

# *MicroSave*

*Market-led solutions for financial services*

Offices across Asia, Africa  
and Latin America

[www.MicroSave.net](http://www.MicroSave.net)  
[info@MicroSave.net](mailto:info@MicroSave.net)

---

## **Innovative Approaches to Delivering Microfinance Services: The Managed ASCA Model in Kenya**

**Nthenya Mule, Susan Johnson, Robert Hickson & Wambui Mwangi**

**November 2001**

**Submitted by:**

***K-Rep Advisory Services Limited***

**Wood Avenue off Argwings Kodhek Road**

**P.O. Box 10543**

**Nairobi**

**Tel: 572387 Fax: 564053**

## **Table of Contents**

<b>EXECUTIVE SUMMARY .....</b>	<b>3</b>
<b>ACKNOWLEDGEMENT .....</b>	<b>5</b>
<b>LIST OF ACRONYMS.....</b>	<b>5</b>
<b>1 INTRODUCTION.....</b>	<b>1</b>
1.1 The Context .....	1
1.2 The Local Financial Landscape.....	2
<b>2 ASCA MANAGEMENT AGENCIES: THE MODEL.....</b>	<b>2</b>
2.1 Products and Services.....	2
2.2 The Role of the ASCA Management Agency .....	5
2.3 Organisational Structure: Ownership, Governance and Management.....	6
2.4 Administrative and Operating Systems .....	7
2.5 Financial Management .....	8
<b>3 ANALYSING PERFORMANCE.....</b>	<b>8</b>
3.1 Outreach: Breadth and Depth .....	8
3.2 Financial Performance at the Group Level.....	9
3.3 Financial Performance of the AMAs Themselves.....	11
<b>4 EXPLAINING PERFORMANCE .....</b>	<b>12</b>
4.1 Members Preferences for Managed ASCAs.....	12
i) Loan flexibility .....	12
ii) Monthly repayment.....	12
iii) Repayment can be re-negotiated.....	12
iv) Access.....	13
v) Benefits of ownership.....	13
vi) Support in times of need.....	13
vii) Key member concerns about the model.....	14
4.2 Achievements of, and challenges facing the model.....	14
i) Default Management .....	15
ii) Constraints to the growth of existing AMAs.....	17
iii) Further development of products and services .....	17
<b>5 CONCLUSIONS.....</b>	<b>17</b>
5.1 Strengths and Weakness of the AMA Model .....	17
5.2 Lessons for Mainstream MFIs.....	18

i)	Reducing Operating Expenses.....	18
ii)	Improving Outreach.....	19
5.3	Recommendations for Donors.....	19
<b>6</b>	<b>BIBLIOGRAPHY.....</b>	<b>20</b>
	<b>ANNEX 1: RESEARCH METHODS.....</b>	<b>21</b>

## EXECUTIVE SUMMARY

### Background

In the Central Province of Kenya, based in the small town of Karatina in Nyeri District, there exist a number of local organisations that have developed a microfinance model in which they provide management services to group-based loan funds. These organisations operate profitably, without donor funding, and are expanding rapidly - serving approximately 29,000 clients in mid-2001. They are operating in exactly the same market as the main Kenyan MFIs whose country-wide coverage is estimated to be 135,000, but for whom high operating costs, slow intake and high client exits have constrained their efforts to achieve financial and organisational sustainability.

### The Study

This study set out to study the organisations operating the model in greater depth. The groups operate as Accumulating Savings and Credit Associations (ASCAs) and we have therefore coined the term ASCA Management Agencies (AMAs) to describe the organisations providing these management services to the groups. The study set out to examine the operations of the AMAs and the groups they work with. This was done through a series of interviews with group members, group officials, staff and management of the AMAs themselves, along with data collection based on available records. Three organisations participated in the study: Partnership for Productivity (PFP), the Women's Enterprise Development Institute (WEDI) and the Small Enterprise Development Institute (SEDI).

### The ASCA Management Model

The AMA assists women to form a group and, from the first meeting, members make a minimum monthly contribution of KShs100, which are called shares. From the first meeting savings are converted into loans to members of the group. As the fund grows, two types of loan are offered: short term loans called advances on which interest is paid at 10% per month, and longer term loans up to two years with interest payable at 17% flat. At the end of the year, dividends are calculated and profits distributed in relation to members shares. The dividend rate depends on the performance of the group with indicative rates varying between 16% and 60% where dividends were actually paid.

The role of the AMA is the mobilisation of the groups, and a field officer attends the monthly meeting. She may also assist the group to develop its constitution and by-laws and register with the Ministry of Culture and Social Services. Field officers keep accounts of group transactions, of which the group secretary also keeps a copy. The group pays the AMA a service fee of 1% of the value of the fund up to a maximum of KShs2,500 per month. In addition the AMA has a key role in default management. The AMA is responsible for identifying and following up defaulters, an aspect of the service which members appreciate as it avoids the social friction that may be caused by following up on defaulters themselves.

Apart from PFP, which is registered as an NGO, the other AMAs are run as sole proprietorships with owner-managers. The Programme Managers in WEDI and SEDI own the institutions and oversee their running. They drive the programmes single-handedly, recruiting and supervising all staff, networking with existing groups to draw in new clients and making all strategic decisions. The AMAs performance in terms of outreach and income is therefore determined to a large extent by the foresight, ingenuity and hard work of the Programme Managers.

### Performance of the model

Breadth of outreach: The estimated outreach of these three AMA was 29,000 in mid-2001, up from approximately 17,000 at the end of 1999. The geographic coverage of these groups has spread out from the base in Karatina to cover Kirinyaga District to Laikipia District and encompassing Nyahururu, Nanyuki and Nyeri. During the last 18 months fierce competition for clients has forced AMAs to extend their reach to less populous areas away from Karatina and Nyeri. As a general rule AMAs have extended

further into remote rural areas in this region than the MFIs. It is also calculated that in 1999 MFIs operating in the region around Karatina had approximately 2000 members while the AMAs had approximately 10,000. However, the figures for AMA membership should be treated with caution as it is not always possible to establish the status of members, some of whom may be in long term default but because of the nature of the model still appear in the records.

**Depth of outreach:** While the research did not undertake a survey to establish specific socio-economic characteristics of members, the qualitative evidence suggests that the model has greater depth of outreach than the standard MFI model. Groups were numerous in rural locations, and could also be formed among professionals such as teachers, nurses and civil servants. The design of the model appears to offer greater flexibility for poorer clients due to the fact that it is not required that a member have a loan; loans can be as small as needed and for periods as short as a month. These features as well as the monthly meetings make the approach popular.

**Financial performance of groups:** The total value of funds held in the groups is estimated to have been KShs155m (US\$2m) at the end of 1999 and Kshs215m (US\$2.75m) by mid-2001. This gives an average savings per member of KShs4,524 (US\$58). However, group records do not easily allow the status of the group's loan portfolio to be established, and hence clear statements about the effectiveness of the approach in managing default are difficult to make.

**Financial performance of AMAs:** The AMAs use the service fees to cover their costs and are proving profitable. The cost structure of the AMAs is kept very low with a minimum of fixed assets. Salaries are low, offices are rented, and book-keeping systems are mostly manual – only one AMA has a computer. One of the AMAs does not even have electricity, choosing instead to operate during daylight.

### **Explaining performance**

Members explain the **advantages** of the AMA groups as follows: access to loans is more or less assured; loans are flexible in terms of size and duration; saving and repayment is monthly; there is the potential to renegotiate repayment should problems arise; the group is a means to extend social networks which can offer social support in the event of crises and lifecycle events; interest stays within the group and the dividend can be high.

The key **concern** that members express is over the service offered by the AMA in return for the management fee, especially in relation to debt collection. In this case when the AMA has to visit members to reclaim funds, it will charge the member the costs, which may be up to KShs500. This may absorb any money the member has available for repayment and the group has not regained any of its funds. Members and groups feel aggrieved by this process.

This is one of the key **challenges** facing the model. The delegation of the debt collection role to the AMA produces an incentive problem. The AMAs earn a fixed fee from the group and therefore in order to maximise their own returns wish to minimise the time and effort they spend following up defaulters. Moreover, the fact that they can charge pass for follow could be seen as an added incentive not to deal with them effectively.

A further problem is that, once the default problem has become significant in a group, the exact means through which it can be liquidated are unclear. This is, in part, caused by the lack of a clear and documented service agreement between the AMAs and the group which defines service and exit options. It is, in part, the problems in default that have led to rapid growth: since declining repayment tends to result in falling income for the AMA and the incentive to recruit new groups.

A further complication in this situation is that because the group owns the funds, attempts by the AMA to pursue default more severely, may be resisted by groups. Groups have the ability – and the right – to determine the default management regime and some groups will wish to be stricter than others.

The resolution of this problem could involve a stronger and more clearly defined set of responsibilities for the group in terms of default management, since it is the group members that own the funds. Second, and in consequence of the first point, service agreements between groups and the AMAs which address more explicitly the roles of the different parties in relation to default management could be introduced. Third, means through which to better link fees to the success of the AMA in recovery could be explored. Fourth, service agreements could better clarify the options of the members and the groups to exit the service. Finally, strategies could be developed with the AMAs to address the revitalisation groups that have significant default problems.

