Client Protection Under Covid

By Frances Sinha
M- CRIL

***Frances Sinha** is co-founder and director of M-CRIL (now merged with EDA Rural Systems), working in training, evaluation, research and specialist ratings in microfinance and financial inclusion. Based in India, she has been closely associated with global initiatives for social performance management, reporting and assessments, including the development of Social Ratings, the Universal Standards for Social Performance Management, the Client Protection Principles, True-lift principles to support pro-poor practice, and gender analysis. Currently she is on the board of MFIs in India and Cambodia, and engaged as a lead consultant with UNCDF for the evaluation of their global financial inclusion initiatives.*

The client protection principles[1] and their indicators have been developed for 'normal' times. There is no specific guidance on protecting clients when a pandemic puts every household at risk and market closure means that clients cannot earn: when 'over-indebtedness' has become complete inability to pay the instalments on outstanding loans due to factors outside the control of the client or the lending institution.

Looking at the situation particularly in India, and for a small urban MFI that I am associated with, I reflect on the responsible measures that are needed in these challenging times.

COVID has hit us, leading to unprecedented situations, to which microfinance institutions and their clients are still adjusting. The basic and potentially catastrophic risk of infection has led to market shut-downs, transport shut-downs, and uncertainty about when things may normalize (if the virus weakens or an effective

[1] https://www.smartcampaign.org/about/smart-microfinance-and-the-client-protection-principles There are seven principles of client protection: 1. Appropriate product design and delivery, 2. Prevention of over-indebtedness, 3. Transparency, 4. Responsible pricing, 5. Fair and respectful treatment of clients, 6. Privacy of client data, 7. Effective mechanisms for complaint resolution.

vaccine can be deployed). Market and transport shutdown in many countries has affected most sectors of the economy, including the informal sector. Microfinance borrowers typically lost their ability to earn: they could no longer trade; teashops, canteens and small manufacturing units had to close; casual work disappeared; casual and domestic employers usually did not pay staff if they were not showing up for work.

Microfinance Institutions (MFIs) suddenly found the ground cut from beneath their feet. The microlending business model depends on revenue from the regular inflow of loan repayments, combined with ongoing outflow of loan disbursements to continue generating more revenue. Market shutdown meant that Inflows and outflows came to a stop. Not only could most clients not make their regular repayments, there was little scope for loan disbursement in terms of demand and supply too, with MFI branches closed, field staff not going out into the field – and very marginal use of digital payments systems. Nevertheless, operational expenses of running an MFI continued – overheads, rents, and particularly staff salaries. Whilst travel expenses reduced, MFIs were trying to continue to pay and motivate their staff recognizing the importance of their salaries for their families. At the same time, repayments to lenders to MFIs were also falling due.

In these circumstances, key principles of client protection apply more than ever. Even in 'normal' times, low income clients may face a shock (illness, death, crop failure, business failure) that makes them unable to pay their loan instalment. Under COVID, many clients have lost their livelihoods, losing their ability to meet household needs, let alone repay instalments on outstanding loans. Pressure on clients to repay in such circumstances is not appropriate.

The introduction of a moratorium on loan repayments – by some MFIs independently, or in some countries (such as India, Myanmar) by the regulator – has been an important stop-gap measure, postponing the repayment requirements. But having a moratorium raises further questions: Do clients fully understand the implications of a moratorium – that it does not involve a waiving of the interest due during the moratorium period, and that the interest accumulates and will need to be paid after the moratorium ends? Would some clients prefer to continue their instalments without a moratorium? For other clients when is the appropriate time to start repayments = can some clients start repayments earlier, do other clients need more time to recover?

Communication for transparency is a key part of client protection. Keeping in touch with clients has continued through regular phone calls by field staff. MFIs' management quickly realized the importance of these calls for two way communication: giving key messages - about coping with COVID 19, what to do in case of illness, what government support might be available, what options there were for loan repayment, and also an opportunity for structured conversations with documented responses on a small number of 'survey' questions better to understand each client's situation and perspective: What are the main sources of income for the household and how have these been affected by the market lockdown? What are the client's main concerns and how is she coping? Does she feel able to pay her loan instalment or does she need a moratorium? When does she think she can start repayments again? What repayment structure would she prefer? Will she need a bridging loan to restart her business?

