994

Starting Membership: 25 **Current Membership**: 29

Characteristics of the Group:
The group is located in Mweiga which is a small rural Kenyan town in Central Province. The businesses are largely livestock and agriculture based and include butcheries, market traders, restaurants, hardware and retail shops.

Dropouts: This group has been fairly cohesive. Seventy five percent (75%) of the current membership are starters. Four have left. Two females could not pay due to poor business performance, one female could not meet the regular time requirements and another left voluntarily although his business is still going on.

Other Issues:

An interesting aspect of this group is that 7 of the current group dropped out at one stage or another to access their savings. They then returned to the group and started at the lowest level again. This is an indication that individuals in the group value the savings services provided.

GROUP CASE STUDY: 4

Name of the Group: Mathare Wendane, NCCK

Date Formed: 1997

Starting Membership: 29 **Current Membership**: 27

Group Characteristics
The group is based about 15Km outside Nyeri. Members however come from areas within a 4.5 Km radius from an area which has limited transport. Businesses include clothes dealers, market traders, grocery stores hair salons and carpenters.

Dropouts: Officially the group only had two dropouts. One left due to illness and one migrated from the area.

The group however was going through a process of disintegration. The meeting we attended only had 10 present out of a total of 27 registered members. Three members were defaulting on their loans and had not attended the meeting. The group was advised by the credit officer that they as a group needed to cover for the other members. The group has already paid a certain amount and were finding it difficult to continue paying as the amounts were quite a large amount (over KShs.20,000). The credit officer advised that if they did not pay back or get the loanees to pay back the outstanding loans within the next few weeks, the group would have to stop operating.

In addition to the three defaulters, there are also eight impending exits in the group. They want to balance their outstanding loans with their savings, but the loan policy does not allow this. Most of these people took their first 15,000 loans without really understanding how they would be paid back. The screening too ensures that members had viable business.

Other Issues:

- The group is finding it difficult to mobilise people in the area to join. People are scared they might lose their assets e.g. cows. Another MFI tried to penetrate this rural area and failed.

- The current group is spread out with members coming from different places within a 5 Km radius. This is quite a distance as there is limited available transport in the interior which tends to discourage attendance and is an indication of the difficulty MFI's will have using the solidarity methodology in rural areas.

- A lot of the people in the area are conservative and not used to business. Young people have left the villages and gone to look for work. Those that are left are not exposed and need to be educated on the use and purpose of loans.

- Two years before, people were afraid of MFI's as they heard it was related to devil worship. This has now subsided as the churches intervened.

INDIVIDUAL CASE STUDY 1

Individual Not Receiving Micro-Credit Loan
Waiganjo is a young man aged between 25 and 30. He is a transient hawker who sells his goods next to the main market in Nyeri town on a very busy road. He sells his goods from a small carton. These goods include matches, handkerchiefs, thread, combs, toothbrushes and other small trinkets. Waiganjo maintains a small stock so that he can escape from the council authorities quickly and easily. Despite the transient nature of his business he has been doing it for several years and is able to make an average of KShs. 400-700 a day or between $2200 and $3800 per year. This is between 10 and 15 times Kenya's per capita income. Waiganjo is aware of various micro-credit schemes but is not interested in taking a loan despite his ability to pay.

He is afraid to take out a loan and would rather continue as he is. He has two children and lives on a farm near his traditional home, about 50 Km from Nyeri town.

INDIVUDUAL CASE STUDY 2 (Mama Wanjiru Drop-out)

Mama Wanjiru sells cereals at the Karatina market. She was a member of KWFT but recently dropped out. After paying back on both loans, she decided to take a break and resigned from the group (KWFT and Faulu) to access her savings for the business instead of borrowing again. She is not yet sure she will return to the group but she may consider it in the future depending on her needs and the performance of her business.

INDIVIDUAL CASE STUDY 3

Josephine, The Vegetable Seller-Dropping Out, Moving On, Coming Back
Josephine is a successful retail trader in vegetables at Nyeri market. She is unmarried has one child and lives in rented accommodation in the town. She is originally from Karatina , but by selling small quantities of vegetables and carefully saving at the Equity Society she has save up enough to move to Nyeri and start trading in the market.

She kept her savings in KCB but heard about KREP Juhudi Credit Scheme and she got together a group of 30 people to join the scheme in 1993. "I wanted to improve my business …this meant I could buy goods in larger quantities". She was a chairlady of the group and from an initial loan of KShs. 10,000 she built up to KShs. 50,000 in 1996, however, in that year disaster struck as she fell sick, needed medical treatment and could not do business. She 'balanced out' her loan by repaying with her savings and left the group.

In 1997 she was fit again and during 1998 she joined another MFI in Nyeri. She took one loan with this group but soon left as she did not like the way the MFI held the savings, rather than the members. She has now got together another group of 30 people and has arranged for them to join the Juhudi Scheme in the next few weeks.

At the time of the interview her financial strategy was as follows:

1. KCB savings account to start earnings.

2. A merry-go-round of 25 people in which each puts in KShs. 50 per week and 3 'winners'

3. The purchase of five acres of land -not yet formed-security.

4. A life insurance policy with Madison Insurance of KShs. 1,940 per month / a friend introduced her to this.

5. A secret hiding place to keep cash.

She would prefer it if the K'REP meetings were monthly rather than weekly, to reduce the time spent in meetings and because many of her clients are salaried and settle their bills with her monthly, in arrears. Ideally she would like an MFI that would save with and borrow on an individual basis.

INDIVIDUAL CASE STUDY 5 (Mama Wangare -Potential Drop-Out)

Mama Wangare owns a retail grocery shop in Karatina town. It is a well stocked successful store and sells all kinds of basic consumer goods, bread, soap, vaseline, cigarettes etc. Mama Wangare has been a long standing member of KWFT. She has taken out 6 loans thus far, her last loan amounting to KShs. 150,000 ($2,500) although she had actually applied for KShs. 250,000 ($4,000) which was denied. Mama Wangare also has the second highest savings in the Mt. Kenya region (about$1500). In order to accommodate the growing needs of her business, she would like a larger loan, but at present KWFT's limit is (150,000). She feels she does not yet have security requirements to go to a bank. If however KWFT does not approve a larger loan amount, she is thinking of leaving the group. She also requested that KWFT begin to offer members shares in the organisation.

INDIVIDUAL CASE STUDY : 6 (Patricia Muhunge-Poor Dropout)

Patricia was a member of PRIDE until 1996. She fell ill and was unable to meet the weekly savings requirements and loan payments. When she left, after taking account for her outstanding loan balance, she was given her savings. These savings helped to tide her over for a short while during her illness. Her business declined completely while she was ill in 1996 and 1997. In 1998 she got KShs. 1000 ($15) from a friend to restart the business. Her main line of business is rope and basket weaving. Patricia is a single parent with 5 children living in the slum areas of Thika. As her business improves, she is thinking of going back to PRIDE to obtain a loan.