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Dropouts in Northern Province, South Africa

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with fieldwork assistance from Nthenya Mule and
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Acronyms

ECI	Ebony Consulting International
FGD	Focus Group Discussion
GDP	Gross Domestic Product
HDI	Human Development Index
MCP	Micro Credit Programme
MFRC	Micro Finance Regulatory Council
MFI	Microfinance Institutions
NGO	Non Government Organisations
PRA	Participatory Rapid Appraisal
PSA	Provident South Africa
PWR	Participatory Wealth Ranking
RDP	Reconstruction and Development Programme
SEF	Small Enterprise Foundation
SMME	Small Medium Micro Enterprises
TCP	Tshomisano Credit Programme
UK	United Kingdom
VIP	Visual Indicator of Poverty

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Executive Summary

Provident South Africa (PSA) and Small Enterprise Foundation (SEF) agreed to allow researchers to look into the dropout issues at their respective institutions with a view to understanding client behaviour and reactions to institutional issues that result in clients dropping out.

In 1998, SEF clearly described the impact of dropouts on an institution:

Dropouts have the potential to very seriously damage the success of the Programme. For every member recruited a lot of staff time (and therefore…money) is invested in the training process and administration. Over time as the member takes larger and larger loans this investment is gradually rewarded and a profit is made from interest payments, which can be used to recruit new members and provide loans.

Where a member drops out the organisation is damaged in a number of ways:

1. *Loss of money: the resources invested in a new member are lost.*
2. *Loss of income: income, which would have come from the increasing loans, is lost. The larger the loan the member would have taken, the greater is the loss to the organisation.*
3. *Damage to growth: Dropouts reduce morale in the centres from where they drop. This may make other members more likely to drop, it may also make it difficult for staff to recruit new members*
4. *Damage to staff morale: high numbers of drop-outs make staff feel that they are failing or not achieving what they hope for. Low staff morale reduces productivity and leads to poor growth and more dropouts.*[1]

Both institutions recognise this, and are seeking ways to improve their products and services to ensure sustainable financial services. In the time since the research was done, PSA issued a press release that the institution was considering closure due to delinquency and default issues. They subsequently ceased operations in South Africa[2].

Dropouts are defined as clients who leave the programme before completing all the loan cycles that are offered by the MFI[3]. The dropouts can be categorised as "voluntary" or "forced" dropouts. Forced dropouts are those that may be excluded by policy from returning for another loan – for example, any client with less than a 67% collection percentage at PSA, and at SEF clients are "forced to rest" while waiting for defaulters to fulfil their loan obligations. Voluntary dropouts, on the other hand, are clients that the institution may wish to retain as clients, but who have chosen not to continue borrowing.

Among the different reasons for dropouts at these two institutions were:

- resting (dropping out and dropping back in when needed),
- rigidity of the products or policies– weekly payments and group meetings,
- family problems,
- unprofitable businesses,
- "over-trading" or very competitive environments and, to some extent,
- the leniency of the programmes towards delinquency and default.

[1] From the Development Department of The Small Enterprise Foundation "Analysis of Reasons for Drop Outs from the TCP" written by Anton Simanowitz and Nsumbulana Mtsenga, March 1998

[2] Although PSA was closed down we decided to still present this report as many lessons can be drawn from the PSA experience.

[3] This definition is used by other ***MicroSave*** studies and is quoted from the Tanzanian Dropout Study with was researched by Florence Maximambali, Christopher Lwoga and Stuart Rutherford

The above were factors in both forced and voluntary dropouts.

The MFIs each offer one loan product with varied loan terms; SEF additionally requires collateral savings that clients often look at as a second savings product. Greater choices within the loan products - for example, instalment choices of weekly, fortnightly or monthly to match client income streams - could go a long way in reducing dropouts at PSA. At SEF a change in the delivery system, which currently disallows paid–up customers to re-group and borrow could rapidly reduce dropouts. New loan products and possibly new voluntary savings products (depending on regulatory requirements) may also help retain clients within the institution, even if they are not always actively borrowing.

Greater, and clearer, communication amongst Management, field staff and clients appears to be needed in both institutions. However, some communication may need to be reduced, not increased! Clients at both institutions are well aware of the fact that they need not fear prosecution if they fail to pay. This has undoubtedly led to dropouts and write-offs. Less communication at PSA about a 67% collection rate being deemed acceptable seems in order, while more communication regarding interest rate, term and instalment changes is also in order. At SEF greater communication between staff and Head Office appears likely to increase Head Office's dissemination of policy and knowledge of client issues.

Overall, clients felt strongly about their institutions and many who had dropped out with some bitterness declared they would rejoin the institution if certain changes, as briefly outlined above, were made. PSA and SEF clients are generally self-employed and do not have a lot of choice in institutional financial services, though they certainly are spoiled for choice in the informal sector where *mashonisa* (moneylenders) thrive. With slightly different target groups and slightly different locations, it appears that both institutions have the potential to remain leaders in microfinance in Northern Province.

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1. Introduction

1.1 What is this report about and why are we doing it?

This report is about the dropout situation at two Microfinance Institutions (MFIs) in South Africa's Northern Province. Small Enterprise Foundation (SEF) is a Grameen-styled NGO-MFI that is experiencing high dropouts in its poverty-targeted programme. Provident South Africa (PSA) is a for-profit, formal sector institution operating through a network of commission-based Agents providing individual loans to small enterprise operators.

PSA and SEF were selected because they have both achieved a substantial level of outreach in the Northern Province and are aware of, and concerned about, the impact of dropouts on their profitability and long-term sustainability.

Because the institutions operate in very different ways and have widely different strategies, this report should not be read as (nor is intended to be) a "compare and contrast study" whereby one methodology might emerge a "winner"! The differences in the two institutions do provide interesting juxtapositions and demonstrate that though one methodology may meet some of the needs of the productive poor, no methodology meets all the diverse needs of the non-homogenous poor.

It is hoped, and anticipated, that common issues that arise at each of the two institutions, and among the clients and drop outs will lead to greater understanding of clients' needs, and an improvement in the products and services designed to meet those financial needs. Where appropriate, the report jointly addresses the common issues facing the clients of these institutions. And where appropriate, the report addresses problems, and potential solutions, for each institution separately.

1.2 How the research was conducted

The study draws from research already done by ***MicroSave*** in other regions of Africa. Industry information for South Africa also informs the report, as does the internal data collected and reported by the institutions with regard to dropouts, payment history, policies and procedures.

The study primarily uses qualitative research methods so as to learn directly from the clients. The participatory research tools used include focus group discussion (FGDs), individual interviews and participatory rapid appraisal (PRA) techniques: Product Attribute Ranking, Ranking Reasons for Dropout, Financial Sector Trend Analysis, Seasonality Analysis and in the case of PSA, detailed wealth ranking analysis. More information on these tools can be found in Appendix 1.

2. Financial Services in South Africa, and Northern Province

2.1 A brief background of the South Africa situation

The South African microfinance sector differs quite significantly from the East African, and even Zambian, microfinance markets. The market is led not by international or large local NGO-MFIs; instead private sector, for-profit micro lending institutions, and enterprise finance lenders lead it. Before 1992, financial services to the poor, or the "unbankable", were provided by NGO's, parastatals financiers and the informal sector (burial societies, rotating savings and credit associations, and the *mashonisa* – or moneylender). Banks were not offering credit to the poor, although they had been providing deposit facilities to the poor for a long time.

After the Usury Act Exemption of 1992, which removed interest rate ceiling for all loans under R6, 000 (roughly $725)[4], the private sector responded to the opportunity. This sector grew exponentially from a portfolio of less than R400 million prior to 1992 to approximately R15 billion in 2000 (Coetzee and Grant, 2001). Note that the Usuary Act ceiling was again lifted to R10,000 in 1999.

The result was a massive growth in micro-small lending, but it also became clear that the intent of many micro lenders bordered on, or crossed over, the line of unethical practices. The government joined forces with industry stakeholders in 1999 to establish the Micro Finance Regulatory Council (MFRC) to

[4] R8.25 = $1.00USD when this research was conducted.

regulate the lower level lenders. Since the launch of the MFRC there have been changes in the market, including increasing formalisation of the industry, more interest by the commercial banks in micro finance, introduction of wide range of new actors (like furniture and clothing stores that capitalised on information gained with in store lending services over years) and increased access by clients to credit products.

