MicroSave India Focus Note # 108

How Can BC-MFIs Tap Household Savings?

Akhand Tiwari, Akhilesh Singh and Graham A N Wright

October 2014

In India, MFIs that offer savings products to their clients are not able to attract savings because they are not perceived as savings service providers by their clients!

Microfinance institutions (MFIs) in India offer savings products in partnership with commercial banks under the business correspondent model (BC-MFIs). Indian MFIs are limited by regulations and only banks and deposit-taking NBFCs are legally permitted to offer savings products. Partnerships between MFIs and banks provide specific value propositions for both, and as a result, many MFIs offer savings products via these collaborations. We have witnessed successful and less fruitful examples so far—both of which provide meaningful insights for regulators and practitioners alike. In this Note we focus on an issue that MFIs often face—that clients do not adequately transact in their savings accounts.

There could be many reasons for this behaviour. We know that borrowing from multiple sources and year-on-year borrowing are common activities amongst MFI clients. Do they live credit-led lives? Do they use credit products in order to meet their household expenses? What savings avenues do MFI clients currently use and for what purposes? Are there any distinguishing characteristics of those avenues?
MFI clients were using various methods of saving that are in line with our existing understanding of the financial lives of the poor.[1] So we explored why some savings avenues are preferred by MFI clients. Based on previous analysis of the savings behaviour of low-income customers in Asia and Africa, we used three parameters to understand their behaviour: 1. longevity of association with financial institution; 2. the value of the savings (how much a client would save by that particular method); and 3. frequency with which savings are made (regularity of saving).

> We talked to MFI clients in semi-urban and urban areas in central Uttar Pradesh. The MFIs used by these clients offered a savings product in partnership with a commercial bank. The accounts offered were basic savings bank deposit accounts.

Three Drivers of Savings Behaviour

We found that all the three could be described as functions of surplus (the amount kept aside by the client for saving), reliability (trust with the service provider), and operations processes (ease of access).

With respect to **surplus**, we observed that clients only deposit large amounts in banks. They are anchored to an amount of Rs.500 (US$9) as a minimum amount to deposit in a bank.[2,3] Lower amounts of savings are generally deposited with local groups or with chit fund companies offering a doorstep service. Some clients accumulate daily surpluses at home to create a lump sum of Rs.500 or more, and then deposit that at the bank. However, this requires discipline and commitment from the client as daily expenses often mean that the surplus amount is spent before the client is able to deposit it. Many clients say that they know they will not be able to save such a large sum, and to avoid spending what they have, they save smaller surpluses with local saving groups.

The **reliability** of the savings channel is the basis of a client's decision on how much to save and the period of association. A reliable avenue is used to build lump sums for medium or long-term purposes. Banks are reliable and thus used for long-term savings and higher-value deposits. In contrast a new local savings /chit group is likely to be viewed as less reliable. It will be used only for time limited savings – a year or six months with low deposit amounts of Rs.20-Rs.50 (US$0.30 – 0.75) per week to start with.[4] Lump sums created with these mechanisms are typically used for short-term purposes.

The **operational processes** of the savings avenue also dictate how frequently that particular method is used. Deposit-taking NBFCs, chit funds, and local savings groups are doorstep services that are used more frequently by clients due to their convenience. Banks require more complicated processes – time spent travelling to and from the branch, filling out application forms, etc.

Together, *surplus* collected by the client, *reliability* of the service provider, and the *operational model* help us to describe the mental model MFI clients have about

[1] Portfolio of the Poor, **Stuart** Rutherford, Ignacio Mas, *Kenya Financial Diaries*
[2] The amount of Rs.500 was mentioned by most MFI clients we interviewed. Their anchoring to this amount seems to be a result of the value attached to the amount – it is considered a substantial saving by MFI clients.
[3] Anchoring is a cognitive bias to rely too heavily on past reference or on trait or piece of information while making decisions. Read more here
[4] There are examples where low income households have saved with a new company. These could be classified under 'special instances' where returns on investments beat the reliability aspect.

savings. If we consider these elements together we understand why local savings groups are used more frequently, and why the amounts of those savings are low; and we understand more clearly why banks are used less frequently and why higher amounts are saved in them. Clients look around for convenient savings avenues and then choose based on how they fit into their mental models.

