Low Income Lives

MicroSave
Market-led solutions for financial services

The daily costs of debt: Problematising repayment

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Author:
Mathilde Maîtrot

The theory

Microfinance represents a hallmark of modern development initiatives. Widespread claims from the sector assert that it offers a sustainable solution to poverty, supported by impressive 99% repayment rates. For Bangladesh, more than any other country, microfinance also symbolises the nation's economic and social development, with growth in the sector and the sustainability of its institutions coalescing with the persistent decrease in poverty and extreme poverty rates at the national level. Its fame has, however, drawn tough scrutiny from international donors and researchers concerned with its impacts on the ground.

Commonly, analyses and critiques of microfinance pay particular attention to interest rates, loan sizes, and target groups — "are clients poor enough?" This blog, in line with two other pieces published by colleagues as part of this series on repayment, has a different focus and scrutinises what lies behind the commonly reported 99% repayment rates.

But you may ask since research has shown that poor people can save, they can presumably also repay their loans, so why make a fuss about repayment? There are two important reasons here. First, interrogating this is particularly significant – as the potential of microfinance depends on the scope for profitable and sustainable investment by poor borrowers. Second, as this blog will show, its importance has less to do with whether the poor can repay, and more to do with how they repay, and how repayments affect their lives. Before saluting poverty-alleviation trends and attributing them to microfinance[1], we, therefore, need to look more closely at how the poor repay their debt to MFIs.

Method and data

In this article, I draw upon the quantitative and qualitative insights gained from a large community survey and from interviews and focus groups with villagers and MFIs credit officers. The survey covered 490 households and 4,022 villagers in four villages in Bangladesh (anonymised hereafter) over the course of a year. Thirteen MFIs operate in the four villages studied, including local, national and international NGOs, commercial banks, state banks, international banks, and government-initiated programmes. These institutions combined have provided loans to a sizeable majority of the population studied, with 60% of people being active borrowers and 5% former-clients. The remaining 35% of households have neither used nor registered with any MFI.

In the absence of a baseline study, I used reported perceptions of variations in well-being to explore the fortunes of client, non-client, and former-client households. Although these variations in perception can be influenced by unobservable endogenous factors outside of microfinance, not captured by this study, the figures below (Table 1) provide scope for understanding the significance of the reported impact.

1. We may attribute positive figures, of course, to a myriad of other factors, such as uninterrupted economic growth, remittances, and the government's social protection programmes.

Table 1: Households and livelihood trajectories

	Improving		Stable		Declining		Total	
	cts*	%	cts	%	cts	%	cts	%
Client and former-clients	108	33.9%	113	35.4%	98	30.7%	319	100%
Non-clients	46	26.9%	85	49.7%	w	23.4%	171	100%

*cts: counts, number of households
Source: community survey results

The community survey results show that on average, for 32.5% of the studied population, the primary financial concern[2] is education. For 26.5% of the population, it is asset acquisition, and for 21% it is food provision, followed by medical care (6.5%), wedding-related costs (5%), and loan repayment (3%). Moreover, after establishing the poverty status of households included in the studied population, we can observe that the livelihood trajectories of households vary significantly according to their poverty status, as Table 2 indicates.

Table 2: Households' livelihood trajectories by MFI and poverty status

	Improving		Same		Declining		Total
Current-clients	cts	%	cts	%	cts	%	cts
Non-poor	29	66%	10	22.7%	5	11.3%	44
Poor	54	36%	63	42%	33	22%	150
Very poor	19	19.6%	28	28.8%	50	51.5%	97
Total current-clients	**102**	**35%**	**101**	**34.7%**	**88**	**30.2%**	**291**
Former-clients	cts	%	cts	%	cts	%	cts
Non-poor	1	50%	1	50%	0	NIL	2
Poor	3	23%	7	53.8%	3	23%	13
Very poor	2	15.4%	4	30.8%	7	53.8%	13
Total former-clients	**6**	**21.4%**	**12**	**42.8%**	**10**	**35.7%**	**28**
Non-clients	cts	%	cts	%	cts	%	cts
Non-poor	15	45.5%	15	45.5%	3	9%	33
Poor	29	31.1%	46	49.5%	18	19.4%	93
Very poor	2	4.44%	24	53.3%	19	42.2%	45
Total non-clients	**46**	**26.9%**	**85**	**49.7%**	**40**	**23.4%**	**171**

* cts: counts, number of households

2. Households could only provide one answer.

Findings

Performance and discipline

For the large majority of respondents, repaying loans was a daily struggle. Although the loans were of relatively low value, ranging from USD 26 to USD 77, the terms and structure of repayment placed a huge challenge on household financial management. The repayment of these loans is scheduled largely on a weekly basis. Each MFI collects repayment from one neighbourhood at one particular time and day of their choosing. For example, BRAC on Monday at 5pm, Grameen on Tuesday at 11am, ASA on Wednesday at 3pm, BASHA on Thursday[3] and so on.