## Conclusions

The key **strengths** of this model are the entrepreneurial spirit of the providers and their need to respond to client demand rather than donor satisfaction; that the model builds on the popularity of informal group mechanisms such as ROSCAs and ASCAs; that its low entry and operating costs allow for easy replicability. The model also offers a middle road between MFI provision and self-help group approaches that tend to assume the capacity for user-management.

However, the **weaknesses** include poor portfolio management, weak institutional management, dependence on a single director, and the incentive problem in default management.

The lessons for mainstream MFIs are that operations can be carried out on a low cost basis and that adaptation of products may allow for greater outreach in terms of both breadth and depth of coverage.

Recommendations for donors: This model has arisen out of the withdrawal of donor support to a local NGO that then developed this model in order to survive. This suggests that withdrawal can spur innovation. However donor intervention in the model is likely to undermine its positive attributes, especially, for example, if a fund was created for AMAs to on-lend to groups. On the other hand, it appears that the incentive problems involved in the design require revisiting in order that they can be better aligned. In addition, these organisations would benefit from the improvement of their management and administration systems if appropriate technical assistance can be provided.

## Acknowledgement

The authors are especially grateful to Mr Mugo of WEDI, Mr John Okumu of PFP and Mr Waigwa of SEDI for their co-operation in allowing us to conduct the study and their assistance in its completion. We are also grateful to *MicroSave* for funding it.

## List of Acronyms

AMA	ASCA Management Agency
ASCA	Accumulating Savings and Credit Association
CEO	Chief Executive Officer
MFI	Microfinance Institution
PFP	Partnership for Productivity
ROSCA	Rotating Savings and Credit Association
SEDI	Small Enterprise Development Institute
WEDI	Women's Enterprise Development Institute

<i>Ngumbaco</i>	Advances – short term loans of one month
<i>Giteti</i>	A ROSCA or ASCA

# **Innovative Approaches to Delivering Microfinance Services: The Managed ASCA Model in Kenya**

Nthenya Mule, Susan Johnson, Robert Hickson & Wambui Mwangi

## **1 Introduction**

During the 1990s, microfinance organisations using the group-based lending model and with donor support have reached approximately 135,000. However, high operating costs, slow intake and high client exits have constrained their efforts to achieve financial and organisational sustainability. By contrast, in Central Province, there exist a number of local institutions using a microfinance model that, in the same environment and without donor funding, are operating profitably and expanding rapidly. The model these organisations operate is one in which they provide management services to group-based loan funds. The groups operate as Accumulating Savings and Credit Associations (ASCAs) and we have therefore coined the term ASCA Management Agencies (AMAs) to describe the organisations providing these management services to the groups.

The managed ASCA model was originally conceived by Partnership for Productivity (PFP) based in Karatina. This is a local NGO that had started out in Western Province in 1968 and provided a range of donor funded developmental interventions with women's groups, including lending to individuals and groups. It started working in Nyeri in 1988, having moved there because it was seen as being an economically vibrant region inhabited mostly by Kikuyu who are known for their business acumen. In 1994 donors withdrew funding and, lacking funds, PFP decided to work with the groups that had their own funds in a revolving loan fund or ASCA. They assisted the group in the management of the fund run to a specific format for which they charged a fee. This model was not successful in Western Kenya and that part of PFP's operations closed down. Then in 1995 the training officer of PFP, who had played a key role in developing the model, decided to start his own company - the Women's Enterprise Development Institute (WEDI) - opening an office immediately next door to PFP and taking with him some of the groups from PFP. This organisation then recruited a large number of groups. In January 1999 one of the WEDI staff then also broke away and started another organisation called Small Enterprise Development Institute (SEDI) and, as with the earlier split from PFP, took some groups with him from WEDI. This process has continued to this day and now some eight such entities operate the Managed ASCA model in the region with estimated outreach to over 25,000 clients. These comprise PFP, WEDI and SEDI based in Karatina, which are the focus of this study. A further three organisations have been formed in Karatina during 2001. Another organisation called Kenya Entrepreneurship Promotion Programme (KEPP) is based in Thika.

This objective of this report is to describe the operation of the model and to examine its performance. The last section examines its strengths and weaknesses and suggests lessons that other MFIs and donors can learn from this experience.

### **1.1 The Context**

The late 1990s have been a period of macro-economic decline in Kenya with official figures (Central Bureau of Statistics and Ministry of Finance and Planning 2001) indicating that year on year growth has declined steadily from 4.6% in 1996 and turning into negative growth of 0.3% in 2000. Agricultural growth in 2000 has declined more rapidly to negative 2.4%. Official figures also suggest a doubling of inflation between 1999 and 2000 from 3.5% to 6.2%.

Central Province, in particular Nyeri, Kirinyaga and Muranga Districts are heavily dominated by tea and coffee farming and these areas also have vibrant enterprise areas in both district centres and small towns. The recent substantial decline in coffee prices on the world market has had a dramatic effect on local incomes in these areas since the high levels of 1997. This situation, along with the 'splitting' of coffee co-operative societies from their secondary societies into autonomous primary societies has contributed to instability and violence in the coffee sector. By contrast tea prices have been more stable.

The Government's Kenya Poverty Assessment (1998) using 1994 data suggests that Nyeri District - the second richest in the country - does not experience absolute poverty<sup>1</sup> in a year when the rains are good. Other districts of Central Province may not quite achieve this level but are not far behind. Beyond the high-potential agricultural areas on the slopes of Mt Kenya, livelihoods are based on irrigated horticulture activities, and in the Nyahururu and Nanyuki areas livestock farming and the production of wheat on more extensively operated farms with the far north and east of the region giving way to ranching and some European farms. The year 2000 was characterised by a severe drought. As a consequence electricity rationing resulted in manufacturing and industrial sectors working below capacity levels, leading to reduced production. The retail sector, which relies on significant inputs from the manufacturing and industrial sectors, was also adversely affected.

## 1.2 The Local Financial Landscape

The financial sector based in Karatina<sup>2</sup> but extending to Nyeri and other districts in Central Province comprises a huge range of financial institutions. Starting with the formal sector, all five of the main nationally present banks have branches in Nyeri District: Barclays, Standard Chartered, Kenya Commercial Bank, National Bank of Kenya and the Co-operative Bank. Building societies and Non-Bank Financial Intermediaries (NBFIs) such as Equity Building Society, Consolidated Finance and the Housing Finance Corporation of Kenya (HFCK) are also present. The Savings and Credit Co-operative (SACCO) sector is quite diverse. There are 'rural' SACCOs such as Nyeri Farmers SACCO Society, Nyeri Tea Growers SACCO and Mathira Tea Growers SACCO. There are also employee based SACCOs such as Nyeri District Teachers SACCO and SACCOs associated with smaller local employers such as hospitals (eg Uringiti at Tumutumu Hospital) and local councils. In addition in the *matatu* sector over the 1990s, SACCOs have arisen based in the transport associations that run specific routes.

Further financial intermediaries in the formal sector are parastatal organisations such as the Agriculture Finance Corporation, Kenya Industrial Estates (which gives individual loans to enterprises) and the Kenya Post Office Savings Bank. Organisations which have been donor funded and offer group-based lending programmes are Kenya Women Finance Trust (KWFT), K-Rep, FAULU and the Small and Micro Enterprise Programme (SMEP).

This diversity of formal financial intermediaries is complemented by a vibrant array of informal financial mechanisms. Rotating Savings and Credit Associations (ROSCAs - known locally as *iteti*) are very popular and operate in both rural and urban areas with a number of modes of operation. In urban areas where transactions are daily some of these do not meet but a collector appointed by the group runs their activities. Some of these groups have developed into ASCAs that operate their own loan fund. Finally, there are a small number of moneylenders although they tend to maintain a low profile.

## 2 ASCA Management Agencies: The Model

In this model, there are two organisations: the AMA and the group. Groups may already be in existence or may be formed by the AMA, but as a group with a constitution of its own it registers with the Ministry of Culture and Social Services. The AMA then provides services to the group to enable it to manage its activities.

### 2.1 Products and Services

The AMAs offer a template for the operation of the ASCAs that is almost uniform. Small differences have arisen as the organisations have formed and this has in part been a response to client feedback. The products are described below and summarised in Table 1.

Members form a group and from the first meeting members make a minimum monthly saving of KSh 100, which are also called shares. Members may save as much as they wish. From the first meeting

<sup>1</sup> Absolute poverty is defined here as below an overall poverty line which captures the basic minimum food and non-food consumption requirement. (Government of Kenya 1998).

<sup>2</sup> See Johnson 2001

savings made are converted into small loans to members of the group, at ten per cent per month. This continues until the fund grows sufficiently to offer the two main credit products. One is a short-term advance (known locally as *ngumbaco*), which is usually for a month and on which a flat 10% interest is paid (annual effective rate 120%). An access fee of between KSh 10-20 (US\$0.13-0.26) is paid in order to get the *ngumbaco*. *Ngumbaco* may be renewed for up to three months, if the interest is paid monthly. Members are entitled to advances of between two and three times their savings. The other credit product is a longer-term loan for up to three times shares for between ten and 24 months at 17% flat, repaid in equal monthly instalments. A one per cent application fee is levied on these longer-term loans and the application form requires other family members to act as guarantors or household assets to be pledged. A grace period of one to three months is permitted on the loan.