The 1999 Usury Exemption Act requires all institutions providing loans below R10,000 to register with the MFRC if they wanted to charge rates higher than the ceiling under the Usury Act. They are monitored by the MFRC and the MFRC does have the power to enforce their standards or cause litigation against institutions not following the Act. Almost all cash lenders (30 day lenders)[5] charge a standard 30% per month with loans payable in full monthly, upon receipt of the borrower's paycheque[6]. The ability to charge higher rates and/or become a legal MFI has stimulated membership and virtually all microlenders and microfinance institutions have joined.

As a result, MFRC data on the microfinance industry provides a good indication of what is happening on the credit side of the market. On behalf of the MFRC, Coetzee and Grant of ECI (2001) estimated the market on the basis of these figures and other sources. There are over 4.5 million loan accounts and loans outstanding of almost R14.9 Billion, ($1.8Billion). Private sector companies provided all but R600 million.

2.2. The poor in Northern Province and access to financial services

The Northern Province is a region of extremes. It covers 9.6 percent of the surface area of South Africa, has more than 12 percent of the population, and produces only 3.7 percent of its GDP. As a result it is the poorest province in the country, with a per capita income that is less than a third of the national average. The Human Development Index (HDI) shows that the Province is less well off in terms of public sector spending on education and health care especially. While these averages are also lower than the national average, the resulting HDI score is about 70 percent of the national level. In terms of the components of the HDI, life expectancy is marginally lower than the average for the country, and the literacy rate is 90 percent of the national average.

As can be expected, the unemployment rate is higher, and the labour absorption capacity and the rate of urbanisation lower than the national average. The province also suffers from high levels of crime, further affecting growth.

Most of the economic growth in the Province can be ascribed to the growing prominence of the government sector. The largest sectors in the Northern Province economy, in order of size, are community and social services, mining, commerce and agriculture; and both the agriculture and mining sectors are declining.

The development potential of the Northern Province is seriously hampered by water scarcity. More than 74 percent of agricultural land is suitable for grazing only, while only 13.2 percent is arable (of which 20 percent is irrigated).

The labour participation rate in the Northern Province is the lowest of all provinces. This can be ascribed to the relatively large proportion of women who are either engaged in subsistence agriculture or supported by relatives who work elsewhere. In addition, a fair number of the men not formally employed also work in the subsistence agricultural sector where possible. The labour force numbered 1.1 million in 1995 (formal sector, informal sector and unemployed). The labour force increased by 5.7 percent per annum between 1980 and 1995. This high rate can be attributed to the relative youth of the inhabitants. The formal economy is unable to absorb the large number of new entrants together with trying to absorb the already unemployed. The national level of dependency (measured as number of

5 Note: We differentiate between cash and term lenders by the loan term; Cash lenders generally lend for 30 days while Term lenders tend to lend for 6 to 36 months.
6 In a discussion with a microlender in Louis Trichardt, the authors were told "Everyone has to charge 30%. We are all part of the MFRC which is like a monopoly". The reality is that there exist no prescription by the MFRC on interest rate levels.

people that each economically active person should support) is 2, while in the Northern Province it is 3. If the high unemployment figure is considered the dependency ratio is at least twice that of the formal figure.

All in all, these statistics present a picture of a difficult place for financial institutions to easily operate. However, as in the rest of South Africa cash lenders operate and dominate in the Northern Province microfinance sector. Names like “Quick Cash”, “Easy Cash”, “Rainbow Cash” etc. are found in all the major towns. As is usual the cash lenders primarily serve the employed urban dwellers, leaving the rural communities and self-employed with little access to formal sector financial services.

Until February 2001, the Microenterprise Alliance found five MFIs involved in enterprise finance operating in the Northern Province: Small Enterprise Foundation (SEF), Provident South Africa (PSA), Marang, Akanani and Agishana. Although Agishana and Marang were still making loans, they had many operational and financial problems.

Northern Province Enterprise Finance MFIs						
Name of MFI	Active Borrowers	%of Women clients	Number of savers	% of Women Savers	Loans outstanding in R million	Average Repayment Rate in %
Marang Financial Services	6, 000	92			3.3	99
SEF	12, 115	97	12, 115	97%	7.9	98.5
PSA	40, 000	80			39	+80
Agishana	1, 400	73			1.7	70
Total	49, 515		12, 115		50.9	
Source: Micro Enterprise Alliance, 2000						

Floods in early 2000 compounded problems for many Northern Province inhabitants as many houses and assets were destroyed. Many MFIs lost clients to these floods, and there were reportedly increased delinquency and defaults following the disaster.

PSA and SEF have been operating within this environment for more than 3 and 9 years, respectively.

3. Structure, orientation and products of the MFIs studied

3.1 Who are Provident South Africa and Small Enterprise Foundation?

3.1.3 Provident South Africa (PSA)

PSA forms part of Provident Financial plc. based in the United Kingdom, which has been operating for over 120 years. It is a for-profit corporate entity with the objective to be a leading provider of simple financial services to poor households. They seek to enable customers to gain access to goods and services that could not otherwise be accessed without loans. They do not have a specific poverty focus and lately have begun to shy away from lending to salaried people because of the disconnect between monthly salary payments and weekly loan instalments. Clients are allowed to use the funds for what they wish, though it is encouraged that the business be the focus as it is the source of repayment.

By June 2001, PSA had 39,015 active clients in four branches and a workforce of 135 employed staff and 626 self-employed Agents – commission-based credit officers. PSA is increasing its client numbers by 1200 new clients per week though high dropouts and a write-off rate of around 250 clients per week, according to their staff, temper this rapid growth.

PSA Loan Products[7]		
	23 week loan	33 week loan
Available for first time borrower	Yes	No
Loan Size	R600 – R3,000	R1,000 – R7, 500
Nominal Interest	9.5% per month	7.5 % per month

[7] All information on PSA product terms and conditions come from “Policy Decisions for Provident South Africa – Version 12 – March 2001”, “Arrears Guidance and Policy Document for Provident South Africa”, “Introducing…Provident South Africa”, a Provident South Africa Power Point Presentation and comments on draft report - all provided by Management

Effective interest	56.17%.*	62.36%*
Repayment Frequency	Weekly	Weekly
Security	None	None
Grace Period	None	None
Rebate	Offered	Offered
These figures as calculated by PSA		

Features of the PSA Loan/Delivery System	
Methodology	❑ Individual loan
Eligibility	❑ Must be South Africans between 18 - 65 (Identity Book required) ❑ Must own a business, ❑ Must be within a 2 km radius of a PSA Agent.
Procedures	❑ Agent identifies good and bad potential clients ❑ Visits home and business to discuss loan ❑ Gathers customer details, checks stock, assesses income and expenditure ❑ With Loan Application (Customer Information Sheets), recommends loan to Development Manager ❑ Development Manager Home Verification Visit for all new customers ❑ Agent disburses the loan at the client's home/business and makes all collections at the same place. ❑ Collections are generally made on Saturdays
Conditions	❑ Maximum first-time loan, in exceptional cases only, is R2,000 ❑ First time borrowers must take a 23 week loan ❑ Good quality customers (successful completion of loan, with above 67% collection percentage) may take a 33 week loan
Repayment	❑ Weekly, at home or business ❑ Some Agents allow clients to pay monthly or fortnightly ❑ Prepayments are accepted by some Agents, not by others (Agents are not allowed to retain float) ❑ No default charges, even if customer takes longer to pay
Follow on Loans	❑ A 67% collection percentage (not calculated over the full period of the loan) is required before a follow on loan may be taken ❑ Loan sizes may be repeated, decreased or increased depending on stock check, income and expenditure assessment ❑ Area Managers must complete a Home Verification Visit on all customers applying for R3000 or more ❑ Loans of R5500 – R7000 are only available to those who have successfully repaid a loan of R5000 ❑ A client may make a bulk payment in order to move up to a higher loan amount if s/he has five or fewer weeks remaining on the existing loan and a collection percentage of 80% (less than 80% must receive approval from Regional Manager) ❑ A statutory 3 days delay between loans (A "cooling off period" specified in the Usury Exemption Act)
Agent Issues	❑ Training: One-day induction; 3 further one-day seminars over the next 6 months ❑ Commission: New clients: R4 ($0.50) for each new customer, R12 ($1.50) after the customer has repaid 50% of the loan and charges. Thereafter only 5% commissions will be paid

3.1.2 Small Enterprise Foundation (SEF)

SEF is a non-profit, NGO dedicated to ending poverty and unemployment by working with the rural poor of South Africa, in a sustainable manner. SEF was registered in July 1991 and commenced operations in January 1992 with the objective of empowering very poor women by providing credit and training for self-employment. Although the institution is improving its sustainability, discussions with Development Department staff indicated that the institution enjoys generous donor support and is willing to delay sustainability in favour of greater outreach to poorer women.

