MicroSave Briefing Note # 3

Mobilising Savings

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Introduction

Throughout time, all around the world, households have saved as insurance against emergencies, for religious and social obligations, for investment and for future consumption. The importance the poor attach to savings is also demonstrated by the many ingenious (but often costly) ways they find to save (Rutherford 1999). But for a variety of reasons, most informal mechanisms fail to meet the needs of the poor in a convenient, cost-effective and secure manner. As a consequence, when poor households' are provided a safe, easily accessible opportunity to save, their commitment to saving, and the amounts they manage to save, are remarkable.

Savings have risen to the top of the microfinance community's agenda. Previously microfinance institutions (MFIs) viewed savings as the poor relation -- Vogel's (1984) "forgotten half" - and typically extracted savings from clients through compulsory systems. There was a prevalent and powerful perception that "the poor cannot save", thus compulsory savings systems often required members to deposit small token amounts each week and levied more substantial amounts at source from loans. These compulsory savings were then often "locked-in" until members left the organisation. Compulsory savings generate a loan guarantee fund for the MFI, but drive up the effective cost of loans. By contrast, voluntary savings are a service from which clients can withdraw and (often but not always) on which they receive interest. This note focuses on voluntary savings services.

A substantial proportion of client exit from microfinance institutions is driven by the credit-only focus of these institutions. For example, in Bangladesh clients drop out in order to (1) collect the funds from their compulsory savings accounts, (2) to access microfinancial services where their savings are available in an emergency, (3) to access enhanced services from other MFIs, i.e. ones that offer a wider range of products. East African microfinance customers also drop out to collect the funds from their compulsory savings account (Wright, 2001).

Microfinance institutions can avoid some client exit by mobilising savings from the public which can be collected profitably on a large scale. Poor people need savings services because of emergencies, opportunities (which are often unexpected), to pay for lifecycle events associated with death or marriage, and to smooth payments of their consumption needs. People do not need loans all of the time, but they do need savings all of the time. (***MicroSave***'s "Market Research for MicroFinance Toolkit" can help MFIs research and understand these issues).

Savings as a Service and a Source Of Funds For Loans

To offer credit services, the microfinance institution selects borrowers that it trusts through business assessments, character assessments, cash flow analysis, or a combination of several tools. In savings mobilisation, however, it is the customer who must trust the MFI (Robinson, 1995).

To begin the process of introducing savings services, the MFI must always conduct market research and feasibility analyses. Once these tests are completed, the institution uses the information to design appropriate high-quality services, which are then tested in pilot projects (see ***MicroSave***'s "Toolkit for Planning, Implementing and Monitoring Pilot-Tests"). The institution should publicize its instruments and services in locally appropriate ways.

Compulsory and voluntary savings are usually incompatible. However, some institutions have designed programs where a percentage or a value amount of savings are made available to customers, but once customers are allowed to remove part of their savings, they usually prefer complete voluntary savings mobilisation. Quality voluntary savings services will usually mobilise more than locked-in savings.

Savings Products

What is most important is not any particular savings product, but the combination of products available from the MFI, which each saver can customize for his or her particular needs. For large-scale savings mobilisation to be viable and to finance substantial portfolios, savings must be mobilised from the public and not from the poor alone. This makes it possible to serve large numbers of small savers profitably. While the transaction costs of very small accounts make mobilising savings from the poor expensive, the larger account sizes of the non-poor raise the average account size and permit a combination of institutional profitability and wide outreach. This cross-subsidization is the only way that the poor can be served cost-effectively on a large scale. However, such practice requires special attention to ensure that the products are attractive to all potential savers.

Cost Issues

Contrary to popular opinion, mass savings mobilisation from the public need not be an expensive source of capital. Small savings, when captured as part of savings mobilisation, can be collected at relatively low financial costs. In addition, there are synergies created through the economies of scope between savings and lending.

Products' interest rates and fees can also be used to provide:

- Incentives to build up and maintain balances
- Disincentives to withdraw
- Revenue from transactions/ledger fees

Information costs and loan loss provisions are expected to be less when MFIs can draw on the deposit histories of potential borrowers to analyse their capacity to pay and creditworthiness. It is essential that MFIs cost their products to make informed pricing decisions. Costs of new products are difficult to determine in advance, so pilot-tests are needed to estimate cost accurately. Interest and fees charged should be carefully structured to give clients a choice between products with different ratios of liquidity and returns.

Some Basic Principles for MFIs in Large-Scale Savings Mobilisation

Profitable large-scale savings mobilisation is not a matter of adding a few products to a microcredit institution. It changes the institution fundamentally. MFIs should offer only a few carefully designed savings (and other) products. Too many products make branch management too complex and expensive and many products are not necessary for most clients.

- Large-scale savings mobilisation should be limited, except in highly unusual cases, to publicly regulated and supervised institutions that are legally permitted to mobilise public savings.
- Microcredit institutions introducing voluntary savings should pay particular attention to the preconditions required and to appropriate sequencing in terms of research, product development, pilot-testing and roll-out.
- Products are necessary but not sufficient for profitable voluntary savings mobilisation from the public, as they are only one element in a much larger set of requirements (including MIS, training, marketing etc.) for the profitable large-scale mobilisation of savings.

Management, Organization and Human Resources

High quality, experienced, and committed governance and management are essential. The MFI should stop efforts to raise voluntary savings if these are not available. Management and staff training and incentives related to each step of the sequencing process are essential. Some managers and staff (especially middle managers) may object to, and in some cases refuse to implement, the necessary broad-based changes. This problem, where it arises, must be carefully and quickly dealt with (usually not easy). Because mobilising voluntary savings from the public will change the institution dramatically, management, organisation, internal supervision, liquidity management, and financial intermediation are likely to need fundamental restructuring.

Who Benefits from MFIs that Offer Voluntary Savings Mobilisation to the Public?

Clients benefit from savings services, since they need and demand the service. However, the MFI benefits too, for several reasons. First, clients are likely to be more satisfied and therefore more likely to repay their loans to maintain on-going access to the package of financial services. Second, savings provides microfinance institutions with an attractive source of capital: locally mobilised voluntary savings is potentially the largest and the most immediately available source of finance for many microcredit institutions. Small voluntary savings can result in large amounts of funds that are more stable than other funding sources. Third, the MFI receives additional income from loans made, investment of the new capital, and also from fees charged on savings transactions. The national economy also benefits as savings are brought out of the informal into the formal sector and made available for reinvestment.

References

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