MFIs in Bangladesh are known for enforcing **strict on-time** repayment. MFIs use strict repayment policies as a disciplinary device to ensure their employees maintain a sustainable financial performance. Failing to bring the exact expected repayment amount back to the MFI branch has severe consequences for the career prospect and status of MFI employees. The means used to ensure that repayments are collected on time is effectively up to credit officers themselves. The nature of the means deployed can, therefore, vary from persuasion to pressure, humiliation, manipulation, and coercion.

Living by default

In response to such pressures, households adapt their behaviour, in ways that have significant financial and social impacts on their lives. Mainstream development literature and policymakers often use the term “coping strategies” to refer to the means through which households cope with shocks and events and mitigate risks associated with them.

However, the term “strategy” emphasises a calculative behaviour and planned development, when defined as a “skilful use of a stratagem” or “a plan, method, or series of manoeuvres or stratagems for obtaining a specific goal or result” (*The Random House Dictionary*, 2011). As will be demonstrated below, the data collected shows how, once indebted, constraints – rather than choices – dominate the livelihoods of client households. Therefore, the term “strategy” becomes inadequate to describe their coping process.

Poverty and vulnerability

People who are poor often not only lack income or assets but are also vulnerable and susceptible to experience further poverty and forms of marginalisation. In rural Bangladesh, seasonality directly or indirectly affects the sources of such vulnerability, whether their livelihood relies on agriculture or not. Following harvest cycles, significant variations in food production affect the availability and price of food in rural areas, and indirectly the diet of households.

3. BRAC, Grameen, ASA, BASHA are all MFIs operating in the area studied.

For households that are headed by women, the loss of the main income-earner remains the key driver of poverty and vulnerability, as women experience marginalisation and discrimination in the labour market. In this context, the earnings of vulnerable households, male or female-headed, can vary irregularly week-by-week, month-by-month, and seasonally.

Strict repayment schedules add a substantial additional pressure on the changeable earnings of poor and vulnerable households. Repayment tactics pursued often result from minimal or no choices and opportunities available to clients. These involve reducing food consumption or quality, selling assets, borrowing money from informal sources or pushing children to drop out of school to work and earn.

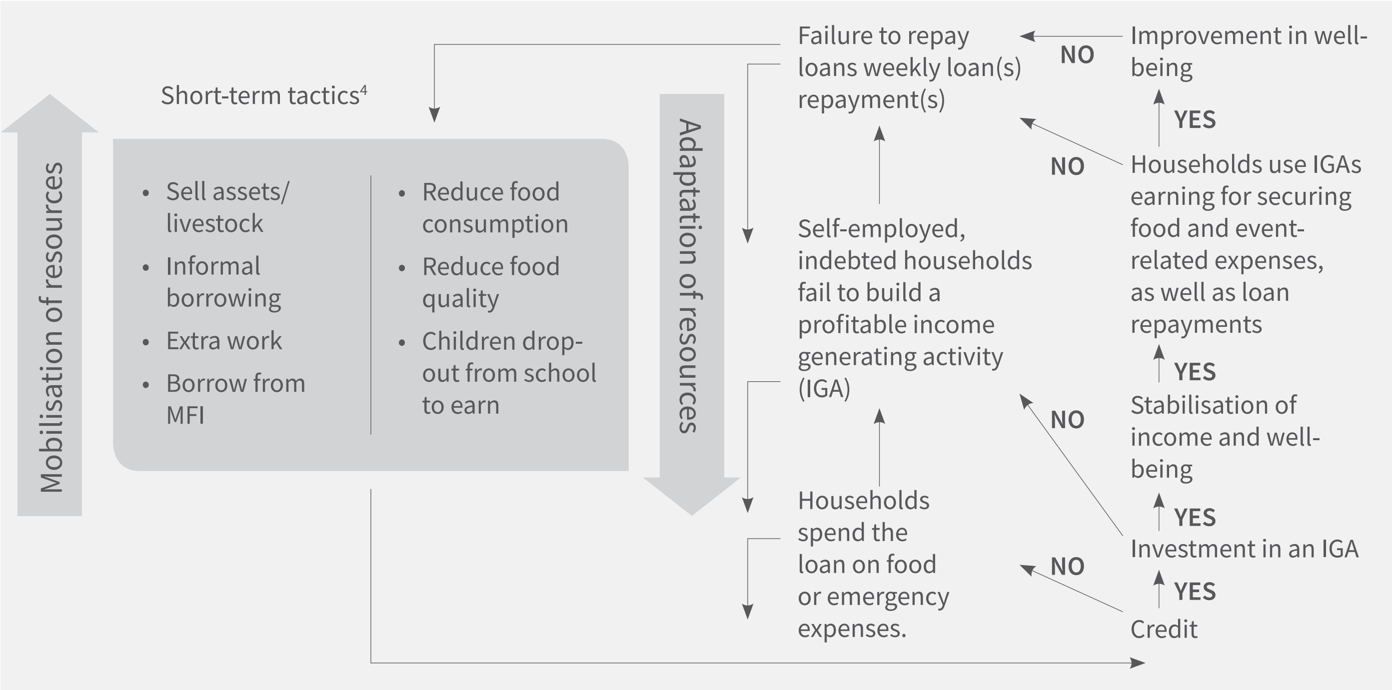
During the 'coping' periods, households are not protected from the persisting "unexpected". When sudden shocks and events emerge, they need to spend, urgently a possibly adapt their livelihood. These shocks may include be internal to the household, such as illnesses or deaths. They may also include hazards external to the household, such as flooding, cyclones, or robbery (and the loss and destruction of assets they often incur). As one respondent Farida described:

> Author: "Then why don't you do something with the money you took?"
>
> Farida: "Loans were all spent on food. I did not get a chance to do anything else with them. Then if someone falls sick, I have to pay for it. It is so hard to give up. Sometimes I wish I had no loans, there are people from the village who ran away because of these loans."

The vulnerability of households to shocks, exacerbated by poverty, unexpectedly absorb their reserves and future earnings, if any. When coping tactics are few, it can precipitate households towards a downward coping spiral. Figure 1 illustrates this process, with "NO" signifying the occurrence of shocks prompting an overwhelming need to spend earnings on unforeseen outlays.

For these households, coping with shocks while repaying loans transforms their livelihoods into a series of consecutive short-term tactics. These short-term measures often absorb their income and erode their energy and networks in ways that preclude them from building a financial buffer.

Figure 1: Experiences of loans



Source: the author

Extra work

Labour is a major resource and also the most exposed means households have to cope with adverse shocks and hazards. However, working more or harder constitutes a limited and risky coping tactic. In rural Bangladesh, a household is a complex family-based social unit composed of one to 15 or more people who are typically related by blood or matrimony. Members of a household "eat from the same pot", as sharing food commonly recognises the members' belonging to reciprocal ties. Conventionally, men bear the financial responsibilities of their household members by providing their labour to earn and meet their basic needs. It is considered the man's responsibility to provide his parents, wife, and children with food and security.

The availability of extra work when needed is not guaranteed due to unemployment, few market opportunities, and market saturation. In low income families, income-earners, therefore, often already work as many hours as they can. Extra work endangers their health, for instance, while working in adverse weather conditions or taking up hazardous occupations. One of the major sources of vulnerability is health. Diseases, illnesses, or disabilities of one of the household members – whether it is occasional, chronic, or temporary, can have serious long-term effects on the income and livelihood of households.

4. Access to and affordability of tactics largely depend on the household's asset endowment, composition, and livelihood.

A large majority of women (96%[5]) are *grihini*, which means housewife. For them, working outside their home to earn can throw disrepute on their household and have negative implications on their daughters' prospects for marriage, which is a matter of great concern for poor and extreme poor households. A woman who works to generate an income can be an indicator of extreme poverty in this context, as they would be likely to either be widowed or have husbands who suffer from severe illness or disability. The opportunities for paid work for women or children are often precarious and, in some cases, expose them to more social and physical risks.

Selling assets

One way that households cope in response to pressures from credit officers to repay loans while faced with adverse shocks and hazards is by renting out or selling assets. These assets include jewellery, land, livestock, or furniture. Assets can be transformed into liquidity easily but not always on favourable terms when dealt with urgently. Very poor households often cannot use this tactic as they have no or few assets to sell. This partly explains the aspiration of households to own assets and build a buffer in preparation for shocks or events. Although respondents acknowledged that saving lump sums for acquiring assets is critical, they perceive the saving process as "tiresome" as it can represent huge opportunity-costs and efforts for people who live on low and unreliable incomes.