The organisations only really differ in the details of their products. For example, SEDI claims to calculate the interest on a declining balance basis for these longer-term loans. The interest paid by members on loans is paid into the Revolving Loan Fund and, therefore, belongs to the members. At the end of the year the dividend is calculated. This is based on the interest accumulated in the fund. The high rates of interest on loans means that the interest paid into the fund is substantial and hence yields very high dividends. Dividends are calculated by the AMAs on behalf of the groups, and an allowance of 30% of the value of the fund is made for loan loss provision before the remaining profit is distributed as shares. In some of the organisations, the dividend also comprises 10% of the amount that a member has paid in interest on advances. This adjustment was made as a result of feedback from members: those who take advances (*ngumbacho*) realised that they were paying much more interest than those taking longer term loans and thought that they should therefore benefit more when the dividend was paid. Also in December there is a bonus or “celebration” which is a flat payout of around KSh 500 (about US\$6.40). This is deducted and provided to the group as cash before the members’ dividends calculated. Individual dividends are either paid as additional shares or used to offset outstanding loans.

In addition the group may decide to save for a specific project of their own. This may involve a monthly contribution that is used at the end of the year to buy all members a specific household or other item such as cooking pots, plates, mattresses or jumpers. This project is also completed in December.

Savings withdrawals can be made down to KSh 1,000 (about US\$12.80) if the member has no loans outstanding. Otherwise, she can only withdraw down to the value of the shares required to guarantee her short-term advance (one third the value of the advance). She cannot withdraw at all if she has a long-term loan.

PFM has introduced an Education Booster Fund, which has also been adopted by SEDI. This allows members to save so that they can meet the education expense requirements for their children at the beginning of the year. Members save any amount they wish each month over and above the minimum KSh 100 per month. The savings receive 10% per month interest, but withdrawals can only be made in December.

A member can leave the group by giving notice. She can then withdraw her shares, net of any outstanding loans, and she may receive a proportion of the accumulated profit in the fund. This calculation can slightly differ between the AMAs, but more importantly if there is a significant degree of default in the group, the AMA will not usually allow the ‘profit’ element to be withdrawn by the member. If default in the group is very serious then even withdrawal of shares may be difficult.

**Table 1 Services Comparison Matrix**

	<b>PFM</b>	<b>WEDI</b>	<b>SEDI</b>
<b>Group Formation</b>			
Registration Fees (paid to group and retained by the group)	KSh 150 per member, for new groups; non-refundable	KSh 150 per member, for new groups; non-refundable	KSh 150 per member, for new groups; non-refundable
Passbooks	KSh 50	KSh 30	KSh 50

	<b>PFP</b>	<b>WEDI</b>	<b>SEDI</b>
Registration with MCSS <sup>3</sup>	KSh 1,000	KSh 1,000	KSh 1,000
Minimum Share Contribution per month	KSh 100	KSh 100	KSh 100
Share Withdrawal	Can withdraw shares up to a minimum of KSh 1,000	Can withdraw shares up to a minimum of KSh 1,000	Can withdraw shares up to a minimum of KSh 1,000
Late Joiners Registration Fees	Average shareholding	Average shareholding	Average shareholding
<b>Advances (Ngumbaco)</b>			
Maximum Advance Amount	Three times shares	Three times shares	Two times shares
Interest Rate	10% per month	10% per month	10% per month
Loan Access Fee <sup>4</sup>	KSh. 10	KSh. 10	KSh. 10
Loan Term	1 month	1 month	1 month
Late Payment Penalty	10% of total outstanding amount	10% of total outstanding amount	10% of total outstanding amount
Rollover Conditions	2 cycles of interest only payments. If full outstanding balance not paid by 3 <sup>rd</sup> cycle, seek intervention of lawyer	2 cycles of interest payment only. If full outstanding balance not paid by 3 <sup>rd</sup> cycle, seek intervention of lawyer	2 cycles of interest payment only. If full outstanding balance not paid by 3 <sup>rd</sup> cycle, seek intervention of lawyer.
<b>Long Term Loans</b>			
Maximum Loan Amount	3 times shares	3 times shares	3 times shares
Loan term	15-24 months KSh 5,000 – 15 months KSh 10,000 – 20 months KSh 15,000-20,000 – 24 months	5-24 months KSh 5,000 – 5-15 months KSh 10,000 – 10-20 months KSh. 15,000 – 10-24 months KSh. 20,000 – 10-24 months	15-24 months KSh 5,000 – 15 months KSh 10,000 – 20 months KSh 15,000-20,000 – 24 months
Interest Rate	17% p.a. flat	Flexible: 10% p.a. flat for shortest repayment periods on each loan step; 17% p.a. flat on the longest repayment period on the loan step	17% p.a. reducing balance
Loan Application Fee	1% loan amount	1% loan amount	1% loan amount
Late Payment Penalty	Deduct total outstanding instalment from shares	Confiscate and sell off pledged assets	10% of outstanding instalment amount – deducted from shares
<b>Shares</b>			
Monthly Contribution	Minimum contribution KSh 100	Minimum contribution KSh 100	Minimum contribution KSh 100

<sup>3</sup> Ministry of Culture and Social Services

<sup>4</sup> This fee is a condition that has been introduced by the groups and not the AMAs. The members view this as a way of the individual showing appreciation for the services s/he can access from the fund. This fee goes back into the capital fund.

	<b>PFP</b>	<b>WEDI</b>	<b>SEDI</b>
Dividend Earnings	Payable annually and calculated as follows: Total Revolving Loan Fund (TRLF) = advances + long term loans + cash in bank Annual Profit (AP) = TRLF – shares – 30% of TRLF as a loan loss provision Group Dividend % = Annual Profit/average value of shares over the year x 100% Dividend paid to each member = Group Dividend % x individual member’s average shares over the year The dividend is credited to members share accounts or used to reduce outstanding loan balances. ‘Bonus’ = KSh 500 paid in cash to members - also paid in December.		
<i>Voluntary Savings</i> <sup>5</sup>	Can contribute to the Education Booster Fund, specifically to pay for education expenses Can contribute to the Project Fund. These monies are used for RoSCA activities or to buy specific items for the whole group and are accounted for as a “member’s” account.	Can contribute to the Project Fund. These monies are used for RoSCA activities or to buy specific items for the whole group and are accounted for as a “member’s” account.	Can contribute to the Education Booster Fund, specifically to pay for education expenses Can contribute to the Project Fund. These monies are used for RoSCA activities or to buy specific items for the whole groups and are accounted for as a “member’s” account.

## 2.2 The Role of the ASCA Management Agency

The AMAs mobilise women to form ASCA groups. While in the past, they also recruited men’s groups, their experience with them has been very poor and there are now only a very few in the programme. They visit new areas and inform women of the model and benefits of forming such organisations. They work either with existing groups<sup>6</sup>, or facilitate the formation of new groups, which have on average 30 members. When groups do not reach these levels, groups from neighbouring areas may form a group under the auspices of the AMA. In towns, individuals may sign up at their offices and once sufficient women have indicated interest the AMA will call them to form a group<sup>7</sup>. When a group forms, members pay a KSh 150 registration fee to the group fund.

The AMA field officers are responsible for meeting the group on a monthly basis and co-chairing the meeting to ensure that the proceedings are carried out according to the model. She will also assist the group to develop its constitution and by-laws that are necessary for its registration with the Ministry of Culture and Social Services (MCSS). Field officers keep the group’s financial records, which are disaggregated by member in the group’s register<sup>8</sup>, tracking the size of the total revolving loan fund, tracking defaulting members so that the AMA can take action to follow up on these defaulting members. The group also keeps a record of these transactions alongside the minutes of the meeting that are kept by the group secretary. Each individual’s transaction is also entered in her own passbook.

<sup>5</sup> “Project” is an activity determined by members, usually a merry go round. Until members have saved enough for the Project’s activities, the money saved through this account is loaned out and bears interest.

<sup>6</sup> Sometimes field officers will breakaway and form their own AMA, in which case they usually take with them the groups with which they were working. In other cases, but less often, there are groups that are already formed that will approach the AMAs for management services.

<sup>7</sup> Clearly the screening function, which self-selection of members is supposed to perform is missing here, it has not been possible to assess the relative success of groups formed in this way and groups which were self-selected.

<sup>8</sup> Although the individual member’s name is recorded in the group register, the practice is to assign each member a number, and this number is used in reference to that member’s affairs.

At each meeting the group pays the AMA a fee for the services it provides. This fee is set at one per cent of the value of the group's total revolving loan fund. However, there is an initial three-month trial period during which the service is given free. This allows the group to build up its loan fund. As the group's total revolving loan fund grows so the fee they pay is increased up to a ceiling. This ceiling varies between KSh 2,500 and KSh 3,000 (USD 31 to 38) depending on the AMA. However, the fee is not necessarily calculated at exactly one per cent at each meeting. Rather, as the fund grows it will go up in steps in amounts that are convenient and easy to collect.