The Current Market Position of MFIs

If we apply this same test to MFIs, they typically meet the requirements of reliability since they have been serving customers with credit products for many years. MFIs also pass the test of accessibility, tied to operational processes, as they also offer doorstep services – typically once a week at the group meeting. However, MFIs are still unable to attract the small cash surpluses that local groups are able to attract. We could speculate there is an intention-action gap resulting from limited marketing and communication efforts by MFIs, or an image problem of MFIs.[5] The former is incorrect because many committed MFIs do make efforts to market and communicate their products. So we are left with image problem – that MFIs are just credit service providers. This appears to be the problem.

Saving with MFIs is not a practice that MFI clients have observed and, as such, MFIs do not fit into the mental models of the clients. One client we interviewed said, "*Who saves with MFIs?*" when asked why she does not use the savings account she opened with the MFI. Like her, many clients who opened a savings account with an MFI perceived the savings account as an element of the credit process—treating it much as they treat a compulsory credit insurance product as rider to access credit. Worse, many are concerned that MFIs will offset any savings held against outstanding or overdue credit balances. The savings account is not seen as a separate product or service. As a result, and despite regular communication from the MFI about their savings accounts, clients do not use them.

A typical MFI is positioned as a credit service provider. In order to increase the use of savings accounts, we need to reposition MFIs. Over time, and with more clients depositing their surpluses with MFIs and becoming *active savers*, MFIs can reposition themselves as comprehensive financial service providers. This is very much like the situation in the late nineties in India when MFIs struggled to position themselves as reliable credit service providers.

Tweaking Product Design to Change Market Position

In order to influence savings behaviour among MFI clients, we suggest simple tweaks to the design of existing savings products – very much in line with what many MFIs have done around the world. The principal element of such a design will *use clients' demand for credit to help trigger active savings behaviour to stimulate a habit of saving with MFIs*. MFIs can communicate that: 1. higher savings with their partner bank will demonstrate client's better debt service capacity and will quickly graduate them to higher loan sizes; and 2. that savings are held by the bank and can be withdrawn by the client independently of any credit balances with the MFI, and are thus flexible and safe.

This product must be combined with changes in the MFIs' branding to: 1. include the provision of saving services as key product offerings and 2. stress partnership with a commercial bank to capitalise on the trust in public sector banks.

MFI clients are always keen to create lump sums both in the short term and in the long term. They will like the fact that while they increase their chances of getting a higher loan, they also create a lump sum in the process, which they can keep or use for any expense. This will nudge clients into saving with MFIs in the short term. In the long term, clients will able to experience the benefits of small savings by realising the lump sums they have created. Their perception about MFIs will shift to seeing MFIs as comprehensive financial service providers.

Many MFIs in different countries already offer savings and credit products either separately or linked with each other.[6] It is essential to highlight that these product designs should never be communicated as compulsory savings. The MFI is essentially projecting higher loan amount as a motivation to save more with their partner bank. These are normal voluntary savings accounts – but demonstrated ability to save regularly and larger savings balances will influence credit decisions.[7] Where clients want, the savings could also be linked a specific goal – an aspirational commitment savings product that has worked well for many MFIs.[8]

If MFIs in India clearly project the benefits of linking savings with credit, and if they design in functional elements that do not add any operational complexity, these product modifications will provide positive results for them.

[5] Intention Action gap refers to disconnect between what a person wants to do and what the person actually does.
[6] Most clients see compulsory, locked-in savings tied to loans as increasing the total cost of credit.
[7] Some examples include, J-PAL's Green Bank Experiment, Commitment Savings Product in Malawi, Buro Bangladesh
[8] The *Jijenge* Account offered by Equity Bank Kenya, Card Bank in Philippines, and Janalakshmi