Informal borrowing

Among respondents, borrowing money from informal networks like family, neighbours, friends, or moneylenders is common. They may use the money for either predictable expenses like a daughter's wedding, asset repair, debt repayment, or for unexpected needs like medical treatment. Informal borrowing generally represents a fast and convenient way to address an urgent need of liquidity. It help them meet liquidity-needs without the borrower needing to travel to the town, face bureaucrats, or speak to strangers about personal financial matters. Informal borrowing also usually avoids the risk of rejection. It constitutes an important dimension of people's livelihood and social lives and one of the most common ways households mobilise resources.

Access to peer networks depends on the level of connectedness that a household has and its reputation in the community. Peers and relatives from whom households borrow understand the changeability of their livelihoods and irregularity of their earnings. The terms of informal borrowing from peers and relatives are therefore often flexible and offer possibilities of re-scheduling repayment. During a group discussion with other declining and stable clients, Anuwara (35, housewife) explained why she reluctantly borrowed from her peers to repay her loan:

5. The remaining 4% are widows or abandoned women.

> "To repay Grameen, I first loaned money from ASA then had some difficulties in paying the instalments. So, I borrowed money from others [peers and relatives] just so that I could meet the instalments. Then I stopped with ASA. I admitted myself in Society and again I missed many instalments and would borrow money from others [peers and relatives]. Eventually, they quit on me too. Then I went to BASHA. If I am able to pay then it is all good but I have to survive too so I had to borrow money from others often".

For the poor, borrowing cash from peers is a limited and possibly risky tactic. This is because peers often experience similar seasonal variations and share the associated risks. When the poor multiply their informal lending sources to repay loans, their financial and social lives become further interlaced. This exposes their economic choices to the judgement and critique of their peer group. Moreover, informal borrowing as a repayment tactic depends crucially on the access of households to social networks and almost always implies a degree of reciprocity between the two parties.

Because of their low capacity to repay, informal lenders often consider poor and vulnerable households too risky to lend to. The poor are therefore susceptible to being excluded from informal reciprocal networks in their community (although they might benefit from donations). The fear of eroding their social networks also prevents the poor themselves from accessing them, as they are afraid of bringing shame and becoming further marginalised.

Moneylenders often represent an alternative to the peer group. However, while loans from peers or relatives are often virtually interest free, interest rates practiced by moneylenders represent a non-negligible barrier for poor households. When financial risks are too high, vulnerable households often prefer to avoid them. As a result, poor and vulnerable households usually tend to either be excluded or self-excluded from those transactions to avoid the risk of conflict and the humiliation of failing to repay their lenders.

Yet, when loan repayment is due, poor and vulnerable households are more likely to enter a patron/client relationship with local moneylenders, accepting unfavourable terms. Sometimes, this relationship becomes exploitative for borrowers and can result in violent disputes when the repayment is not met – including threats, physical violence to the borrower and family member, harassment, asset destruction, and even robbery.

Table3: Source of cash in case of emergency

	Phamillia	Rickshapoor	Bhaatbag	Saripur	Average
Own savings	7.7%	10.8%	7.5%	32.5%	14.5%
	10	10	11	40	71
Selling assets	11.6%	6.5%	8%	5%	8%
	15	6	12	6	39
Extra work	8.5%	3.8%	6.8%	3.3%	5%
	11	4	5	4	24
Borrow from:	1.5%	NIL	NIL	NIL	.4%
NGO	2	NIL	NIL	NIL	2
Bank	8.5%	3.8%	2%	NIL	3.5%
	11	4	3	NIL	18
MFI	27.3%	42%	43.5%	33.6%	36%
	35	38	64	41	178
Family	17%	14.4%	16.3%	11%	15%
	22	13	24	14	73
Neighbour	11.6%	8.6%	7.5%	8.1%	9.5%
	15	8	14	10	47
Moneylender	3.1%	7.6%	3.2%	7%	4.7%
	4	7	5	7	23
No option	3.1%	2%	6%	NIL	3%
	4	2	9	NIL	15
Total	100%	100%	100%	100%	100%
	129	92	147	122	490

Source: community survey results

Multiple borrowing

A further strategy that households deploy to deal with the pressures to repay as well as to cope with adverse shocks and hazards is borrowing from multiple formal sources. Figure 2 illustrates this phenomenon.