Apart from the facilitation of the meeting, arbitration of disputes and the keeping of group records, the AMA has a key role in default management. Indeed this is a key service that the group sees itself as purchasing from the AMA. When a member is in default, the onus is on the AMA to follow up and ensure that the outstanding monies are recovered. If a member has not made a short-term advance repayment, she is charged an additional 10% on the total outstanding amount of both principal and interest. This penalty is charged to those clients who do not show up at the group meeting to present their case and possibly negotiate a change in terms. Following this she is either required to pay the full outstanding amount, or she can convert the outstanding short-term advance arrears into a long-term loan. This latter option is with the group's consent, and the member must cite a "very good" reason, why she cannot meet the obligation of clearing the outstanding balance: for example an illness requiring hospitalisation, or an unforeseen calamity such as fire, theft of business stock, or a poor harvest. The role of the group and the AMA in following default is not always very clear. Since many members see this as a service they are purchasing from the AMA, they believe that the AMA should be responsible for follow up. However, in some groups, members will get involved in visiting the member, in others they will only go so far as to direct the AMA staff to the member's house. On the first occasion that a member misses a payment on a loan, the AMA staff and /or group's officials, go to visit the delinquent member to establish the reason behind non-payment. If the reason is regarded as 'valid', then new terms of repayment can be negotiated with the member.

A member who is not able to raise the full outstanding balance on a short-term advance may opt to make an interest payment only. This provision for making just the interest payment is permitted up to three successive times. After that, the member is obliged to make the full outstanding payment of principal and interest. A member who has made an interest only payment cannot access any additional short-term advance funds. The group regards her as someone who has "...lent herself money" and because she has not returned what is due to the fund, her privileges, in terms of access to credit, are therefore restricted.

If it is a long-term loan, which has fallen into arrears, there is a slight variation in the follow up procedure. The AMA does not impose a penalty on the outstanding balance, as is the case with short-term advances. Instead, the AMA makes deductions against the member's shares for the instalment payment that is due but has not been paid. The member is then followed up in home visits, sometimes with the intervention of group officials.

If these visits do not bring enough pressure to bear on the defaulting member, then the AMA issues a letter, summoning her to the office. If the member remains unresponsive at this point, the group is apprised of the situation by the field officer. At this stage the Programme Manager may then begin making home visits to the member, either at her place of business or her residence. If these measures still prove ineffective, then the AMA may utilise a lawyer. First the lawyer will write a letter demanding payment and threatening legal proceedings against the defaulting member. All the costs incurred by the AMA in pursuit of monies in arrears are borne by the defaulting member. Eventually court proceedings against the member may be undertaken, and although this is rare, SEDI had recently pursued one defaulter to court; which according to the manager, had dramatically improved repayment performance in other groups. An alternative approach may be the use of the local administration, and administration police.

### **2.3 Organisational Structure: Ownership, Governance and Management**

Apart from PFP (and KEPP in Thika), which as indicated above is constituted as an NGO, the other AMAs are run as sole proprietorships with owner-managers but WEDI has also been seeking NGO

registration. The Programme Managers in WEDI and SEDI own the institutions and oversee their running. They drive the programmes single-handedly, recruiting and supervising all staff, networking with existing groups to draw in new clients and making all strategic decisions. The AMAs performance in terms of outreach and income is therefore determined to a large extent by the foresight, ingenuity and hard work of the Programme Managers. By contrast the local manager of the PFP programme is accountable to senior staff of PFP based in Nairobi, to whom he is required to report monthly.

The three AMAs have a fairly flat management structure: a programme manager to whom all field officers report. The CEOs in WEDI and SEDI are also the Programme Managers. The Programme Manager is therefore responsible for all decision making, both strategic and operational, and overseeing the day-to-day management of all field activities. In all three organisations, the Programme Managers also act as field officers, perhaps filling in for absent staff and attending to groups and helping them keep their records, and in particular visiting groups where problems arise. The Programme Managers also perform a key role in default management. They follow up on difficult clients and are the ones who will decide the course of action to be taken on defaulters.

The field staff have the primary responsibility of attending to groups and helping members keep their records. In PFP and WEDI, the field staff who have been there the longest are also given the responsibility for recruiting new groups. While the field staff in SEDI are now beginning to take on the responsibility of client recruitment, they rarely carry out this function alone; the Programme Manager will usually accompany field staff on recruitment campaigns.

The flat organisational structure and owner-managed structure of WEDI and SEDI allows them to respond quickly to situations on the ground. If there is potential to begin operations in a new area, they can immediately move to open an office provided they have the funds to do so. For example, both WEDI and SEDI have opened offices in Nyahururu in 2001 because they see it as an area with good potential. PFP however does not have the same kind of flexibility. Any changes that the Programme Manager might want to introduce in the programme have to be cleared with head office and any funds needed for investment will have to be agreed.

The model operates with absolutely minimal fixed costs. Offices are rented, (one does not even use electricity); all officers use public transport and the salary structure is kept low. Staff are usually Form Four leavers or have a diploma in accounting or business. Salaries are in the range KSh 4,000 to 7,000 per month. It is this that makes barriers to entry very low: the need is to know how to run the model, be effective in dealing with people and be able to develop a degree of trust with the members.

## **2.4 Administrative and Operating Systems**

The AMAs are responsible for ensuring that all their clients receive bookkeeping services on a monthly basis. At the beginning of each month the Programme Manager checks and verifies a monthly work programme that schedules the dates when each group will be visited and by whom. All group records are held in files kept in the AMA offices. Those AMAs that have branches in Nyahururu (WEDI and SEDI) have their respective branch offices keeping files for the groups in the areas served by those branch offices. SEDI indicated that their branch office is required to forward files every month and these are audited by the head office.

All the institutions use a manual operating system with all data on a particular group captured in the group's file. Every month, the field officer attending the group is required to fill out details of the group's performance in the Monthly Performance Form. This form captures each ASCA member's account in terms of shares, loans disbursed, loans repaid, outstanding balances, the size of the Total Revolving Loan Fund (TRLF) and the service fee paid to the institution. In addition, the field officers also make notes of difficulties that may have arisen with particular clients. If the AMA issues any letters on default follow-up, these are filed with the group's records. However, there is no systematic way of identifying a problem ASCA other than the memory recall of the Programme Manager and the field officers.

When ASCA members are unable to make it to the meeting for whatever reason, some groups allow the member to drop off her share contribution and any loan repayment to the AMA's offices. The AMA's staff receiving the money is supposed to enter the information on the monies received in the group's register, and at the next meeting, the field officer takes the money to the group. Some groups prohibit their members from making late payments at the AMA's offices and would prefer the member to either seek out the group's treasurer, or keep the money and bring it to the next meeting.

## 2.5 Financial Management

The AMAs are responsible for ensuring that the financial records of the ASCAs are up to date and any problems arising are dealt with accordingly. The ASCAs also keep identical records on the group's performance, but in most instances, these records are simply a copied from what the AMA's field officer has noted down in her files. At first they operated with specially printed forms kept in loose leaf files; one of the organisations has now moved onto a specially printed ledger book.

The field staff are responsible for noting progress on payment of outstanding loans, whether short or long term. Short-term advances are itemised on the back of the Monthly Group Performance form, while share contributions and long term loans and their corresponding repayments are noted on the front side of the Monthly Group Performance form. Each group is treated as a discreet unit, and there is no consolidation of all outstanding loans, service fees charged or loans that are in default. The AMAs therefore do not have a clear idea of how the entire portfolio of all the ASCAs they deal with is performing. Other than the notes made on the Monthly Group Performance form, there is no other mechanism of tracking how loans are performing.

PFK-Karatina is required to account for its income and expenditure by its head office monthly. WEDI has financial records and audited accounts, which also capture the organisations financial performance in terms of revenue and costs, however SEDI does not yet keep adequate financial records.

## 3 Analysing Performance

### 3.1 Outreach: Breadth and Depth

PFK started operating with this model in 1994 with some 130 groups from its previous programmes. When the training manager decided to start WEDI in 1995, he took approximately 80 of these groups with him. By mid-2001 the total membership of PFK, WEDI and SEDI was about 29,000 (see Table 2).

**Table 2 Numbers of groups and approximate numbers of members by organisation**

AMA	Dec-99		Jul-01		Annual Growth Rate
	Groups	Members	Groups	Members	
<b>PFK</b>	174	5,742	255	8,415	31%
<b>WEDI</b>	300	9,900	430	14,190	29%
<b>SEDI</b>	52	1,716	200	6,600	190%
<b>Total</b>	<b>526</b>	<b>17,358</b>	<b>885</b>	<b>29,205</b>	<b>46%</b>

In 1999, it was calculated<sup>9</sup> that the MFIs in and around Karatina had approximately 2,000 members, while the AMAs operating in a similar area had approximately 10,000 members. By 2001 the AMAs outreach had grown to 855 groups representing a total membership of approximately 29,000 and growth in this 18-month period of about 46% per year. Average group size has remained at about 33.

There has been considerable growth in membership over the past one and half years and the geographic coverage of these groups has spread out from the base in Karatina to cover Kirinyaga District to Laikipia

<sup>9</sup> See Johnson, S 2000.

District and encompassing Nyahururu, Nanyuki and Nyeri. During the last 18 months fierce competition for clients has forced AMAs to extend their reach to less populous areas away from Karatina and Nyeri. As a general rule AMAs have extended further into remote rural areas in this region than the MFIs.

In comparison MFI growth in the same region has been averaging about 27% per year (see Table 3).

