

# MicroSave India Focus Note 59

## Andhra Pradesh Crisis – Clients’ Perspective

Anjaneyulu Ballem, Trivikrama Devi and Veena Yamini A.

January 2011

### Background

India Focus Notes 55<sup>1</sup>, 56<sup>2</sup>, 57<sup>3</sup> and 58<sup>4</sup> discussed the Andhra Pradesh (AP) crisis at length – from the background and build-up to the crisis; what is likely to happen next; what microfinance institutions (MFIs) should do; and what the government should do. This Note focuses exclusively on clients’ perspectives, before and after the crisis, gathered by the *MicroSave* team at various points of time, in a wide variety of locations, across Andhra Pradesh, after the crisis broke in October 2010.

Clients’ historically admired and appreciated MFIs, because of their products and delivery systems, which offered:

1. Easy access to collateral-free loans;
2. Convenient, doorstep delivery;
3. Quick processing of loans with little documentation;
4. Lower interest rates compared to moneylenders etc.

Even for self- help group (SHG) members with loans through the bank linkage programme, MFIs were an attractive option, as they provided larger loan amounts in a short span of time. For most members, the loans they received from/through the SHGs were insufficient for their needs. In addition, in SHGs, other transaction costs were common: there is often a long waiting period until the bank linkage loans are disbursed; some bankers demand that SHG members keep at least 10% of the loan amount as fixed deposit, while others insist that SHG members buy insurance products to get the bank loan. SHGs also need to spend considerable time and incur substantial direct costs to receive the loan and make monthly repayments at the bank.

For these reasons, many people were borrowing from MFIs with relatively high interest rate, even though they could get loans at 3% through their SHGs. MFIs provided them easier access and client focussed service not otherwise available.

While many poor people did take loans from MFIs for the reasons cited above, others hesitated to take loans because of:

1. The rigidity in frequency of collections (most MFIs require weekly repayment - irrespective of the cash flows of the clients);
2. Compulsory weekly meetings (which put pressure on the clients’ time);
3. Stricter collection practices;
4. Higher interest rates etc.

Sectoral stakeholders have been advocating the need for product innovation and enhanced usage of technology to reduce the delivery costs. However, as MFIs were growing rapidly, the incentive to invest in innovations was missing. Most MFIs were happy rolling out vanilla group products with repayments at weekly frequency. All this has changed over-night after the Ordinance issued by the Government of Andhra Pradesh. The following sections of the Note capture the perspective of clients’ in AP on microfinance.

### Clients’ Perspectives Of MFIs

After the Andhra Pradesh State Government issued the MF-Ordinance<sup>5</sup> in October 2010, matters have become worse for MFIs, banks and clients themselves. The general trend has been that clients have stopped repayment of loans to MFIs – due to pressure from elected representatives and active workers of various political parties, as well as other local leaders; or because MFI staff are not coming to collect; or due to peer pressure.

There are three broad categories of client reactions to this:

#### 1. *Those who are willing to pay despite the situation*

Some clients are willing to pay, thinking that it is better to pay weekly instalments now than to have to pay larger amounts later when the issue is resolved. Clients are unable to pay because MFI field staff are unable to come for collections. In some villages, MFI loan officers have been arrested by the police, based on the complaints received from their clients. As a result of these incidents, many loan officers have stopped visiting villages. In other areas, the management of third parties has become a major challenge for MFI staff. One MFI loan officer noted, “*I know how to convince and manage our clients, but I really do not know how to manage local politicians and Panchayat Presidents and Ward Members, who are not allowing me to enter the village*”. MFI clients of Ramavaram<sup>6</sup> said that they are

<sup>1</sup> [http://microsave.org/briefing\\_notes/the-andhra-pradesh-crisis-three-dress-rehearsals-%E2%80%A6-and-then-the-full-drama](http://microsave.org/briefing_notes/the-andhra-pradesh-crisis-three-dress-rehearsals-%E2%80%A6-and-then-the-full-drama)

<sup>2</sup> [http://microsave.org/briefing\\_notes/india-focus-note-56-the-andhra-pradesh-crisis-so-what-next](http://microsave.org/briefing_notes/india-focus-note-56-the-andhra-pradesh-crisis-so-what-next)

<sup>3</sup> [http://microsave.org/briefing\\_notes/india-focus-note-57-the-andhra-pradesh-crisis-what-should-mfis-do](http://microsave.org/briefing_notes/india-focus-note-57-the-andhra-pradesh-crisis-what-should-mfis-do)

<sup>4</sup> [http://microsave.org/briefing\\_notes/india-focus-note-58-the-andhra-pradesh-crisis-what-should-the-government-do](http://microsave.org/briefing_notes/india-focus-note-58-the-andhra-pradesh-crisis-what-should-the-government-do)

<sup>5</sup> Andhra Pradesh Microfinance Institutions (regulation of money lending) Ordinance, 2010

<http://www.serp.ap.gov.in/SHG/index.jsp>

<sup>6</sup> Names of the villages and names of the respondents have been changed

willing to pay the instalment amount, but MFI staff members are not coming to their area for collection.