Figure 1: Categorisation of households by client-ship statuses and participation patterns[6]

Current-clients 60%	Single MFI client-ship (40%)
	Multiple consecutive MFI client-ships (8%)
	Multiple MFI client-ships (52%)
Former-clients 5%	Single MFI client-ship (30%)
	Multiple consecutive MFI client-ships (20%)
	Multiple MFI client-ships (50%)
Non-clients 35%	Multiple MFI client-ships (50%)
	Not interested or self-excluded (too rich or too poor) (70%)

Source: the author (inspired by Matin et al, 2003

Households often resort to taking multiple loans that are not invested in any income-generating activity. This is because they generally use this tactic as a short-term means of coping. The impact of multiple client-ship on the household's well-being often depends on the situation of the borrowing household when the loans are taken and on how the household uses them. While some households manage their loans in a way that allows them to maintain their wellbeing, other households cannot bear the pressures that constant borrowing and frequent high repayments can have on their livelihood. During a group discussion, Aklima and Sophya shared their experiences of multiple borrowing.

6. The percentages presented in this diagram are based on the quantitative data collected (the left cells) and on the estimation of the author (based on participant observations, field notes, interviews, and informal discussion with community members).

Aklima: “Well, I took a loan from one of the organisations and I am paying back in instalments. Then I needed more loans, so I went to another one for that reason. I needed loans for different reasons.I had to get my daughter married so I had to take a loan from one [MFI]. Then I needed loans to pay medical expenses, so I took a loan from another one. I am paying everyone back bit by bit.”

[…] Sophya: “My husband took BDT20,000 [approximately USD238] from one organisation where I have to give back BDT600 per month [approximately USD7.15]. That is a lot to pay off per month. So I decided to take more loans from another one to pay for the first one. […] Initially I was doing well. I took the loan and spent it and then I had to ask from another bank [the term bank is used commonly to refer to MFIs]. Now I am affiliated with many banks. I am always taking loans and I am always paying back. I cannot get out of it. It is tough to pay back the loans. But we are keeping up somehow.”

Reports collected from clients indicate that credit officers know of the clients’ financial distress and multiple client-ship. However, numerous clients reported that credit officers either choose to ignore it or even encourage clients to take more loans to repay existing debts. In the four villages studied, respondents stated that credit officers are aware of the destructive coping tactics clients adopt to repay, and reported that credit officers sometimes encouraged them to borrow from other MFIs to repay on time and continue borrowing larger sums.

Moving from one coping tactic to another, poor and vulnerable clients generally struggle with extreme trade-offs between the need to repay their loans and covering the basic needs of their household members.

In summary

A small proportion of poor clients can afford to save on a regular basis and repay their loans. For them, microfinance can be used as a means to ‘smoothen’ consumption. This is possible when the earnings and expenditures of clients are relatively regular and predictable. Yet a large proportion of people in the studied context are vulnerable and are exposed to health, climate, seasonal-related shocks and hazards. The repercussions of debt on their lives can become problematic as their ability to cope is limited.

As a result of coping tactics being used simultaneously, the livelihoods of the vulnerable poor become increasingly hazardous and unfavourable. Over long periods of time, they develop a short-term vision of their livelihood, whereby the quality of their lives partly depends on their ability to afford weekly repayments.

The incentive structures within microfinance institutions and their management system rely on households continuously taking up loans. Therefore, rather than being aligned with or supporting the long-term livelihood strategies of clients, multiple client-ship especially can lead to an exhausting debt cycle, where repayment depends on loans and not income from continuous labour and earnings.

The exacerbated vulnerability of poor clients, combined with rigid organisational structures nurture a form of short-termism that can further their marginalisation. What this reinforces then is a need to focus not on whether poor clients repay, but on how clients who are poor and vulnerable repay, and at what cost.

