MicroSave Briefing Note # 42

Cash, Children or Kind?

Developing Security for Low-Income People in Old Age in Africa[1]

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Introduction

The number of people aged over 60 in the developing world is predicted to rise from 375 million in 2000 to 1,500 million in 2050 (Gorman, 2004)[2]. In sub-Saharan Africa the number of people aged 60 and over, will more than double in the next 30 years, despite the impact of HIV/AIDS on life expectancy at birth (Gorman, 2004). Africa's older population will have increased to 204 million by 2050 from the present 42 million (HelpAge, 2005a)[3] which will make more than one in ten in sub-Saharan Africa to be over 60 (Gorman, 2004).

Challenges of Old Age

'Old age', a relative concept, has been used in this paper in relation to the regular income earning capacities of people, regardless of age or source of income. Old age comes with some financial challenges. People get used to a regular life style during their productive years, which changes with age as they lose their direct source of income and thus become dependent on previous investments, if any, or on social safety nets.

Economic:

Small regular source of cash: For most of the respondents, meeting basic needs of food, shelter and clothing is the biggest challenge in old age. The issue is not the high cost of these consumption needs but that of planning to ensure a small but regular source of cash during old age.

Mismanagement of funds: Those people privileged enough to retire with a pension from a company or the government often receive a lump sum. In many cases, lack of knowledge on investment opportunities or of business acumen leads to the loss of the whole amount within a very short time.

Access to credit: The aged are often willing to shift to some work/business that demands less physical labour. As a result they may want credit to start a business but lack the necessary collateral in the form of assets or savings.

Social

Excess financial costs: The HIV/AIDS pandemic is shifting much of the responsibility for taking care of children to their grandparents - who themselves are often in old age and have meagre income. "… they are faced with the arduous task all over again of raising children and finding money for clothes, food and school and clinic fees" (Hampson, 2005)[4].

Social Challenges: When people retire their lack of engagement in work makes them feel unwanted, a problem exacerbated by the disintegration of extended family structures, which have left parents and grandparents uncared for.

Preparing for Old Age

MicroSave's study revealed both economic and social issues in relation to preparing for a secure old age. Respondents felt that Africans in general do not consciously plan for their future – there is little or no culture of saving up for future needs. Daily consumption needs take priority even though these are not always restricted to necessity items. Hence money, which could have been saved for the future, is used up.

The common activities that are taken up, more as traditional practices, rather than as a conscious preparation for old age, are as follows:

Investment in Assets: In simple terms, the common trends in investment may be categorised as follows. Those with

- Small savings commonly invest in small-scale farming (e.g. growing crops and rearing animals)
- Medium sized savings invest in small businesses (e.g. butcheries, trading or rent farms for commercial farming)
- Larger savings invest in plots and build houses for rent, or buy a tractor for work in large wheat farms.

Investment in Children: While school fees constitute a significant part of household expenditure, parents view this as an investment, assuming that children will take care of them in their old age. Depending on the social background, some send their children to school or engage them in vocational education to acquire skills through apprenticeship, while others invest in their children by ensuring they get to university and get good jobs.

Invest in parallel business: Many employed people invest in small agricultural projects or enterprises during their employment years. Their children or other family members run these, until the employed person themselves take over after retirement. Those who can accumulate a lump sum, invest in long-term business such as building schools or rental houses in the towns and cities.

Save Cash in Banks: Saving up in cash in banks is not the most common way to save. Most citizens of East Africa simply do not have enough faith in banks to entrust their long-term savings to them. In addition, banking charges are very high – particularly in Kenya.

[1] This ***MicroSave*** Briefing Note was prepared on the basis of the findings of the research conducted. The full paper is available on ***MicroSave***'s website: http://www.***MicroSave.net*** under - Study Programme

[2] **Gorman**, Mark, "Age and Security", HelpAge International, 2004

[3] Aging in Africa, HelpAge International, Issue 23, 2005a

[4] **Hampson,** Joe, "Threats To Health And Well Being In Africa", Islamset http://www.islamset.com/healnews/aged/Joe_hampson.html

Some respondents said that while people save up in banks through savings accounts or fixed deposits, these were more for short-term needs than very long-term requirements.