SEF actively targets the poor and very poor through their two loan programmes - Micro Credit Programme (MCP) and Tshomisano Credit Programme (TCP). The TCP programme arose after two years of operation of MCP as SEF felt that the "very poor" were being excluded from MCP by those

better off (less poor) clients. TCP uses Participatory Wealth Ranking (PWR) to identify the poorest households in a village and then provides the opportunity for membership to the women in those households. SEF loans are permitted to be used only for business purposes – field workers and client committees check loan usage very closely. Loan sizes are determined based on the stock value of the businesses. At SEF's request, only the TCP programme was examined in the course of this report. Operations policies do discuss an education loan, but it does not appear to be operating in practice. Therefore, only the business loan product is discussed below.

SEF Loan Products[8]			
Designation	10 or 15 Fortnights loan	6 Month loan	10 Month loan
Loan Size	R100-R500	R1,000 – R10, 000	R1,000 – R10, 000
Nominal Interest	2% per month	3.3% per month	3. % per month
Effective interest rate	44 – 45 % p.a.	68% p.a.	65 % p.a.
Repayment Frequency	Fortnightly	Monthly	Monthly
Available to first time borrowers	Yes	No	No
Collateral	Joint and several	Joint and several	Joint and several
Savings	Minimum R2 per fortnight	Mandatory	Mandatory
Group meeting	Mandatory fortnightly	Mandatory fortnightly	Mandatory fortnightly
Centre Meeting	Mandatory	Mandatory	Mandatory

Because of the Grameen-styled operations and the specific targeting, the process for becoming a TCP client takes a bit of time. TCP sends staff to a village area, and through the local leadership obtains approval to conduct a PWR to determine eligibility to join.

Features of the SEF Loan/Delivery System	
Methodology	❑ Group Lending
Eligibility	❑ Must pass the "poverty test" (formerly via a Visual Indicator of Poverty test; now through Participatory Wealth Ranking) ❑ Must be South Africans within 15 years age difference from other group members ❑ Must be friends living in the same demarcated village ❑ No relatives ❑ No two members in one household
Procedures	❑ After group identification, 7 day training may begin ❑ 6 days on TCP policies, philosophy and procedure ❑ Day 7 is group testing and Final Group Recognition ❑ Savings starts during training ❑ Develop loan proposal; approved by Group ❑ Loan disbursement is staggered 2 - 2 – 1 (poorest first) ❑ Group Chairperson must check stock bought with loan, outstanding money and receipts. (Same is checked again by Centre Chairperson and SEF Field Worker) ❑ Type of business and successful completion of prior loan determine "choice" of loan terms after first loan ❑ Group meetings are fortnightly, even if clients are all repaying monthly
Conditions	❑ First loan must be less than R500, repayable over 10 fortnights ❑ First loan values have predetermined maximums based on types of business ❑ Loan values are based on business values (determined by group and field workers based on stock values), or as TCP Principle No. 8 states "If we keep our promise in maintaining excellent credit discipline, SEF will give us larger subsequent loans subject to [our ability to repay]."
Repayment	❑ Repayments are fortnightly, in case of first loans, fortnightly or monthly thereafter depending on loan chosen (based upon business type and good collection history) ❑ R2 savings are required
Follow on Loans	❑ Increases are up to 1.5 - 2[9] times the last business value; "*It should be made sure…that members will always be able to get their last loan size as a repeat loan.*" "*Nobody can be forced to take a smaller amount*"

[8] All information comes from "Tshomisano Operations Policy", "Group Training Manual (3rd edition)" or from discussions with field workers, branch or head office staff.
[9] Note: Group Training Manual written in 1997 states "double the size of the first loan", Tshomisano Operations Policy in 1998 states 1.5 times

3.2 MFI dropout data

3.2.1 Provident South Africa

On average, 51% of PSA's clients dropped out from inception until June 2001[10]. The distribution of dropouts varies across the branches. The older (Pietersburg) the branch, the higher the dropout rate (61%). The newer the branch (Louis Trichardt), the lower the dropout rate (33%). This could conceivably mean that longer-term clients with generally larger loan amounts are dropping out, however the data providing loan amounts or "cycle" of dropouts was not available.

Researchers were given a Paid Up Analysis report from PSA, which indicates the quality of "paid up" clients (those clients who paid up but did not take on a further loan)[11]. The clients are segregated into "quality" collection percentages of: 100%, 81-99%, 67-80% and below 67%[12]. The calculation for these percentage collection categories is not entirely clear as it takes into account the number of payments made over the last 12 weeks, though the loan terms are 23 and 33 weeks.

The Paid Up Analysis for July 2001 showed that of the approximately 28,000 clients who have dropped out of PSA, almost half were below 67% quality and therefore ineligible to take on a new loan and thus "forced" dropouts. Another 9% of clients were in the 67-80% band, which could indicate that they had not been particularly easy clients for Agents to deal with – and could have made them forced dropouts via "exclusion by Agent".

There is any obvious portfolio quality issue when so many clients are operating at below 81% collection[13]. Management indicated that this was a formula that had worked for them, however and allowed flexibility for clients. Management indicated that their biggest concern among dropouts were those that were good quality clients. About 10,500 clients (about 33%) of dropouts fell into that category. These are presumably the voluntary dropouts.

Women make up 80% of PSA's overall clientele and about 76% of dropouts are women, indicating that male clients are dropping out at a marginally faster rate. Generally the gender composition in rural South African communities is skewed in favour of women, because men tend to leave their villages in search of employment. It may be this tendency that is revealed. Female dropouts tend to represent higher percentage in the more rural branches (80 – 85%) than in more peri-urban branches (70 – 77%), again a possible indicator access to other employment.

PSA clients are 98 percent informally or self-employed, as compared with 2 percent employed by others. However, a far larger percentage of dropouts come from the employed individuals - about 15%, but up to 24% in the urban branches of Pietersburg where employment opportunities are conceivably more available. PSA did indicate a shift away from employed personnel as potential target clients, which may also be a reason for this statistic.

It was not possible with the records availed to the researchers, to determine in what cycle, or at what loan amount dropouts were occurring.

3.2.2 Small Enterprise Foundation

SEF's "Excel"-based MIS did provide information by loan cycle, poverty level, etc. However, it was not easily manipulated as it was across several spreadsheets, which did not "read" from each other. The result was that the researchers crossed the data themselves, which may have led to some transcription errors.

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[10] Average across branches since the start of the programme.

[11] The data was incomplete meaning the percentages of "clients by quality" do not add to 100%.

[12] There is some uncertainty as to how this percentage is calculated. It is *not* on-time repayment rate. It calculates the number of payments over the prior 12 weeks, not the entire loan term. A repayment of 67% or more within the repayment period is considered to be good. Those with less than 67% repayment are considered to be customers of low quality and cannot be granted repeat loans.

[13] The 81 – 99% collection band is very broad. Most NGO MFIs are far stricter in their measurement of portfolio quality.

Over the last 3 years, the TCP dropout rate remained at 18% until the end of last year. In the first quarter of 2001, the dropout rate increased from 18% to 33%. Across all the branches from 1998 until the year 2000, it varied between 16 and 26 %. But since the beginning of this year, it increased from 26% to 45%. An analysis of TCP data on dropouts revealed the following characteristics.

Dropout per Loan Cycle

One in every four clients in the first loan cycle dropped out. One in three clients, who completed the second, third, fourth, and fifth loan cycles, dropped out. Finally one client in two dropped out in the sixth and the eighth loan cycles. Looking at all cycles, 78% of dropouts completed only one or two loan cycles. This could indicate that people were "trying it out" and decided against continuing, which is a common phenomenon among MFIs. Because of the youth of the TCP programme, there is a small client population that have reached the higher loan cycles. However, we do see that quite high percentages of those clients do dropout which may indicate that they were experiencing difficulty with the relatively higher payments required by the larger loans.