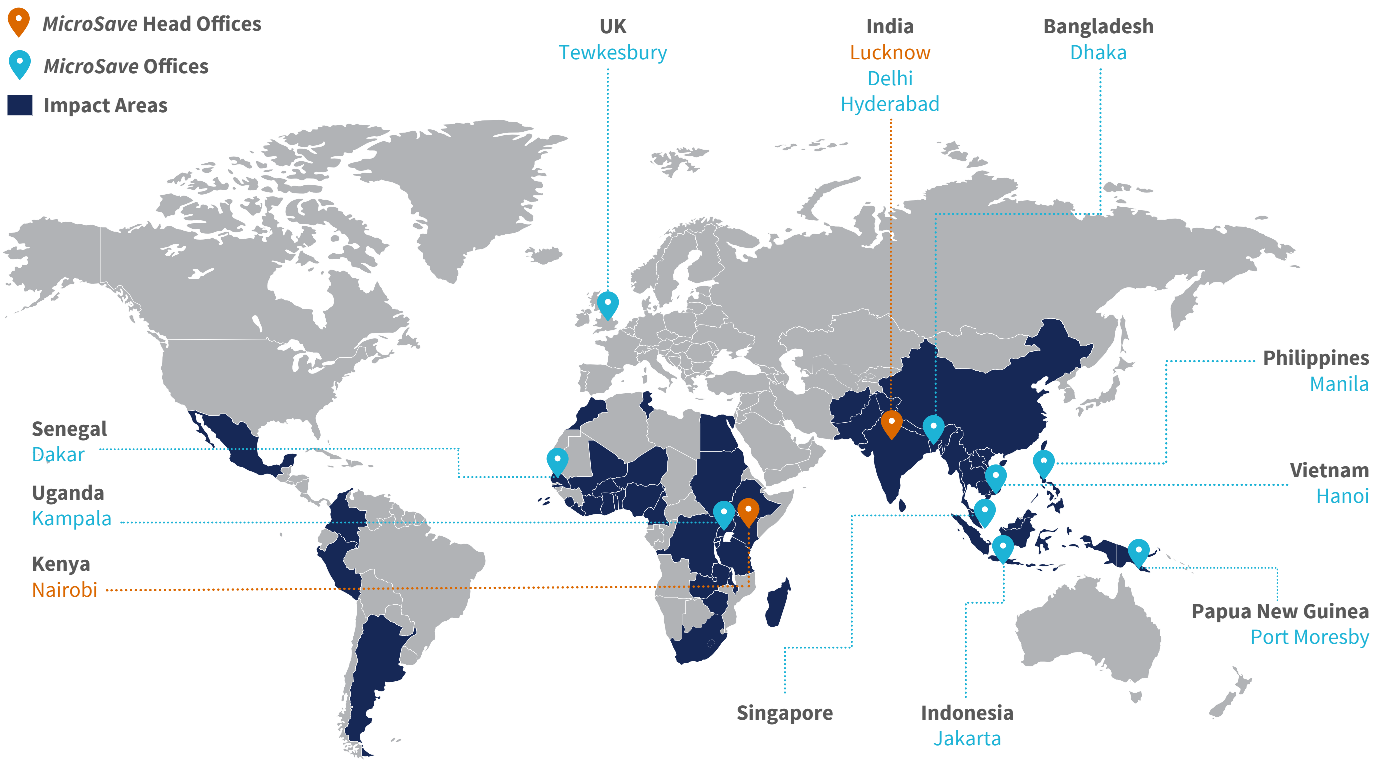
Author: Mathilde Maîtrot

Mathilde Maîtrot is a Lecturer in International Development and Global Social Policy at the University of York and a member of the Interdisciplinary Global Development Centre (IGDC). She is also an Honorary Research Fellow at the Global Development Institute where she completed her PhD examining the social performance of microfinance institutions (MFIs) in Bangladesh.

In a 2018 article published in *Development and Change*, Maîtrot examines the emergence of a ‘practice drift’ at the branches of MFIs that, among other things, affects loan allocation, targeting, repayment methods, and loan use.

About *MicroSave*

MicroSave is an international financial inclusion consulting firm with nearly 20 years of experience, operating in eleven offices across Asia and Africa. Our mission is to strengthen the capacity of institutions to deliver market-led, scalable financial services for all. We guide policy, provide customised strategic advice and on the ground implementation support.



www.*MicroSave*.net

Asia Head Office

28/35, Ground Floor, Princeton Business Park, 16 Ashok Marg,
Lucknow, Uttar Pradesh, India 226001

Tel : +91-522-228-8783 | Fax : +91-522-406-3773

Email: Manoj@MicroSave.net

Africa Head Office

Shelter Afrique House, Mamlaka Road, P.O. Box 76436,
Yaya 00508, Nairobi, Kenya

Tel : +25-420-272-4801 | Fax : +25-420-272-0133

Email : Isaac@MicroSave.net