A prolonged period in which collections have not happened in the field meant that at least some clients have had a rethink on their continued relationship with MFIs. Even amongst clients willing to repay, the general perception has been that the MFIs might collect repayments, but not sanction any further loans. In Rudrapur, clients are willing to repay as long as the MFIs promise them to give further loans. In the Rayapruam village clients who recently completed repayment of their loans, and are waiting for new follow-on loans, are not happy with the Ordinance which stopped MFIs' disbursements. Hence, uncertainty is building up amongst clients and chances of repayments are reducing with every passing day.

## **2. Those who want a clarification from the government before making payments**

After the crisis erupted in October, many local administrators, as well as local and state politicians have been openly telling clients not to repay to MFIs. This campaign has been very effective in many areas, and created significant uncertainty (not to mention opportunism) amongst many MFI clients.

As a result, in many places, MFI clients do not want to repay their loans unless the government makes a clear, formal announcement on repayment to MFIs through prominent TV channels. Local Panchayat Presidents and Ward Members and political representatives are expecting an official letter from local Mandal Development Officer or Mandal Revenue Officer regarding repayment of MFI loans; otherwise, they do not want to allow MFI staff to enter villages/towns.

Some MFI centre leaders stated that loan officers have approached them with a copy of the Registration Certificate<sup>7</sup> given by the District Rural Development Agency (DRDA), but that they are waiting for the local government administration's guidance on this issue. MFI loan officers say that people do not attach any value to the Registration Certificate issued by DRDA, asserting that these documents have been produced by MFIs, rather than obtained officially through the DRDA.

In Gajulapalli, MFI clients say that many of the families have taken so many loans from MFIs that now it has become very difficult for them to pay all the instalments due. Some families have to make loan repayments every day of the week, other than on Sundays. These people are now expecting/hoping that the government will waive all MFI loans. In contrast, in Peddapalli village, MFI clients want the government to show them alternative sources of credit - otherwise they will have to go back to the informal moneylenders.

## **3. Those who are taking the opportunity to default on repayments.**

In some places there are dominant members, including the centre leaders, who are not allowing the members to repay,

<sup>7</sup> As per MF-Ordinance, all MFIs operating in the State of Andhra Pradesh must now be registered with specified authority to conduct business in the villages or towns in which they have been operating or propose to operate.

as they want to use this as an opportunity to default on or renegotiate their loans.

The extensive discussions of MFI interest rates and other charges (for example processing fee, insurance and business development service fee etc.) in various forums, especially in the electronic media, has increased the clients' awareness of the costs of borrowing from MFIs. This has brought a new set of problems for the repayment of existing loans to MFIs. For example, many clients have started thinking that they have overpaid on the loans that they have taken to date.

In Kothapalli village, one of the MFI clients who had recently taken loan from a prominent MFI, attended a meeting about the Ordinance, and calculated the entire amount she was supposed to pay to the MFI in addition to the principal amount. After this calculation, she concluded that the MFI was charging exorbitant interest, and spread this information in the entire village. As a result, all the members decided not to repay their loans, demanding that the MFI reduce the interest rate to Rs.1 per Rs.100 per month. The media coverage of the crisis and alleged suicides attributed to MFIs has also affected clients' belief in MFIs. In Mamillapalli village, for instance, some clients are under the impression that MFIs caused clients elsewhere in the state to commit suicide. Hence, although none of the clients the team met actually knew of anyone who had committed suicide, they have decided to stop taking loans from MFIs, mainly on the basis of media reports and what they have heard from other villagers.

## **Non-clients' Perspectives of MFIs**

Non-clients' perspectives on, and prejudices about, MFIs have been strengthened. Many of the non-clients do not know how MFIs operate, as MFI staff do not share their norms and terms of business with anyone other than their clients. Many of them believe that MFIs are charging higher interest rates than local moneylenders. The present crisis, publicised through media, has made the MFIs infamous - even amongst those who have never before heard of microfinance. Many such non-clients believe that poor people across the state have committed suicide because of pressure from MFIs and the use of coercive practices for repayments.

## **Conclusion**

The main impact of the crisis has been on the credit discipline demonstrated by the clients. The credit discipline, so carefully nurtured by MFIs has been almost completely eroded. Yashoda of Jagatpur says, "*Only a few weeks back, we used to worry about instalment amount that needs to be paid on time to MFIs. We could not even sleep properly until we mobilised the necessary amount. But now we know how to manage the loan officer of MFI in case we do not have money for payment of the instalment*". The implications for the credit risk associated with lending to the poor in India, whether through joint liability groups, or through SHGs, are enormous and profoundly worrying.