SEF Dropouts per loan cycle

Loan Cycles	Paid-up	Returned	Dropped out	Percentage per Cycle	Percentage of Total Dropouts
1	1351	1037	314	23%	56%
2	356	231	125	35%	22%
3	131	87	44	34%	8%
4	101	67	34	34%	6%
5	66	42	24	36%	4%
6	35	19	16	46%	3%
7	17	12	5	29%	1%
8	5	3	2	40%	<1%
Total	2062	1502	564	27%	

Source: Small Enterprise Foundation: TCP Programme Dropouts: October 2000 – March 2001

Dropout per Loan Term

Loan terms and cycles are quite closely correlated, so it is not surprising that most of the dropouts occur during the fortnightly loan terms, which are offered in the earliest loan cycles. The fortnightly loan clients account for 82% of total dropouts, the 6-month clients represent 15% of total and 10 month clients, 2% of total dropouts. Interestingly, the 6-month term has a high percentage of dropouts, which might be related to the relatively higher instalment payment that those borrowers would have than other clients (fortnightly or 10-monthly) for the same loan amount.

It should be remembered that SEF's clients are selected primarily for being among the poorest of their villages. It is therefore expected that they would be most vulnerable to other poverty related conditions including the incapacity to use the loan productively which can cause an inability to repay, or to continue with a loan programme. Furthermore, the recent floods in Northern Province did affect SEF's (and PSA's) rural clientele, as does their lack of access to markets beyond their local villages due to poor communications, infrastructure and indeed, possibly entrepreneurial talent, expressed by the women as an admission that they were "over-trading the area" with their similar businesses[14].

4. Reasons for dropouts

Both institutions are concerned about the high drop out rates they are facing. Despite the different methodologies and motivations (one is for-profit and the other not prioritising financial sustainability), it appears that they share several similar reasons for their escalating drop out rates – policy problems and delivery (process) problems. Notably, Provident prides itself on its weekly loan policy keeping payments low for its clients, and SEF touts the benefits of being in a collective, group-based context. It

[14] SEF provided emergency loans to some of those clients hardest hit by the floods

is these two areas that clients claim are the greatest reasons for dropping out of each programme respectively – and it is what non-clients fear or dislike most about the other programme.

SEF clients talked of the fear of weekly payments - *"Don't even talk about the interest rate. Having to pay that loan weekly would be too expensive"*. PSA clients seemed to feel almost the same way about the pressure of group meetings and were dismissive of group guarantees preferring to be personally responsible for their own loans, ***and no one else's.***

4.1 Policy Issues: Too lenient, too rigid

Too lenient and too flexible (dropout and default issues)

To a clientele that may have feared "the authorities" in the not so distant past, or perhaps to separate themselves from the notoriety of both *mashonisa* and the cash lenders, SEF and PSA assure clients that they will not go to the Police or Courts to resolve default issues. The resultant **leniency** is that those clients apt not to pay have little to fear from either institution. PSA did apparently resort to hiring debt collectors in a few cases, but overall, clients seemed well aware that they would not be overly inconvenienced if they did not repay on a timely basis, or at all.

Client/guarantors at SEF complained quite bitterly about not being able to do anything about the defaulters in their groups. At PSA the responsibility of collecting from delinquents and defaulters rests on the Agent's shoulders, with assistance from the Development and Area Managers.

"*TCP should not have informed people that they do not work with police because when we tried to apprehend defaulters they said, "*Where are you going to report us, TCP does not work with police. So, when you approach them they say "go to the police, we will meet you there"."

One group said that they had told TCP they did not think some members should get loans because they were not credit-worthy. "*The FW said that these are loans for the poor and they should not be denied anyone*".

PSA clients taunt Agents and dodge them; Agents in turn threaten seizure of assets and use "harassment" techniques– showing up at clients' homes at odd hours and demanding the money. Yet, Agents say, they may see one of their clients in the *shebeen* (local informal pub) drinking with cash in hand, but he will not pay knowing that he will not be taken to court.

As one Development Manager told researchers: "*Some customers are self-sufficient, but they don't pay because there is no penalty. People are talking to each other that this is no penalty for non-repayment*". As a result he says that he and other Development Managers, write off between 8 – 13% of their loans.

At SEF this leniency is a "selling point": In their guiding principles, which are described to potential clients during initial training, clients are told, "*...the foundation of Tshomisano loans…. [is that they] are the right of the poor who form groups and centres. The loans are disbursed without the need of collateral or guarantors nor threat of legal action*". To certain clients this can certainly be heard as an easy way to excuse themselves from payment without threat - after all, it is their right and there is no threat of legal action. But, despite this quoted statement, there are indeed guarantors - the group of five, and the entire centre – and *their* inability to collect from defaulters which reduces their desire to be in a group loan schemes.

SEF methodology puts the burden of default collection within the group. Defaulters taunt their group members by reminding them that they cannot go to the police, or the *Induna*/local council. The group is inhibited by a policy that leans towards leniency and effectively limits the group's choices in attempting to collect from defaulters – for hard core defaulters, simple talking, pleading and recitation of the SEF Pledge does not work. Several people expressed a willingness to recommence borrowing with SEF, but insisted that the group system would have to be changed.

Not that individual loans and individual responsibility means a 100% repayment rate. PSA's "non-threatening" policy is coupled by a potentially "**too flexible**" repayment policy. Agents are commission

based and make their money based on clients' repayments. Therefore it is in their best interest to collect as much as possible each week. However, many clients stated that they paid once per month, fortnightly or weekly – depending on the Agent. In groups of clients that came from different zones (and thus dealt with different Agents), clients (and researchers) were surprised at the different instalment payment "policies" from zone to zone.

From PSA's Paid Up Analysis it appeared that almost 80% of dropouts were at collection rates below 81%. It is conceivable that some of these people could have been intentional defaulters, but some of them could have also been people who found themselves with increased payment difficulties as they utilised the "flexibility" option too far, to the point that the instalment due was beyond their capacity. PSA also adds another "**too lenient**" selling point to their loans – even if the client takes longer to pay than the prescribed term, there are no default charges.

These lenient measures at the two institutions may be contributors to delinquency, default and forced dropouts and forced "resting". At PSA, the policy allows many Agents to be "too lenient" and may have contributed to the subsequent problems of default that have grounded the programme.

Too rigid: Weekly repayment

For those clients with strict Agents, the rigidity of weekly loan repayments was a great cause of concern and believed by staff, clients, non-clients and dropouts as a major reason that people left PSA. In one ranking session the clients insisted that the issue be written as: **"***Even if someone dies you are forced to pay that week***"**. While it appears that this runs counter to policy, idea that the weekly payment is absolutely inflexible runs throughout much of the programme and indeed into the non-member communities as well. Although not applicable in the case of SEF, SEF clients, and their Field Workers, expressed real worry about the difficulties caused by "the weekly money", which included PSA as well as other weekly lenders (possibly individuals/*mashonisa* "including some white people" who lend from the pension points)[15].

The main reason that weekly payment appears to be such a grave problem, and an often-repeated reason for dropout at PSA is the mismatch with borrower's income streams. Despite generally being self-employed, usually running shops that should create daily revenue, it appears that the majority of microfinance clients offer credit to their own clients, especially those who have formal employment or pensions. Civil servants, pensioners and the formally employed receive their monthly cheques and repay their creditors – from the *spaza* shops, the local beer vendors, other cash lender etc. In effect these daily traders of foodstuffs, beer, etc. are paid almost as regularly as those that receive cheques from their employers or government!

Much of the discussion on weekly instalments came in the form of "interest rate is too high". Clients had a very hard time separating interest rate and instalment/instalment size with most discussions on these points crossing over from one issue to the other. In clients' eyes PSA charges a very high rate, however, this was often confused with the size of the loan instalment. At a nominal rate of 9.5%, it is considerably lower than cash lenders and the *mashonisa* who clients say charges rates of 30 – 50%. Further, non-clients who told researchers that PSA rates were too high suggested that rates of 10 – 20% per month would be fair. It is believed that while the interest rate certainly does matter to clients, it is the pressure of making the instalment payment each week – particularly if one has a "tough" Agent.

> One dropout, who stated that she would never go back for credit – anywhere – had however learned a lot from the "credit discipline" of PSA's weekly payments. The instalment amount that she had previously been paying PSA she now set aside each week (with obviously less pressure) as savings. From this savings, she was proud to say that she was financing her small *spaza* shop and covering her other needs, without the need of paying interest.
>
> "*When you take a loan, [the repayment] happens to be the same as your commission [profit] and you remain with nothing and end up working for Provident*."

[15] Pension points refer to the locations where pensions are paid to pensioners.

Interest is high according to another client, but it was "*because we weren't buying properly*" that profits were not being made.

Finally, as one client simply said "*It's just tough getting money every week*" – regardless of the interest rate being charged, or how the changes were communicated.