**Table 3 Membership and Growth of K-Rep FAULU and KWFT**

<b>MFI Regional Branches</b>	<b>1999</b>	<b>2000</b>	<b>Annual Growth</b>	<b>2001</b>	<b>Annual Growth</b>	<b>Annual Growth 1999-2001</b>
<b>K-Rep (Mt Kenya West)</b>	2,384	2,007	-16%	2,769	38%	8%
<b>FAULU Nyeri (Mt Kenya West)</b>	1,574	1,753	11%	2,277	30%	22%
<b>KWFT (Mt. Kenya Region)</b>	6,922	9,332	35%	11,665	25%	34%
<b>Total</b>	<b>10,880</b>	<b>13,092</b>	<b>20%</b>	<b>16,711</b>	<b>28%</b>	<b>27%</b>

However, it is important to treat the figures provided for AMAs and MFIs with some caution. It can be hard from the AMA records to fully establish the status of members in the system. It is likely in both cases that some of the members recorded are, in fact, in long-term default, or for voluntary reasons are no longer active members of the group. However, they may be retained in the membership in order to maintain the pressure to recover the outstanding loans or in order to improve outreach appearance. Hence the active membership is certainly lower. But even if we estimated this to be a maximum of one-third of total membership, outreach of 20,000 is still impressive.

A further unknown is the extent to which groups disband since AMAs do not keep records. As is explained below, there is certainly a dynamic of increasing outreach in order to maintain revenue, however old groups are unlikely to disband completely, so that these numbers do mask increasing numbers of inactive groups as well as defaulting members.

The majority of AMA groups are women only; there are very few men's groups. The AMA model serves a wider client base than the mainstream donor funded MFIs who tend to focus their attention on micro and small entrepreneurs, providing credit for enterprise activities. While the clientele of AMAs includes micro and small entrepreneurs, their members are also drawn from other socio-economic strata, including salaried workers such as nurses, teachers and civil servants as well as subsistence and semi-commercial farmers. Hence their reach into the rural areas is much greater than the MFIs. The inclusion of salaried workers can result in ASCAs with substantial revolving funds (some with over KSh 1 million).

### **3.2 Financial Performance at the Group Level**

Calculating the financial performance at the group level requires us to view group members from two perspectives. Because the group lends to itself there is no net profit to the group as a whole. Nevertheless we can look at group members in one instance as savers (who are in effect lending their saving to borrowers in the group) and then separately as borrowers and describe the financial position of group members either as lenders or borrowers. As group members are able to decide whether to save more or to borrow more we can actually look at the earnings and costs of either position.

Even more so than with outreach figures the financial records maintained by the AMAs must be treated with caution due to poor record keeping practices. We have nevertheless attempted a basic analysis of these, rejecting records that appear unreliable.

The dividend paid at the end of 1998 to members in the groups studied in 1999 ranged between 16% and 60%, with an average of 34% for the 16 groups for which data were available. Dividend yields currently

appear to average around 20%. From the perspective of a net saver in the system, this compares favourably to bank deposits, which yield about 2% per annum.

The interest rate charged by the managed ASCAs reflects the high value placed on money in the informal sector. Short-term advances loans charge 10% per month and, therefore, have a theoretical yield of 120% per annum. Arrears in most these portfolios prevent the achievement of this yield, however, the short-term advance funds appear to provide yields of between 40 and 70%. This is calculated on the basis of the internal rate of return (IRR) on the cash flow generated by the short-term advances, a simplified example is provided in Table 4.

**Table 4 Example of using IRR to Determine Effective Yield**

Month Ending	Net Monthly Cashflow	Disbursed	Principle and Interest Recovered
Jul-00	-100,000	100,000	0
Aug-00	5,000	100,000	105,000
Sep-00	5,000	100,000	105,000
Oct-00	5,000	100,000	105,000
Nov-00	5,000	100,000	105,000
Dec-00	5,000	100,000	105,000
Jan-01	5,000	100,000	105,000
Feb-01	5,000	100,000	105,000
Mar-01	5,000	100,000	105,000
Apr-01	5,000	100,000	105,000
May-01	5,000	100,000	105,000
Jun-01	5,000	100,000	105,000
Jul-01	105,000	0	105,000
<b>Total</b>	<b>60,000</b>		
<b>IRR mthly</b>	<b>5.00%</b>		
<b>IRR annual</b>	<b>60%</b>		

From the perspective of a saver in the *Ngumbaco* system, 40 to 70% pa. return compares favourably to bank deposits, which yield about 2% per annum. For the long-term loans have a lower interest rate (usually 17% flat) but a lower level of arrears have a theoretical yield of about 33%. Actual yields on long-term loans portfolio appears to be, however, around 25%. While longer-term loans are usually more risky in microfinance, the higher quality of the longer-term loan portfolio may be explained by the dramatic reduction in the interest rate charged which seems to make these loans more manageable.

The fund yields should not be confused with the cost of borrowing from the group. This is because in order to borrow one must contribute 33% of this oneself. While this contribution may earn around 20% pa. effective (the average amount paid in dividends), to the borrower, who borrows this amount back at a higher rate, they are worth much more than this. With returns on this compulsory deposit at 20% pa., this increases the actual cost borrowing Ksh 5,000 for 12 months to an Annualised Percentage Rate (APR) of about 68%<sup>10</sup>. Applied to short-term advances this translates into an actual cost borrowing Ksh 1,500 for 1 month to an Annualised Percentage Rate (APR) of about 174%. While these figures appear quite high they are generally lower than those calculated for traditional MFIs due to the fact that AMA borrowers (unlike those using MFIs) receive substantial returns on their compulsory savings.

<sup>10</sup> The annual effective rate on these loans depends upon their exact duration and the dividend being paid on savings. Using a cash flow model for a 12 month loan and assuming no return on savings gives an annual effective rate of 96%. If dividends of 20% are imputed on savings, then this rate falls to 68%.

The following financial information was collected from the random sample of 28 PFP groups in 1999 and the 18 groups surveyed in 2001 during the current study.

**Table 5 Savings and Net Worth**

Financial Indicator	1999		2001	
	KSh	US\$	KSh	US\$
<b>Estimated Total RLF (millions) WEDI, SEDI &amp; PFP</b>	155	1.99	215	2.75
<b>Mean savings per group (av. group shareholdings)</b>	137,968	1,769	149,308	1,914
<b>Mean savings per member</b>	4,181	54	4,524	58
<b>Mean worth of group (Av. Revolving Loan Fund<sup>11</sup>)</b>	294,539	3,776	242,564	3,110
<b>Mean worth per member</b>	8,925	114	7,350	94
<b>Average long-term Loan size and % of total fund</b>	5,177	58%	5,596	76%
<b>Average short-term Advance size and % of total fund</b>	2,767	31%	1,584	22%
<b>Average size savings held in bank and % of total fund</b>	982	11%	170	2%

The total Revolving Loan Fund (RLF) of these groups can be estimated at KSh 155 million or about US\$ 2 million in December 1999. By mid-2001 this had increased to an estimated KSh 155 million or about US\$ 2.75 million.

This data suggests that member's average outstanding advances and loans have reduced from about KSh 8,000 (US\$102) in 1999 to about KSh 7,000 (US\$92) in 2001 as a result of a reduced mean worth of groups (banked funds are at a bare minimum). This figure will be distorted (reduced) in rapidly growing AMAs (ie. new groups will have relatively small RLFs bringing down the average), however, the relative maturity of groups appears not to have changed that markedly since 1999. More likely is that this reflects the tighter economic in which members are under pressure to draw down more extensively on their savings.

The data also suggests that these groups represent a very efficient means of intermediating savings as, on average, only a small percentage is banked. The system functions by attempting to re-lend as much of the money collected at a meeting as possible. Thus only excess funds, which cannot be re-lent, are banked. The ratio of loans and advances to actual savings was 191% in 1999 and 160% in July 2001. This is due to the build up of accumulated profits in the fund that have not been distributed as share dividends.

However, as already discussed, there is no data held in the main records on non-performing loans so it is difficult to assess the actual health of group's portfolios. Nevertheless, based upon an analysis of monthly loan and short-term advance disbursements and recoveries we can draw some sketchy conclusions as to the portfolio quality. Short-term advances charge 10% per month and, therefore, have a theoretical yield of 120% per annum. Arrears in most these portfolios prevent the achievement of this. The *Ngumbaco* loan funds appear to be mostly yielding between 40 and 70% indicating substantial losses are being incurred through principle and interest default.

### 3.3 Financial Performance of the AMAs Themselves

The ASCA Management Agencies all charge a 1% commission each month on the total loan fund (loan portfolio plus cash in hand) up to a maximum of KSh 2,500 (USD 32). In addition, a fee is charged for the provision of savings books. Before loan losses are taken into account, this represents an annual cost of a little over 12% to the group fund, which compares very favourably to the effective rates charged by traditional MFIs in Kenya, which are commonly between 50 and 300% above prime lending rates.

However, despite what would appear a relatively modest fee structure these ASCA Management Agencies are proving profitable. For example, SEDI's net profit for financial year 00/01 was around KSh

<sup>11</sup> This is the gross estimated value of the portfolio plus cash in the bank. Not all of this is converted into member shares.

1,253,000 (USD 16,064) giving an adjusted return on assets (AROA) of over 2,000%. This high return on assets is of course a function of the very low asset base but illustrates the low financial barriers to entry in to this market. Profitability is also aided by a highly frugal management style that is in keeping with that of their clients. SEDI operates out of a tiny rented office costing USD 50 per month; Loan Officers earn about USD 50 per month and travel by public transport. SEDI's administrative and operational efficiency ratios<sup>12</sup> are 2.5% and 4.1% respectively, which is extraordinarily efficient compared to the same ratios commonly found in traditional MFIs. Average administrative efficiency for African MFIs has been reported at 57.5% (MicroBanking Bulletin 2001).