Informal Groups: Most women respondents (from low and middle income groups) and men (from low income groups) are members of informal financial groups – the "merry go-rounds" or Rotating Savings (and sometimes Credit) Associations. These bodies help them to save up some money that is eventually invested in an income-generating project or to buy small household items.

Only those people who are more informed and better off invest in shares, co-operatives and insurance policies.

Methods of Saving

All the above investments require funds big or small, short term or long term. These amounts are acquired in various ways.

Specific Schemes: With the lack of a strong savings habit and reliable financial system for the low-income people, cash savings come mostly through forced savings in government schemes, welfare schemes in cooperatives. People also join cooperatives to save up to be able to access a loan to help them buy an asset, which will then bring income in their old age.

Cash Savings: Savings in cash are mostly short term, with an aim to pay for some planned or regular consumption need, or to use as a security to take a loan. People usually tend to consume all what is earned even before the month end. If however they manage to save any small amount, it is saved up in banks and informal groups or with MFIs.

These small cash savings are not directly for long term. They are short-term savings used to buy assets that will help in the long run to earn income or to use as security to get a loan. People find contractual savings very helpful in saving up these small lump sums to use mainly for school fees or for buying household items and electronics in urban areas and working tools or cattle in rural areas. However this kind of product is not yet popular in the region and would require additional promotion. The performance of *Jijenge*, a contractual savings product of Equity Bank in Kenya, reinforces this. It contributes a very small portion to the deposits mobilised by the bank. By contrast, at BURO, Tangail in Bangladesh, the contractual savings agreement product accounts for two thirds of the net savings mobilized.

Save at Home: Due to high banking charges, limited outreach in rural areas and poor past performance of banks in East Africa, most cash savings would be found at home. This kind of saving is again often targeted but for even smaller amounts, such as, buying Christmas gifts. When the target is met, the saving cycle is repeated for another purpose.

Designing A Savings Scheme For Old Age

Awareness Generation: The basic need is to educate people on why and how to save. This should be coupled with a savings scheme, such as outlined below:

Savings Scheme: People expressed the need for an affordable savings product with no or limited withdrawal (may be lump sum every 5 or 10 years) for emergencies. Benefits like using the savings as security to access loans, special customer service, support services such as treatment, funeral support, counseling and business (investment) advisory services, and medical insurance cover will be added incentives.

Pension Cum Mortgage Scheme: The amount saved up would be invested to buy property, which would be subdivided into small plots and distributed to the savers. If the investment were in building(s), the bank would continue managing the building(s) and the savers would receive the earnings on a monthly basis. SACCOs that engage in property investments could do this.

Conclusion

Demand Side: Currently, low-income people rarely plan for old age as either because they do not feel the need to do so or because available resources are meager. When they do, they use a variety of informal, and often insecure, approaches to meet this goal by investment in kind. A key reason for savings through in-kind investment is the inflation rate of 4 to 9 % in the three East African countries and the devaluation of currencies over the past five years (CIA – The World FactBook). This has increased cost of living and has negative impact on long-term savings, especially which is felt by the poor who save small amounts. Furthermore, most banks in East Africa are over-liquid and the T-bill rates in the region are relatively low (as of May 2005 around 8%) which earns low returns on savings.

The potential market for long-term contractual savings services to provide security in old age is huge and growing over time. The two potential markets are the middle aged who would require income streams during their old age in about 20 years time; and the younger population who are entering the income earning stage and have shown a rising consciousness about the need for saving for old age.

Supply Side: Banks in East Africa are presently cash rich and hence a long term high interest savings product may not be what many financial institutions would want to promote. Nonetheless, such long term savings instruments for the low-income market may be attractive products for savings banks to offer. Alternatively, it may be more desirable, for both the banks and their customers, to offer short and medium term contractual savings products. Customers could then use the lump sums generated through these products to buy the land, housing etc. they hope will provide the security in old age.

Institutions offering this product need to be exceptionally stable, have excellent asset-liability management and require careful selling and well-calculated investment plans.