Too many meetings

At SEF mandatory attendance at fortnightly meetings – even for those paying monthly – was a cause of some discontent. For some it was not that the meetings themselves were onerous, but that the meetings often became difficult due to the inevitable "patching" (the process of clients paying off overdue loans of fellow group members):

"*If I send the money, why do I have to attend?*"

"*You can spend the whole day there – from 11am to 5pm. You can even get hungry waiting.*"

These meetings have apparently become longer in recent times according to clients, and staff, since SEF stopped accepting partial payments. This prior "leniency", or contravention of policy, meant that clients did not have to stay at the centre form 11am – 5pm waiting for money to come in from a delinquent or her guarantors. The new rigid application of policy also has another bad effect on delinquency, default and dropout – those "four out of five" clients who had come to the meeting with their required payment, were now sent home with their money. They admitted that the ability to hold on to those funds in households with many other competing financial needs was extremely difficult and could increase the number of defaulters the following week.

"Patching" for Defaulters

As weekly instalments were the over-riding theme at PSA, "patching" was the number one issue at SEF. All roads lead back to patching – problems and dislike of meetings, non-acceptance of partial payments, etc. lead to SEF's hard-line stance on patching – and to the single biggest reasons that dropouts have increased to such an extent at SEF. Woman after woman explained that she was not a dropout, she was merely waiting until defaulters paid and she could resume borrowing again. It appears that these "forced resters" are engaged in a standoff of sorts with SEF – they are not going to make (any further) payments for their group members… and SEF is not going to extend loans unless the groups come up with payments from the defaulters.

How long this standoff will continue is likely to be up to SEF's re-grouping of clients and/or writing off defaulters. Interesting, the researchers did not find that very many of these women had switched fully and were now going to PSA or other lenders. Instead, most of them talked of downscaling their businesses, or simply re-stocking more slowly, using their profits.

Loan Size Determination

That many clients are doing without loans is not to say that all TCP clients relied only upon SEF for loans. Another area of **"rigidity"** at SEF regards loan size determination and loan usage. According to the SEF policies, the type of business a borrower operates and the "business value" or stock value of that business determines loan size. A Committee made up of other group members with approval by the credit officer supposedly determines loan size. In reality, it appears this process is more muddled, according to clients who say that field workers often determine loan size, or that the Committee and field workers determine the loan size together. Complaints of the arbitrariness of the determination were frequent. "*They let you think that everything is OK. Then, the next loan that you get is less than you need*".

Loan Usage

In addition to this, TCP requires that all funds be used for stock purchase and business expenses only. "*Even if you have R4 ($0.50) left over, they tell you to buy stock with it*". This "micro-managing" by TCP caused much complaint. What this has led to, according to clients, is over indebtedness, the opposite of intentions. Of course, it is over-indebtedness (to SEF alone) that caused the refusal in the

first instance, but without clients' understanding the calculations behind the decisions, the clients are simply feeling "lied to" and find the additional money requested, elsewhere. The end result brings the discussion back to default, patching and the current situation of defaulters and forced resters.

Clients explain:

"*Many people have run out of money and business failed because they can't keep a little money aside for contingencies*." Without money for the inevitable emergency, the women sold their inventory, and their business failed.

"*They shouldn't mind! Their concern should be that I am able to pay the R200 monthly!*"

"*This* (buying stock with all the money) *doesn't fit what we do! We sell vegetables and they will rot if we buy them all at once!*"

"*TCP says it has to be for the business, but others don't. So they get it* (the other loan) *but it is the business that has to repay, and it can't*".

"*Before the weekly money, the centre was right and paid. But when you get less that you asked for, you were tempted to get the weekly money*". The result, according to the clients was that these people soon became over indebted trying to make one payment every week and the other one every month, and eventually had to prioritise which payment would be made.

And, clients said that "at the Pension Point" it was easy enough to find many others willing to lend. Of course, the "weekly money" has more frequent pressure than TCP's monthly loan, and "*you have to pay the* mashonisa *first, or he will take your furniture*".

4.2 Recruitment of Agents, client recruitment and group formation

PSA recruits clients by recruiting Agents who find clients in their immediate neighbourhoods. SEF introduces the programme to poor households within a "demarcated area"; people who are interested in getting credit have to form into groups of five until a full centre is created. According to clients and staff at both institutions, recruitment methods are a major contributor to the dropout problem.

PSA management and staff readily admit that Agent recruitment is not done properly and that as a result, Agents do not recruit quality clients. As at least one member of management stated - Agents are in a hurry to make money and therefore recruit "too easily". The Development Manager (DM) has to also check up on clients, but they too are very busy. One DM said that business evaluations to for new clients verification "took about 10 minutes" and the DM was expected to do at least 50 – 60 new client verifications per week. Management acknowledged that DMs did not do proper credit control and did not ensure that clients were not already over indebted. Agents sometimes collude with client and are sometimes just dishonest and have stolen client's money. Agents sometimes collude together even more disastrously - one DM was apparently held up by his Agents who had decided not to repay the company.

Agents do not have an easy job recruiting new clients, collecting loans from existing clients and trying to chase up defaulters who avoid them. One Agent told of the frustration of having to go to clients' homes four times a day to collect payments. "*The last time I had to stay at her house until 10pm. She dodges me and to be paid I have to wait until she comes!*" Agents make money by recruiting new clients and collecting well, and transferring "extra clients" to other (possibly newer) Agents. As they get 5% of overall collections, there is an incentive to have higher balance borrowers. PSA staff said that Agents make between R100 – R400 per week, or \$50 - \$200 per month.

While many PSA clients had good relationships with their Agents, others had different experiences.

Agents had assisted the researchers in gathering clients. However, when the agents got to the meeting area, the Agents did not leave. Clients initially whispered or spoke in lowered voices as the Agents were in the adjacent room. Finally, one woman said that she was going to speak since she was probably going to quit the programme anyway! She said that the Agents had warned them against complaining about them on the way to this meeting. She said that the Agents were not good – and the group of clients assembled agreed.

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Rachel explained that Agents with heavy client loads of bad debtors would not take on more clients. Clients are not always able to change zones to find a better Agent. However, Rachel was also aware that Agents need to reach targets and therefore, she said, they forced clients to take higher amounts than they needed. Their group agreed this was the case. When asked why they took the higher amount (as the higher payments due were a major problem), the answers were simple: "*They know we need the money*", "*Loans are stock; without loans you have no stock*".

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One group said that the approach of Agents is not very nice. "When you are having repayment problems they talk very badly about you". "They humiliate you in front of your neighbours". "They come at six in the morning". And, as one woman complained: "Look at me. I do not have a husband. While seated nicely with my boyfriend, an Agent comes and asks me about the loan. I have not told my boyfriend about the loan!"

Clients felt that they could not raise questions as Agents might feel that they clients were belittling them.

At SEF, group formation and subsequently, patching (group guarantee) are the biggest reasons for dropping out.

There was a lot of support for the ideas of groups… in groups that worked well. One woman spoke of how her group members sold her stock alongside theirs when she was too sick to work. However, as another woman said, "*Money is a devil*" talking about how she thought she knew the women that she had joined with. That woman said that if she had a chance to re-form her group, she would borrow again with women she knew very well. It may well be that when TCP had first selected their area; there was more of a rush to form groups so as to get credit faster – rather than to truly ensure that their friends were credit-worthy.

Additionally, researchers heard that "*They [TCP] are the ones that formed us*" and that clients did not actually choose each other based on their trust in each other, but rather based on the TCP rules: that they be within 15 years of each other, that they not be related, that they be friends and live near each other. The "pool" of potential friends was of course first limited only to those who had met the TCP poverty criteria.

Initially clients said that the group and the guarantee worked out fine. Loans were small and easy to repay. However, as loans got larger, clients began to have difficulty repaying. Group savings accounts were utilised for repayment which caused a good deal of unhappiness as some clients claim that they did not fully realise that their R2 (or more that they voluntarily added) would be utilised to pay for defaulters.

Mostly though, the problem with the group is that while a defaulter remains, the others cannot get loans. Those that cannot get loans from TCP do not necessarily consider themselves dropouts. Some of them still attend centre meetings regularly, even though they are getting no funds… and the defaulters are not paying. As one woman put it "*We are hanging in the balance*". Whole centres are essentially crippled while groups wait for the defaulters to pay.

"*Being an individual is best. Group can be good. But, for those people who are not paying, they would be motivated if they knew another loan was coming*." But, since they saw that those others who had paid in the centre were not getting follow on loans, they were not going to repay either.