## **4 Explaining Performance**

The outreach and performance of this model appears, therefore, impressive in the context of a local financial market that has an abundance of financial service providers for clients to choose between. In order to better understand the reasons for client's participation in this model, the research interviewed representatives of 40 groups in focus group discussions, and conducted individual interviews with 22 individuals.

### **4.1 Members Preferences for Managed ASCAs**

Given the diversity of the financial landscape explained above, many members of these managed ASCAs are often also members of both ROSCAs, MFIs, and hold other types of savings accounts in banks, Kenya Post Office Savings Bank and so on. The perceived advantages and disadvantages of the AMA model were as follows.

#### **i) Loan flexibility**

In comparison to ROSCAs, ASCAs offer more flexible loan products both in terms of size and timing. Loan sizes can be larger than a ROSCA and can be taken more flexibly in terms of time. Advances can be taken for a month with an assurance that they can be rolled over if plans do not work out as intended, and the member can decide the period of a longer-term loan. Many women members use ROSCAs as a mechanism through which they can save to purchase domestic consumer items such as blankets, mattresses, plates, cooking pots and so on. In contrast, the ASCAs offer access to larger sums that can contribute to sending children to secondary school or college, improving or building a house, constructing a water tank, or starting or expanding a business. ASCAs can also offer smaller amounts than MFIs whose minimum loan size is usually KSh 5,000 with pressure to increase loans sizes over time. This often makes them more attractive to the rural population who may not want to take loans of this size.

#### **ii) Monthly repayment**

A monthly repayment structure fits better the potential for money to be found for repayments and the rhythm of a rural economy and those who earn salaries. MFI loans are usually paid on a weekly basis, and begin the week after receiving the loan. Many clients felt that the absence of a grace period following loan disbursements from MFIs is hardly enough time to have invested that money in the business and made enough returns to meet the weekly instalment obligation. However, ASCA loan repayments are monthly and give the entrepreneur enough time to invest the money in the business and make a return.

#### **iii) Repayment can be re-negotiated**

There is scope for negotiation over repayment if what is seen as a genuine problem arises. At the same time, unlike an MFI group, the other members do not suffer immediately as a result of this decision as they are not pressurised to make the repayment on her behalf to the MFI because it is the group that is allowing the member to use its funds for longer. This is an important feature of user-owned group financial systems that have the insight necessary to offer a certain degree of flexibility. This is particularly important at a time when economic activity is low and highly uncertain, as it allows borrowers a level of comfort that an inability to repay will probably not result in the financial

<sup>12</sup> Administrative Efficiency = administrative costs excluding financial costs as % of avg. net portfolio  
Operational Efficiency = total operational costs as % of avg. net portfolio

intermediary taking punitive action that may further compromise her ability to meet her financial obligation and provide public embarrassment.

**iv) Access**

A further feature of user-owned institutions such as ASCAs is that members are fully aware of their rights in accessing loans. As long as they have repaid without creating problems and have the right level of savings they know that their access to another loan is more or less assured. This, in turn makes the group very valuable as a resource by comparison to banks or moneylenders. Indeed, one aspect of this is that a member can attend a group meeting and return with more money than she took to it<sup>13</sup>.

**v) Benefits of ownership**

Many members of ASCAs who are also clients of MFIs stated preferences for ASCAs over MFIs for the following reasons. Firstly, the interest that members pay on loans remains within the group and helps the group asset grow, this allows the members to gradually take bigger loans. Secondly, at the end of the year, ASCA members receive a dividend, which can be quite high depending on the individual’s shareholding and profitability of the fund. By contrast, interest paid on loans from MFIs goes to the MFI and the clients therefore see themselves as “working for” the MFI. Similarly, members are very aware that compulsory savings<sup>14</sup> required by MFIs earn little or no interest returns in comparison to the dividends earned from the group funds.

**vi) Support in times of need**

Members reported that their groups not only offered access to financial services, but also offer social support. The group itself, and the social network it offers, can itself mobilise support, whether financial, material or psychological, during times of crisis or significant lifecycle events. ASCA members repeatedly echoed the refrain that they joined their respective groups to “uplift themselves” by “helping themselves”. There is a clear understanding among ASCA members that the benefits an individual can derive through collaborative effort far outweigh what one would be able to accomplish on one’s own. Of course groups are always diverse in the extent of their cohesion and effectiveness in operating as a group and some groups will develop their identity in these ways while others will not.

MFIs run similar group based systems, however, it appears that AMA groups are bound with a greater cohesion and sense of common identity as a result of group ownership of the financial resources. The considered treatment of defaulters and opportunity for loan re-negotiation is a key way in which members can assist each other. Borrowers know that if their reasons are genuine they will at least get a “hearing”, which contrasts to MFIs and banks.

**Give Me The Ngumbaco Any Day!**

I used to be a KWFT client. I got a loan of KSh 10,000 and had to start paying back the money even before I had got the money out of the bank. I had to repay that loan within 3-6 months, savings *hazizai* (earn no interest). I felt that I was working too hard and I wasn’t getting anything from those people. So I decided to leave. At that time I had KSh 5,000 in savings, but they only gave me KSh 3,500. They told me that some money had to be deducted for the CO’s fare, they said I had missed a meeting and therefore had to pay a fine...at that point I was so upset I didn’t even want to listen to the reasons they were giving me for not giving me all my money. I just wanted to leave and never return again!

-Ruth Waeni, Gatunai Adult Women’s Group

**Helping Kamau Rebuild His Business**

A calamity befell Kamau, a carpenter and member of Nyeri *Mwanjo* group. The day before his group’s scheduled meet date, a fire started up in the kiosk next door to his, where the proprietor ran a food kiosk, and razed a whole line of kiosks to the ground. Kamau was able to salvage some of the timber and tools he was using in his business, but he no longer had a place to carry on his carpentry business. Kamau, through his chairman, requested KSh 10,000, which he would use to rebuild his working shed, but repay the group the money at no interest. The group agreed to alter the terms of their loan policy in light of the situation in which their colleague was, as a sign of support and solidarity.

- Nyeri *Mwanjo* Group Meeting

<sup>13</sup> Of course, this may not be a positive feature if it results in unsustainable indebtedness.

<sup>14</sup> There was a perception that the voluntary savings that MFIs require their clients to set aside as partial collateral for their loans are equivalent to the share/savings contributions ASCA members make every month.

There are many means through which groups can assist individuals in the event of a crisis. This ranges from loan renegotiation in the case of “genuine” repayment problems; to the ASCA welfare fund (to which members make regular contributions), which is used to assist individuals in facing unforeseen difficulties. Some of the ASCAs encountered also had guidelines on what members would contribute on top of this to help a member to defray funeral or hospital expenses. Others had carefully defined who qualified as “next of kin”, for those instances where it is not the member herself who is ill, and either set a contribution amount that will be drawn down from the group’s welfare fund, or may sometimes require additional voluntary contributions.

#### **vii) Key member concerns about the model**

While clients report positively on the intrinsic features of the model, they (unsurprisingly) have some complaints regarding the external management. The key concern is in the way that the AMAs carry out default management and their quest for value for money in paying them a service fee. As indicated above, members see this as a key feature of the service as it means that they can avoid the social friction that they would experience if they had to approach their fellow members for repayment directly.

However, enforcing loan repayment is problematic (especially in the current economic climate) given that the AMA does not have a clear mandate to systematically prosecute or punish defaulters. On the one hand the AMA is asked to be effective (tough) in collecting default, on the other hand group members do not wish to be identified as having ‘set the dogs’ onto their neighbour. As will be discussed below, this is further exacerbated by the fact that there is no direct monetary interest for the AMA in improving loan recovery rates. The fact that members often do not see the fruit of this work is not surprising.

Another concern expressed by members relates to the process by which defaults are followed. As pointed out above, once the initial stages are past, the defaulting member herself incurs the costs of default follow up i.e. up to KSh 500 every time the AMA field staff or programme manager visit the home of a member. This may result in a situation where the AMA itself is taking whatever funds the member has available to make a loan repayment. It is not surprising that members feel aggrieved at this process, not only do they see that they have paid a service fee but the process has worsened the member’s and the group’s situation.

This is not an unusual situation in Kenya even when loans are secured with physical assets. It is often the case that the cost of disposal exceeds the value of the items and the debt remains. In fact, one group having realised this after starting to pursue a defaulter, stopped the legal action and have simply attempted to keep the pressure on the member to make gradual repayments.

Some members question the levy of a debt collection fee in addition to the set AMA commission fee that they perceive includes default follow-up. Alternately, some groups feel that they are only really paying for group facilitation and book-keeping services see the commission fee as being too high.

Members are understandably, annoyed when others do not repay, and desirous of leniency when it is they themselves. This points to the need for this issue to be re-examined and possibly adaptations to the model are required – a point taken up in the next section.

## **4.2 Achievements of, and challenges facing the model**

The model of AMA operation has clearly delivered impressive outreach and growth in the last few years and demonstrates a high level of sustainability at the level of the AMA. First, the approach mobilises local savings and puts them into circulation within the local economy. Second, it offers a set of products whose flexibility appeals to a range of socio-economic groups beyond the micro-entrepreneurs to whom MFI programmes have generally been targeted. Third, it has a low entry cost, which results in strong competition among service suppliers, in turn providing pressure for improved client services. Finally, its low cost structure provides good prospects for sustainability both at the level of the group and the AMA.