"*When you borrow money as a group of five and one fails to repay, the burden is felt by the four members* [who did repay]"
.
"*In reality, the reason we left was that when they gave us cheques they gave us them each. But now the Mama doesn't pay and I have to pay for her? She got her own cheque, she should pay herself!*"

One client said, "*What can you do? They don't mind* [that you cannot get a loan], *and they are your neighbours*".

For some, this waiting was enough to convince them to leave the programme – to formalise what was *de facto* the case. These clients seemed to be annoyed not only with being "punished" for the non-payment of one (or more) members of their group, but they also felt that this sense of "being punished" was belittling to the people who had paid. While many said that they would much rather be individually responsible for loans, some said that they would be happy to re-group – now that they understand what their risks are, their choices would be different.

The patching issues are not news to SEF. In both their prior dropout studies patching came in as a major issue for clients. However, an amendment to the system has yet to be developed.

4.3 Socio economic characteristics

SEF's TCP programme is aimed only at the poorest of the poor, based upon Visual Indicators of Poverty (in prior years) and Participatory Wealth Ranking. According to clients and staff, neither the VIP test, nor the ranking was truly accurate in terms of indicating who was the poorer than others in the same area. As one woman put it – "*My house looks nice, but there is nothing on the shelves to eat*". Likewise, poverty is not static with clients moving over the poverty line in good times, and falling below again when beset with problems. Therefore, clients say, if the PWR or VIP is done once, it fails to take into account theses changes in their lives.

Twice, significant numbers on non-clients showed up at the researcher's meetings with clients eager to explain why they too should be eligible for the loan. Believing that the researchers would be able to answer why they had not been allowed to join SEF, they had arrived to state their case for inclusion in the "poorest of the poor"[16].

From the clients, we did not hear that one client was "more poor" or "less poor" and therefore more likely to drop out. Instances of illness, over indebtedness and business failure seemed to be problems that could beset anyone in their groups or neighbourhoods.

At Provident they do not exclude clients based on their relative poverty or wealth. Instead, a potential client, known to the Agent and either operating a business or about to start one is eligible. Using detailed wealth ranking, the researchers asked Agents to list their clients and discuss the dropouts in terms of their relative wealth to each other. The Agents generally described the rich as people with a nice looking house, with nice furniture and generally a nice car. The wife in such households works as a nurse or a teacher and they operate a business like butcheries or a lounge. The middle category is generally described as a household in which the people work in paid employment and may or may not run their own businesses. They have a nice house, but not of top-of-the-line building materials like the rich. The poor are described as those that work for R10 per day, are often unemployed and unable to send their children to school. They use mud and tin as building materials and have a live (bushes) fence. If they work, it is a domestic or as a farm labourer.

[16] Interestingly, even after hearing their neighbors and friends talk about the difficulty of repaying loans and of the problems of group guarantees, they still hoped to be selected if SEF were to return to the village and approve them for the program.

	Type of Payer				Reasons for Dropping Out				
	Total	Good	Fair	Bad	Agent Decision	Weekly Payments	Got a Job	Resting	Other
RICH	5	5	-	-	-	1	1	2	1
MIDDLE	28	19	4	5	4	5	4	9	6
POOR	15	5	1	9	8	2	-	1	4
	48	29	5	14					

Fourteen were listed as bad payers – clients that the Agent had to chase around to get payment from. The Agents had decided not to allow them to borrow again for reasons such as "*He is a boy who takes his money and uses it to drink. That is why he cannot pay. He is a bad payer and I would not accept him back*" or "*She is a quality customer but does not pay easily. I suffer to get her money*".

Ten of the 29 "good payers" were only resting: "*She says she will come back in September once she is ready to go to Johannesburg to buy things that she sells*". Five clients (none poor) had found employment – in an AIDS information centre, or at a dry cleaner, for example.

Overall, it appears that the poorest are most likely to be excluded by the Agent, as it is too difficult to chase them up for weekly payments. As Agents are working on commission it is likely to be easier for them to concentrate their efforts on "Good Payers" who come more from the "middle" and "rich" income categories.

Non-joiners

Many women came to meet the researchers in the hopes that they were re-classifying the villages and that they may this time fit in the "poorest" category to be eligible. Both the women in the programme and those that wanted in said that there should be no distinction that they were all in the same economic strata, even if TCP thought otherwise. Additionally, as MCP, SEF's micro-credit programme that does not use PWR as an eligibility criteria, does not operate in TCP areas, these women ranked "not poor enough" have no where to join.

Of course, the non-TCP eligible could join PSA if there were an Agent nearby (though the researchers did not find PSA Agents operating in the same villages). But, in PSA (more peri-urban) areas the researchers visited, potential clients said that they did not join because of fear of the weekly payments and the interest rate. Stories of people trapped in the debt cycle are common as the media highlight the sad stories of workers who are left without any funds left after repaying, by automatic debit, their many creditors. New legislation is attempting to assist the many debtors to retain at least a portion of their paycheques and the MFRC and other associations have been working to better ensure that unscrupulous operators are removed from the credit scene. Overall, the news on credit risks in the radio, the newspapers and "neighbourhood gossip" definitely seemed to increase aversion to joining MFIs.

Multiple joiners

The researchers found few clients of either institution who openly admitted to multiple memberships in MFIs, and due to the relative scarcity of MFIs, this seems very possible. However, this did not stop people from being over indebted. Borrowing from *mashonisa* – whether they are pensioners, or PSA Agents (as they are also occasionally called *mashonisa*), or those fully engaged in lending - and the "weekly money" (possibly PSA as well as other lenders) was common. Regular payments to funeral societies and *stokvels* (especially in the more rural areas) contributed to over indebtedness. And the general "credit culture" seems pervasive in these areas. Buying household goods on credit, locally brewed alcohol, food at neighbouring *spaza* shops (small informal fixed location traders), etc. seems to constitute a large amount of the debts of these clients.

4.4 Other Reasons for Dropouts

4.4.1 Business competition

Business competition was a major factor for dropout and inability to repay. At Provident, clients admit that since they all do the same businesses (*spaza* shop, tuck shop, selling at schools) they compete against each other and no one makes significant profits.

At SEF some clients feel very badly about this. One young woman who had attempted to run her own business from her home says that she felt like she was not smart as a result of this loan! "*They train you, but then you get out there and do business. You can't succeed; it makes you look like you are not smart because the training did not work out*".

According to all clients, the reasons for increased competition were not just from fellow microfinance clients, but the overall economic conditions that meant that there were few outside employment opportunities forcing many people to attempt to run *spaza* shops, *shebeen*s, etc. According to one group, social reasons are also to blame for increased competition as there are more unwed mothers who are forced to start *spaza* shops or other small businesses as the fathers are not providing financial assistance.

4.4.2 Loan Diversion

Clients cited loan diversion as another reason that people dropped out. At PSA some clients used a portion of their initial loan to pre-pay instalments and thus felt that they did not have enough to invest in the business to make sufficient profit. Loan diversion was often cited in connection with family tragedies, which required money – such as death and illness of parents or children.

4.4.3 Rebate

Lack of, or size of, rebate was an issue for some clients, though it was not a major reason for dropout, rather a compounding factor. Many cash lenders offer rebates for early settlement, as does PSA. However, the clients that brought it up felt that the PSA rebate was too small to make early settlement attractive.

4.4.4 Lack of communication and transparency

At PSA a significant cause for dissatisfaction and dropout was the lack of communication and a feeling of lack of transparency. Clients complained repeatedly about the "increasing interest rates" and feeling that PSA's interest rate is very high. This appeared to come not necessarily from the actual interest rate but rather from three separate interest rate and/or weekly instalment changes in the prior year. The changes raised suspicion among clients that they were being over-charged.

A client complained that her weekly payments had increased from a R400 weekly payment to R497, apparently for the same loan level – though possibly because the loan terms had been shortened. The client felt she was being cheated by this "extra R97" the other women in the focus group discussion nodded their agreement.

Many clients seemed to feel quite distant from PSA in general, as they worked through Agents and rarely saw any other PSA staff, other than the infrequent Development Manager or Area Manager visits. Agents were called *mashonisa*, or the PSA *mashonisa*, not because of their interest rates or methods, but because of the appearance of being an individual moneylender, not necessarily part of a larger group[17]. Non-clients in one area talked about why they would not take "*Violet's loan money*", but they did not talk about PSA as a whole.

4.4.5 Unhappy staff

Researchers were told that some SEF staff had become PSA Agents, and taken their clients with them. We did not hear this directly from any PSA Agent or meet clients who had dropped from SEF in this manner. However, what was heard was that there is a continuing communication problem between head office and field staff that had not been fully resolved by either a strike by SEF staff, nor subsequent meetings.