The model offers an approach that occupies a middle ground between mainstream MFI operation and self-help group development approaches. By providing external finance to groups, MFIs have to use the

group system as a means of collateral, which can create huge resentment among members when they are required to repay on behalf of others. On the other hand NGOs have also attempted to set up and train self help groups to run their own revolving loan funds - often with injections of external finance - with the intention to eventually leave them to be self-managed. This often fails as it underestimates the management skills and social cohesion required for success. The AMA model recognises the difficulties that groups can encounter in managing their own affairs in these environments. It offers an intermediate route, which recognises that while group the ownership of a loan fund can create a strong internal dynamic, management and arbitration is usually best provided externally. The lack of external resources available to these organisations appears to have been a favourable factor in the strength of its development.

However, now that the model has been operating for a few years there do appear to be problems arising. This can be understood both as a result of the stage many groups have reached; a stage when group funds have grown to a significant level in the eyes of members and at which the accumulation of default starts to present a problem to the group; and this situation has undoubtedly become more apparent in the context of members experiencing falling levels of income. Further analysis of the model demonstrates that these problems in part arise from the contradictory incentives, which arise from the way in which it is structured.

### **i) Default Management**

As already explained, the AMA role in default management is seen as a key service bought through the service fee as it presents a means through which members can avoid the social tension and difficulties they would face by having to follow up members themselves – as indeed they are required to do in the common MFI solidarity lending model. However, this separation of ownership of the funds from the collection service creates what is called a ‘principal-agent’<sup>15</sup> problem. The AMAs earn a fixed fee from the group and therefore in order to maximise their own returns wish to minimise the time and effort they spend following up defaulters. Moreover, the fact that they can pass on costs of follow up to defaulters could be seen as an added incentive not to deal with them effectively.

The quality of the portfolio of the group can gradually deteriorate as the default problem increases. But loans are not written off at the group level<sup>16</sup> as this would send negative messages to other members. Hence the value of the TRLF, on which the AMA levies its fee, does not fall by the full amount of potential loan loss. The model does not therefore allow the AMA to be rewarded in relation to its ability to actually manage the default problem. Indeed the AMA has an incentive to use strategies that maximise the growth of the TRLF (regardless of default) at least until it has reached the maximum service fee.

However, while the formal model does not adjust the service fee for poor default management, there is a mechanism through which this sometimes happens in practice. Group members are very aware of the amount of money that is collected at a meeting from savings and repayments, as this is the money that is used to give new loans at the meeting (and to pay the AMA). If this amount starts to fall, as it has recently due to low savings and poor repayment, then the group may negotiate with the AMA to reduce the service fee. It is at this point where ‘money on the table’ stagnates or falls or when dividends deteriorate, that the default problem becomes more apparent to the group. Nevertheless, this is a *de facto* mechanism, which is not a feature of the model and is likely to be exercised with differing degrees of effectiveness depending on the strength of a group’s negotiation powers<sup>17</sup>.

---

<sup>15</sup> The principal-agent problem is one where the payment incentives are not sufficiently well aligned, or supervision is inadequate, to ensure that the agent delivers services as defined by the principal. In this case the principal is the group and the agent is the AMA. A classic case of the principal-agent problem is where labour is paid a daily rate but the employer cannot adequately supervise – it explains the use of piece work systems. In the context of credit unions see also Branch and Baker 1998; Balkenhol 1999.

<sup>16</sup> Although the members shares may be used to offset as much of the loan as possible.

<sup>17</sup> One group had got to a stage where it had an extremely serious default problem. It had adopted the tactic that unless the AMA produced repayments from the defaulting members it would not sit down at the meeting place, and hence refused to pay the AMA’s service fee.

The process of managing defaulters is problematic because it can create a vicious spiral in which the group becomes discouraged when the amount of money collected at a meeting falls because this means that they in turn may fail to get the loan they wanted that month. This in turn can reduce their incentive to repay and once this spreads to a critical mass of members in the group it is likely to become dormant. Once this situation occurs it is difficult to revive the group, as there is no mechanism through which to force members out and replace them. Members recruited to a group once it is in operation are supposed to pay up-front an amount equivalent to the average shareholding in the fund in order that they are entitled to an equivalent share of the accumulated interest fund. Yet in this situation they may, therefore, be risking their shares against a portfolio of loans in default. A situation that is unlikely to inspire new members to join.

A further point is that the exact means through which a group can be liquidated is also unclear. When a group is functioning well and a member wishes to leave, the member can give notice and withdraw her shares and a proportion of her 'profit'. However, once the group faces a significant default problem, the individual is not able to withdraw the value of her shares and hence is locked into the group. Nor are there rules about how the group can liquidate or de-link itself from the AMA. Some groups may feel strong enough to do this, but many may not<sup>18</sup>. In part this reflects the lack of an adequate and written down service agreement between the two parties which clearly defines exit options.

As a result of this situation where groups are negotiating lower service fees, obviously the income of the AMA is falling. The AMAs strategy is then to create new groups that can replace the revenue it has lost from groups that are having difficulties. However, these groups are not disbanded and remain in the records of the AMA. This in part explains the heavy rate of AMA expansion in the last two years. But clearly also strains the quality of service that a field officer can offer a group if she has at the same time more groups to service.

This situation means that neither groups nor AMAs have an accurate picture of the financial position of groups. While this may not be perceived as an immediate need by the AMAs themselves, there is a serious danger that if the situation continues to deteriorate this could produce a more generalised backlash that could undermine the AMA model. While programme managers are to some extent aware of the extent of this problem and the importance of default management, it is not only an extremely difficult situation for them to deal with but they do not currently see how to develop strategies that could overcome it.

A further complication in this situation is that because the group owns the funds, attempts by the AMA to pursue default more severely, may be resisted by groups. Groups have the ability – and the right – to determine the default management regime and some groups will wish to be stricter than others. The ability of members to negotiate conditions of repayment is a key feature of a user-owned service. The need therefore appears to be for the AMAs to be able to work more effectively with groups in deciding the strategy, rather taking full responsibility for default management. These kinds of negotiations can be difficult and may require a more nuance than the AMAs are currently able to offer.

This section has hinted at some of the ways in which this situation might be improved. First, part of the resolution of this contradiction could be a stronger and more clearly defined set of responsibilities that fall to the group in terms of default management since it is the group members that own the funds and this is the only way in which the principal-agent problem can effectively be solved. Second, and in consequence of the first point, service agreements between groups and the AMAs which address more explicitly the roles of the different parties in relation to default management could be introduced. Third, means through which to better link fees to the success of the AMA in recovery could be explored. Fourth, service agreements could better clarify the options of the members and the groups to exit the service. Finally, strategies could be developed with the AMAs to address the revitalisation groups that have significant default problems.

---

<sup>18</sup> A situation that can be perpetuated by the way in which members may have strong loyalties to the Programme Manager.

## ii) Constraints to the growth of existing AMAs

The AMAs operating this model have already spread their services across a wide geographical area. Further expansion is potentially limited given the existing organisational structure in which field officers report directly to owner-managers. Under this structure, direct supervision by the programme managers of an increasingly dispersed field team becomes problematic given the difficulties of communication and cost of transport. The organisations have limited organisational capacity to manage growth both in terms of their poor reporting and monitoring systems and the lack of staff that could effectively run branches. This is no doubt exacerbated by the risk that field officers, given a degree of autonomy in an area, will themselves split off from the original AMA, so undermining any investment that the owner-manager may have made in this expansion. The most recent case of splintering involved a loan officer taking about 13 groups with him. For this reason, among others, Programme Managers try to maintain their own personal relationship with all clients and often rotate field officers to prevent the development of strong client-loan officer relationships. Indeed, because of this strategy members often see the Programme Manager as the only person who has the authority and ability to resolve their problems.

Alternatively, given the relatively low start-up costs to this system, it may be that an organisational structure of a Programme Manager and a number of field officers is in fact the most appropriate, and that further expansion through breakaway staff is, in fact, the most viable one. The challenge would then be to find means of creating a more positive environment in which ‘splintering’ could occur.

## iii) Further development of products and services

As it currently operates, the AMAs provide a template for the services that the group offers. Strong groups are able to develop their own additional activities, such as mutual support mechanisms for unforeseen circumstances; they may change the rate of interest or adapt loan sizes and so on. In general the AMAs do not operate in a manner that is intended to build the capacity of the group to manage its own affairs. This is again one of the conflicts of interest that can arise. To an AMA a good group is one that is easy to run and which the AMA wishes to carry on deriving revenue from, in part to subsidise the provision of service to new groups. However, some groups are strong enough to learn the system and eventually take it over. An approach by AMAs that sought to better develop the skills of the groups and potentially offer an alternative service, which involved for example, the provision of a supervision or audit function to groups on an intermittent basis, might be a new service for the AMA to offer.

While the products that currently exist appear to satisfy the needs of a variety of socio-economic profiles, developing these products and services further and improving the transparency and accountability with which they are delivered, is likely to be costly for organisations such as these - especially in the current economic environment. While modifications to services have occurred on account of feedback from clients, there is currently limited capacity within the AMAs to systematically respond to client needs and improve service. Aspects such as the improvement of financial management systems are key to the overall development of the service. Indeed some relatively simple modifications and the introduction of systems for cross checking could better ensure the quality of the product to clients.