[17] But some PSA Agents may attract the name through their collection methods too … several harass clients, go to collect at 6:00 a.m or wait until late in the evening to get the money. Some Agents' collection methods are quite aggressive as clearly stated by the clients.

5. Conclusions and recommendations

In conclusion, PSA and SEF both appear to have strong customer bases of clients and potential clients who are seeking improved financial services, generally within the existing service provider. Staff in both institutions (including Agents) appears to be genuinely concerned for both the clients' satisfaction and the institutions' successes.

The following recommendations are not meant for immediate implementation, but rather point out areas that may need further investigation or clarification. The institutions obviously have more experience with their clients than the researchers do, but the researchers do have the benefit of: being external to the institutions, comparison with other dropouts and other institutions and, of course, the benefit of in-depth discussion during several weeks of meetings with almost 300 clients, potential clients and staff of these institutions.

5.1 Improved Recruitment and Loan Size Determination

Staff at both institutions felt that improved recruitment and loan size determination be enacted. Clients agreed.

At Provident South Africa: Agent selection, training and motivation at PSA should be improved. A one-day training for Agents and then subsequent follow-up training over a series of months is likely not to be enough to train them in client selection. Determining business value and business strength are not skills that can be taught quite so quickly. Expectations that DMs make 50 – 60 such assessments weekly (in "10 minutes" each) may need to be revised. While clients certainly do appreciate fast turn around time, slowing it down for better credit control appears necessary. Assessment of other sources of credit is very difficult, especially as so much is from the informal market, but at very least Agents and staff trained in credit assessment is a necessity to ensure that clients are not over indebted by the PSA loan, alone.

Additionally, a restructure of the commission basis for Agents appears to be in line. An increase in commission based on collection and a decrease in commission based on new clients may be an appropriate change. Insistence and commission for, high quality repeat clients may be another, regardless of the size of the loans. A move to a base-salary, plus commission may also be an area to be investigated.

At the Small Enterprise Foundation: groups and committees are mandated to determine the repayment capability based upon stock value. Clients admitted that this technique forced them to lie and show SEF or the Committee one "business" while actually engaging in another. Additionally, stock value may not be the best indicator of ability to repay. High value items infrequently sold will not assist a client in making fortnightly repayment. A shift to looking at profit potential rather than stock value may be looked into.

Loan size determination at SEF needs greater transparency so that clients are not dissatisfied and do not become over-indebted seeking the initial capital requested. An explanation as to why the full amount requested was not provided could reduce the number of clients borrowing from competing sources.

SEF's decision not to have both TCP and MCP programmes operating in the same areas may be an area for further investigation. Clients did not feel that TCP was fairly targeting only the poor because of the changeable nature of poverty, versus the infrequent poverty assessment of it by SEF personnel. It appears that a significant number of people who "failed" the TCP test would be interested in joining SEF – either via MCP or TCP. One area of interest may be standing the original concept of TCP on its head. If TCP was created so as not to allow better off members to exclude the poor, what would be the impact if TCP members were allowed to permit into their groups the supposed better off?

Clients at both institutions both said that dropouts occurred because of business failure due to "over-trading" their local areas. While SEF does offer business training, and PSA proposed to, this may not be sufficient training for clients to really understand the nature of competition. A further investigation of

small business opportunities and avenues for profit making ventures may be useful for both the institutions and its clients to understand.

5.2 Changing or Altering the Big Issues

Small Enterprise Foundation and Patching

SEF clients are stuck … they cannot re-form their groups and they cannot make their defaulters pay. By allowing this situation to remain, SEF's books must reflect a rapid increase in "forced resters" and of the remaining clients, the portfolio quality must be rapidly declining, as they are the defaulters holding back the rest of their centres!

It seems that SEF clients are quite loyal to SEF. Again, they like the programme features – except for the problem presented by "Patching". What can be done? SEF should be able to work with the clients and arrive at a successful solution on how individual responsibility can be added into the programme. The main "problem" seems to be that paying clients have their hands tied by the institution's inability to pursue the defaulters for whom they bear financial responsibility – and for whom they bear the punishment in not being allowed new loans.

Many MFIs groups in other countries write their own by-laws. In these by-laws, each group decides what "punishments" should be meted out for infractions like late coming, missing meetings and non-payment. This could allow the group to demand collateral from each other, if the MFI does not want to do so. Agreement with some local authority to accept these "by-laws" and assist in collection, should it become necessary, may be sought. While clients may be far "harsher" than the institution, they will be agreeing among themselves to these terms.

Research in Bangladesh and East Africa shows that group guarantees are generally only effective in the first few loan cycles. After that, the possibility of continued access to desired financial services is the driving force for clients to repay. The current system punishes those who told researchers how much they valued not only the loans, but also the R2 savings – which were used up by defaulters. SEF should further investigate changes to the Patching policy, including separate savings accounts for voluntary savings untouchable by the group.

Provident South Africa and Weekly Payments/Interest/Instalment Size

Changes in instalments size, loan term and interest have confused clients and made them feel "had". They seem suspicious that they are being cheated. Clarification with clients as to how the rate is calculated and why changes are being made is called for. Since PSA is likely re-forming, there is an opportunity to start over with a "clean slate" whereby interest and instalments are adjusted to meet clients' wants and needs. The interest is higher than other MFIs, but the delivery method is also far different, and "less expensive" in terms of time, money (guaranteeing others) and transport. Clients did *not* seem put-off by the amount of interest as much as they did with the size of the instalment payment.

It could also be that clients are inadvertently taking on more debt than they can handle. The researchers did hear that clients were urged to take higher loans so as to increase an Agent's portfolio. If this is accurate then again Agent commission structure needs to be taken into consideration as does ensuring that clients, Agents and PSA staff have the skills needed to assess credit capacity.

Not all clients want weekly loans as is evidenced by the "flexibility" of payments allowed to clients via the 67% rule. However, this rule also seems to run counter to experience in most MFI programmes whereby allowing clients to get away with a little, eventually leads to clients getting away with a lot! Instead, offering payment options (weekly, fortnightly or monthly) based on the type of business and the prior history of a client might lead to improved on-time payment. It is strongly recommended that tolerance of past dues be rid from the programme as a policy. Zero tolerance of past dues should be implemented – at very least, publicly.

Offering options like monthly loans should do away with the need for what is now called "flexibility". In addition to this, PSA with its excellent MIS should be able to take on board these options and perhaps some others. The researchers found many "school sellers" who found themselves in payment trouble

during the school holidays. If this makes a significant portion of clients, could PSA (or SEF) possibly create a school-seller's loan that disburses prior to school terms, and is repaid before the next holiday?

5.3 Increased individual responsibility

Looking at the area of the Northern Province, PSA (or its successor) and SEF appear to be in a market ready and looking for suitable financial alternatives. While there are many cash lenders, there are few charging a reasonable rate for services. However, it does seem that the "stick" may be needed, even desired to a certain extent, in order to ensure repayment. The credit culture appears to be quite strong, but a willingness to "see what I can get away with", also appears quite strong.

Some clients recommended that they be asked for collateral. In some cases this was in conjunction with asking for individual loans (SEF), but also group guarantors asked for this protection so as to ensure that the group was able to collect loan payments. The collateral could be, as other MFIs have done, not so much things of monetary value, but rather things that make money. For example, the carpenter pledges his saw; the *spaza* owner may pledge her shelves, or her calculator. Some SEF clients said fridges would be appropriate, or beds and sofas. The idea was that clients should understand that loans were serious business and therefore, the threat of losing something important would be impetus to make all payments, certainly more than the group guarantee would.

Additionally, late payments could be charged a penalty. PSA clients are told they have no default charges, and delinquents/defaulters at SEF cause those that have paid to lose their savings or opportunity for follow on loans. Some clients at PSA said that they would be happy to "pay for" the ability to extend their loan or miss a payment due to business or personal problems.

In one way or another, PSA and SEF could seek (legal or local) redress. In the case of PSA any collusion between an Agent and a client to take on a loan with intent not to renege would be limited by loss of collateral and potential prosecution. Few borrowers would want to take the chance. If PSA (and SEF) were able to go to the police, *Induna* or other local leadership for assistance, the stance would change. Again, the loan would take on greater risk – which seems appropriate as accepting credit for one's small business is a serious step and a risk.

Clear policies surrounding these issues, and the institution's commitment to enacting these steps are, of course required.

Appendix 1: Methodology

The research relied on primary Qualitative Research. Some secondary research included: reports as cited within the text, the MIS systems of Provident and SEF, and SEF's own prior research into dropouts. Qualitative Research Tools used were:

Focus Group Discussion:

In groups of 6 – 12 clients, a trained moderator uses a guideline to maintain the focus of the discussion on the reasons for clients dropping out of MFIs. A Discussion Guide is a set of "open" questions that promotes descriptive answers and discussion. A discussion guide should translate the research objective into areas of questioning to ensure that the discussion does not deviate into interesting, but irrelevant discussion. The "main questions" are supplemented by probing questions that look deeply into the "how, why, who, how often" issues.

The FGD Guideline follows.

Participatory Rapid Appraisal

In groups of 8 – 12, a facilitator assists participating communities to utilise tools, which help the community and the facilitator to collect and analyse information about their own lives and community.

The tools can be divided into those for Needs Analysis, Product Analysis, Financial Landscape Analysis and Impact Analysis.

For Needs Analysis

- Seasonality tools (of Income, Expenditure, Savings and Credit)
- Life-Cycle Profile to trace cash needs over time

For this research, Seasonality Analysis was used to investigate the clients' needs for Savings and Credit – as their income and expenditures change throughout the course of the year.

For Product Analysis

- Ranking – Product Attribute Ranking; of Problems/Risks faced by a community; of reasons for default etc.
- Relative Preference Ranking – of key issues/attributes
- Pair-wise Ranking – of key issues/attributes
- Wealth Ranking – simple and detailed

For this research Product Attribute Ranking was used to investigate the attributes most important – positively or negatively – to clients.

Wealth ranking was utilised in the case of Provident clients as SEF already uses wealth ranking to target their clients. This tool was used to determine if the relative wealth of clients was a determinant in dropping out.

Financial Landscape Analysis

- Venn diagram analysis of groups/organisations and their roles
- Cash Mobility Mapping
- Financial Services Matrix
- Financial Sector Trend Analysis

Financial services Matrix and Sector Trend Analysis were utilised to discover other financial services available in the communities, their levels of importance, the attributes of these alternate services and the trend of their use/popularity by the community

The clients met and the tools used can be seen from the following tables.

SEF	Date	Place	Number	Women	Men	Staff	Current clients	Drop-outs	Non-clients
Focus Group Discussion									
SEF	28/6/01	Nwaxinyamani	10	10	0	0	10	0	0
SEF	28/6/01	Nwaxinyamani	4	4	0	0	0	4	0
SEF	29/6/01	Basani Village	6	6	0	0	6	0	0
SEF	3/7/2001	Masia Village	4	4	0	0	0	4	0
SEF	6/7/2001	Bungeni	5	3	2	5	0	0	0
SEF	6/7/2001	Mashau Village	16	16	0	0	16	0	0
SEF	8/7/2001	Bungeni	5	5	0	0	0	5	0
SEF	5/7/2001	Mashau Village	5	5	0	0	5	0	0
Product Atribute Ranking									
SEF	16/7/01	Basani	4	4			1	3	
Ranking reasons for Dropout									
SEF	16/7/01	Bungeni	6	6			1	5	
SEF	17/7/01	Nhjokanjhaka, Shavinyame Village	7	7				7	
Seasonality									
SEF	16/7/01	Shivambu	16	16				6	10
Wealth Ranking									
SEF	3/7/2001	Masia Village	12	12	0	0	12	0	0
SEF	4/7/2001	Shabinyani Village	10	10	0	0	10	0	0
Financial Sector Trend Analysis									
SEF	29/6/01	Bungeni taxi rank	8	8		0	0	0	8
SEF	30/6/01	Bungeni off main rd	8	1	7	0	0	0	8
SEF	17/6/01	Madobi	15	15			8	4	3
SEF	14/6/01	Tzaneen	2	0	2	2	0	0	0
			143	**132**	**11**	**7**	**69**	**38**	**29**

PSA	**Date**	**Place**	**Number**	**Women**	**Men**	**Staff**	**Current clients**	**Drop-outs**	**Non-clients**
Focus Group Discussion									
PSA	14/6/01	Botlokwa	10	9	1	10	0	0	0
PSA	15/6/01	Botlokwa	4	2	2	0	4	0	0
PSA	19/6/01	Louis Trichardt	10	9	1	0	8	2	0
PSA	20/6/01	Ravele	6	5	1	0	5	0	0
PSA	22/6/01	Botlokwa	5	5	0	0	0	5	0
PSA	25/6/01	Ravele	4	3	1	0	0	4	0
PSA	27/6/01	Botlokwa	5	5	0	0	5	0	0
PSA	26/6/01	Ravele	12	6	6	0	0	0	12
PSA	26/6/01	Ravele	7	5	2	0	0	0	7
			63	49	14	10	22	11	19
Product Attribute Ranking									
PSA	18/6/01	Seshego	10	10	0	0	10	0	0
PSA	21/6/01	Lebowakgoma	12	9	3	0	12	0	0
PSA	21/6/01	Lebowakgoma	8	8	0	0	8	0	0
			30	27	3	0	30	0	0
Ranking Reasons for Dropouts									
PSA	18/6/01	Seshego	9	8	1	0	9	0	0
PSA	20/6/01	Louis Trichardt	5	5	0	0	5	0	0
PSA	20/6/01	Ravele	6	6	0	0	0	6	0
PSA	25/6/01	Madobana	6	5	1	0	0	6	0
			26	24	2	0	14	12	0
Financial Sector Analysis									
PSA	14/6/01	Louis Trichardt	12	2	10	12	0	0	0
PSA	19/6/01	Louis Trichardt	8	7	1	0	8	0	0
			20	9	11	12	8	0	0
Individual Interviews									
PSA	14/6/01	Botlokwa	1	0	1	1	0	0	0
PSA	15/6/01	Pietersburg	1	0	1	1	0	0	0
PSA	15/6/01	Pietersburg	1	0	1	1	0	0	0
PSA	15/6/01	Pietersburg	1	0	1	1	0	0	0
PSA	22/6/01	Pietersburg	3	1	2	3	0	0	0
			7	1	6	7	0	0	0
Totals:			**146**	**110**	**36**	**29**	**74**	**23**	**19**

Welcome

- Thank you for coming – we are grateful for your time.
- We are from an organisation called ***MicroSave. MicroSave*** is a research organisation that looks at financial services for people who do not have access to banks. We try to ensure that the clients' voices and ideas are heard by the organisations which provide financial services to poor people
- We are holding these discussion groups to try to understand clients' reasons for dropping-out of MFIs' programmes.
- We would very much like to record these discussions to help us remember them and so that we do not miss any of the issues and ideas you give us. The details of these discussions will not be shared with your MFI and your names will be kept confidential – so please do not be concerned and feel free to express your opinions about the products openly
- As a first step we should introduce ourselves. Please you start and we will follow. My colleague here will prepare name-tags to help us remember your names.

Core Questions	***Probes***
***Warm-up Question**s* 1. Please tell us how long you have been with the MFI? 2. What is your business do you run? 3. What makes people like you decide to join the MFI? 4. What makes people decide to leave the MFI?	• (If interesting response) Have these expectations been met?
Core Questions	***Probes***
General Questions For what purposes did you use the loans you took from the MFI? Did the loans allow you to meet your needs? If not, why not?	Why did you borrow from the MFI? How did you use the loans you took from the MFI? Were the loans offered by the MFI appropriate for your needs?
Impact on Drop-outs Questions: 1. What are the main reasons for clients leaving your groups? 2. Have you seen a change in the number of people leaving the group in the last year? If so, why? 3. Who makes the decision that people will leave the MFI programme? 4. What should the MFI do to further improve its loan programme? 5. What procedures or systems would you like to see change in the MFI? 6. In what other ways could the MFI have better met your needs?	▪ For what reasons did the last three people who left your groups decide to leave? ▪ NOTE: Ensure that the reasons are carefully probed to discover underlying reasons[18] ▪ Is the number of people leaving the MFI increasing or decreasing? Why is this happening? ▪ Who are the people that decide that members should leave the programme? ▪ Please make recommendations on how the MFI might revise its loan programme to better suit your needs. ▪ If you were the manager of the MFI which rules would you change to reduce dropouts from the programme? ▪ Describe other ways that the MFI might help its clients and retain them as members of the organisation.

Closure

Thank you your answers and discussion have been very helpful and informative.

We are very grateful for the information you have provided.

Do you have any questions or suggestions for us?