## 5 Conclusions

### 5.1 Strengths and Weakness of the AMA Model

The strength of the ASCA Management Agency approach is twofold. First the service providers are driven by an entrepreneurial spirit and profit motive that ensures client - rather than donor - satisfaction. Second, the model builds upon the popularity and familiarity of ROSCAs. Third, it is an approach that does has very low entry and operating costs and is therefore potentially replicable without donor support.

The sections above have sought to detail the reasons why members like the design of the managed ASCA system. These features have included: the flexibility of loan size and timing; the monthly savings and repayment which fits the rhythm of income flows; the ability to re-negotiate the repayment schedule when problems strike; the assurance of access; the benefits of a user-owned system in which interest on loans benefits the members and consequently they reap a reward for saving; and finally the support groups offer each other in times of need.

Table 6 below provides a summary of the strengths, weaknesses, opportunities and threats faced by both this model and the more standard externally funded group-based lending model which has tended to dominate donor intervention in the microfinance scene in Kenya.

**Table 6 SWOT Analysis of the AMAs**

	<b>ASCA Management Agencies</b>	<b>Traditional MFIs</b>
<b>Strengths</b>	Low operating expenses and minimal capital costs Strongly client focused products and services (due to financial dependence upon clients) Flexible management able to respond rapidly to opportunities	Well known product with strong donor support Relatively strong information and administrative systems Strongly centralised control over products and services
<b>Weaknesses</b>	Weak portfolio management Weak institutional management High rate of staff breakaway Dependency upon single leaders (lack of middle management) Dependant upon local capital	Weak client focus in products and services Poor outreach (low client intake and high dropout rates) High operating expenses Doubtful financial sustainability Dependant upon external capital availability
<b>Opportunities</b>	Development of simple but effective systems for portfolio management and analysis Development of simple but effective administrative and internal control systems Inter-group financial intermediation of unused group funds (possibly in collaboration with a formal financial institution)	Increase commercial orientation e.g. inclusion of a broader range of clients along with products that serve their needs Reduction of high overhead administration costs Development of low cost and efficient service delivery systems Development of client focussed products and services that attract a broad cross section of clients
<b>Threats</b>	Deteriorating portfolio quality may undermine the reputation of the model causing mass exodus of capital	Withdrawal of donor support

## 5.2 Lessons for Mainstream MFIs

MFIs in Kenya are at a stage that, while having extended outreach, the majority still fall short of achieving financial sustainability. The AMAs therefore offer some valuable lessons in the following areas.

### i) Reducing Operating Expenses

Most Kenyan MFIs have evolved from NGOs concerned with relief and development. They have traditionally been dependent upon donor funding and, unlike private investors, the donor community has been tolerant of high cost structures. Over the last five years there has been a decided shift in donor thinking and MFIs are now generally expected to become commercially viable. Traditional MFIs in Kenya will need to follow the AMA example and radically cut their operational expenses and expand their client outreach if they are to achieve financial sustainability. This requires deeper consideration for example of the levels of staff skills required, and perhaps also a re-consideration on the part of donors of the scope and complexity of reporting required. We are not here suggesting that the extremely minimal level of reporting and financial management of the AMAs can be replicated in the context of the needs of donor or other external funding agencies, however, greater modesty in modes of operating is no doubt possible.

## ii) Improving Outreach

Kenyan MFIs need to look seriously at the underlying causes of their poor outreach (which is resulting from both low client intake and high dropout rates). A number of African dropout studies<sup>19</sup> suggest this phenomenon is resulting from client rejection of mainstream MFI credit products due to their inappropriateness to the financial needs of clients and the inconvenience associated with participation. If outreach is to be significantly improved it is likely that MFIs will have to invest much more time and resources into market research to better understand their clients' financial needs and capacities. Unfortunately the incentive to do this may not arise until donors withdraw.

The MFIs may also need to look beyond their core client base and, with appropriate products, seek out additional clients who can contribute to MFI sustainability. If MFIs are serious about serving poor households they should be able to cater to the needs of a broader clientele without losing their ability to also effectively serve poor households.

However it is also clear that the MFIs are limited in their ability to learn from the AMA model in that user-owned systems have a particular set of dynamics that relate to the lack of external funding.

## 5.3 Recommendations for Donors

Necessity is the mother of invention and the innovation of the managed ASCA model arose as a direct response to the withdrawal of donor funds. At present it is far easier for an MFI that is experienced in donor relations to secure income from donor grants and subsidised loans than from their own loan portfolio. Donors face their own dilemmas in deciding how to encourage MFIs to become more commercially oriented and enable them to exit from these relationships. However, this experience suggests that such a withdrawal can spur new innovation based in grounded experience of the products and services clients need.

Given the history of this model, it is clear that donor intervention in the AMA model could destroy the essential positive qualities that these organisations embody. For example, the provision of fund for AMAs to on-lend to groups could be seen as one approach to the solution of the loan recovery incentive problem we have identified. But this is likely to replicate previous experience when groups often collapse if the funds are perceived as donor money. It is also likely to fundamentally distract the AMAs attention away from providing the services their members need (and will pay for) towards those that the donor needs. It would also considerably stretch the current capacity of these organisations in terms of financial management.

It is clear from this analysis that, while the AMA model has demonstrated considerable success, the model now seems to be at a point that its underlying design needs to be revisited in order to disentangle the incentive structures in a way that can lead it to renewed health and growth. ASCA Management Agencies will probably need technical assistance to achieve this since it currently appears that they are struggling to develop new strategies to address current problems.

In addition, if individual AMAs are to expand further they will need to upgrade their administration and management systems and improve their accountability and transparency to groups regarding fund management. Such organisational development is necessary in order to assure the quality of the service being provided. If these organisations wish to continue their geographical expansion they will need to create a layer of competent middle management and organise their internal incentives in a way that minimises concerns about 'splintering'. However, the bureaucracy resulting from such a move could reduce the AMA's current capacity to respond relatively quickly to the client needs and concerns. It is not yet clear how economies of scale and scope can be achieved in the operation of the model that would justify such an approach. Many expanding small owner-operated businesses are unable to successfully undertake the transition to a medium sized business in which the owner ever-watchful eye is replaced by effective middle management and systems of control.

---

<sup>19</sup> See Hulme 1999; Kashangaki 1999; Mutesasira and Lwoga 1999; Wright 1999; Musona and Coetzee 2001.

The cost of embarking down these paths would be substantial for the AMAs themselves in terms of disruption to their operations and investment in the development of new systems that may not prove to be more cost-effective. There are also inherent dangers to the way donors might also approach the situation. For example, technical assistance provided may not adequately understand the local operating environment.

Donors interested in supporting ASCA Management Agencies should, therefore, be prepared to provide small investments in technical assistance aimed at establishing simple but effective systems for portfolio management and analysis, management and internal control. One approach would also be to operate in a way that enabled the systems developed to be made available to all interested parties to prevent this leading to unfair competition in the managed ASCAs marketplace.

## 6 Bibliography

- Balkenhol, B.** (1999). Introduction: Background and Issues. Credit Unions And The Poverty Challenge: extending outreach and enhancing sustainability. B. Balkenhol. Geneva, International Labour Organisation.
- Branch, B.** and C. Baker (1998). Credit Unions: Overcoming Governance Problems - What does It Take?, Inter-American Development Bank.
- Central Bureau of Statistics and Ministry of Finance and Planning** (2001). Economic Survey 2001, Republic of Kenya.
- Government of Kenya** (1998). First Report on Poverty in Kenya. Nairobi, Ministry of Planning and National Development.
- Hulme, D.** (1999). Client Drop-outs from East African MicroFinance Institutions, Kampala, *MicroSave*.
- Johnson, S.** (2001). From Fragmentation to Embeddedness: towards an institutional analysis of financial markets. FDRP Working Paper no 29, IDPM, University of Manchester.
- Kashangaki, J.** (1999). Client Drop-outs from Kenyan MicroFinance Institutions. Kampala, *MicroSave*.
- MicroBanking Bulletin** (2001). Issue No. 6 MicroBanking Standards Project. Washington, CGAP.
- Musona, D.** and G. Coetzee (2001). Client Drop-outs from Zambian MicroFinance Institutions. Kampala, *MicroSave*.
- Mutesasira, L.** and C. Lwoga (1999). Client Drop-outs from Tanzanian MicroFinance Institutions. Kampala, *MicroSave*.
- Wright, G. A. N.** (1999). Client Drop-outs from Ugandan MicroFinance Institutions. Kampala, *MicroSave*.

**Annex 1: Research Methods**

The research involved three ASCA management agencies: PFP, WEDI and SEDI.

Quantitative data was collected from records held at the NGO’s offices. Financial data on a sample of 18 groups was collected from group records.

Qualitative research involved:

- Key informant interviews with the programme managers and staff of the NGOs
- Focus group discussions with officials of 22 groups.
- In-depth interviews with 40 members from with the groups sampled.

The groups were chosen randomly from lists provided by the organisations. The officials of the group were interviewed and (as far as possible) two randomly selected members from each group. However, availability affected the ease with which this could be done.

Overall, the profile of interviews carried out was as follows:

	SEDI	WEDI	PFP	Total
Organisation level	Programme manager; Financial controller; Credit officers	Programme Manager; Credit officers	Programme manager; Credit officers	
FGDs	6	8	8	22
Individual interviews	10	15	15	40