The Social Performance Task Force (SPTF) developed a useful questionnaire tool for MFIs to adapt and use to suit their situation.[2] A webinar series, *Using Customer Insights to Drive your COVID response*, is available on the SPTF website featuring experiences in conducting clients surveys through phone calls by field staff, sample details, the analysis of findings and how financial service providers to low income households have used the findings to inform operational decisions to support their clients.[3] Organisations who have shared their experience include FINCA International (20 community bank MFIs and banks across all continents), BRAC International (5 countries in Africa and Myanmar), SEF (South Africa), 4G Capital (Kenya) Ujjivan small finance bank and Annapurna (India) Al Majmoua (Lebanon) and Vision Fund International. Microfinance networks in several countries have adopted the client survey tool, trained their members on its application and supported the analysis and reporting – with an overall report for the sector, and separate reports for individual MFIs. Some MFIs have themselves continued to collect and analyse data, adapting and adding their own questions, as the lockdown has continued.

The different surveys have shown that 90% or more of clients are facing a loss in income, around 30% of businesses may continue but are badly affected, reporting

[2] https://sptf.info/covid-19/covid-19-client-interview-tool

[3] https://sptf.info/covid-19/spm-during-the-crisis

that suppliers have increased their prices. Coping strategies reported include reducing household consumption with a small proportion able to draw on savings. Very few clients can opt for digital payments (even with 4G in Kenya).

Blocking effect of coronavirus disease (covid-19) in agriculture. A farmer destroyed his tomato plantation due to the blockade in India.

Photo credit: Shutterstock

A key feature of the findings from such surveys has been the importance of segmentation for understanding significant differences between clients and using this information for follow up. Thus, in India we have seen agriculture continues; those involved in dairying or vegetable production continue to earn – they are able to repay, and continue borrowing, if there are channels do so. On the other hand, many of those self-employed in trade or services have had to shut down.[4] In urban areas where some microfinance households have depended on salaried or contractual employment (including for example domestic workers, drivers), this source too has been largely cut off.

The figures below illustrate this shift as reported by nearly 21,000 (mostly women) clients of an urban MFI[5] in India during May-July. Just 6% of clients in this MFI said

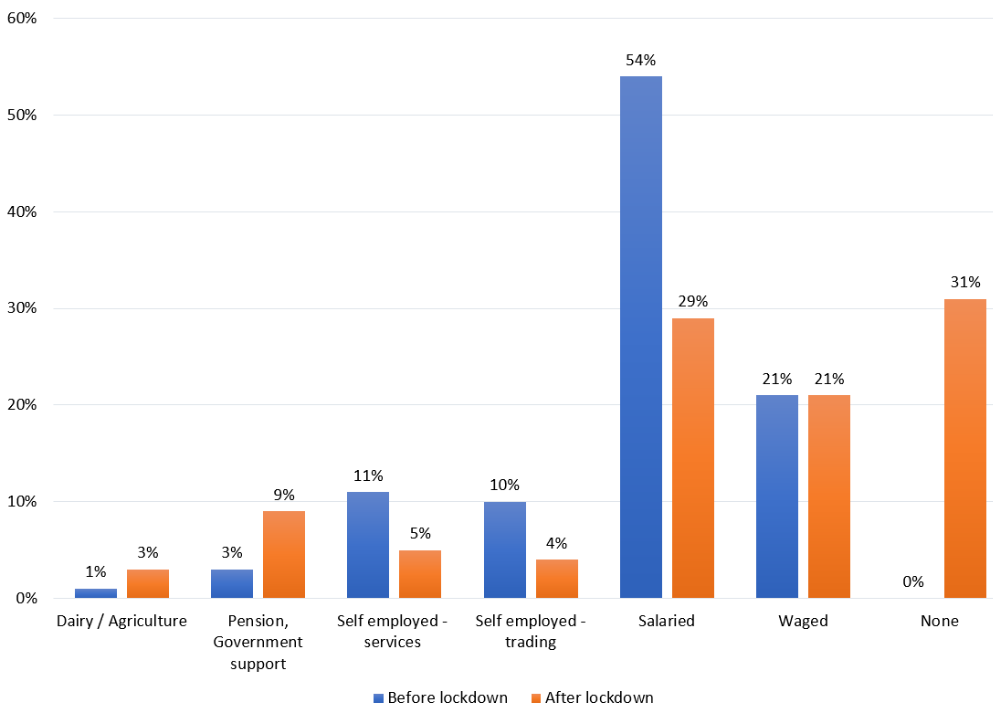
[4] This example of segmentation is documented for SKDRDP, India, in the SPTF client interview tool. The critical relevance of different income sources underlines a need for clear definition of different types of income source (including different trading categories – wholesale or retail) for the client and other household members, with documentation in the management information systems of the portfolio.

[5] This was the number of total clients that could be contacted in one city. Operations saw no need to sample – since field staff were trying to keep in touch with all their clients and the questions were a good

they could repay their instalments on time. The majority needed the moratorium that was advised by the Reserve Bank of India, first announced for two months up to end May 2020, then extended a further three months up to the end of August.

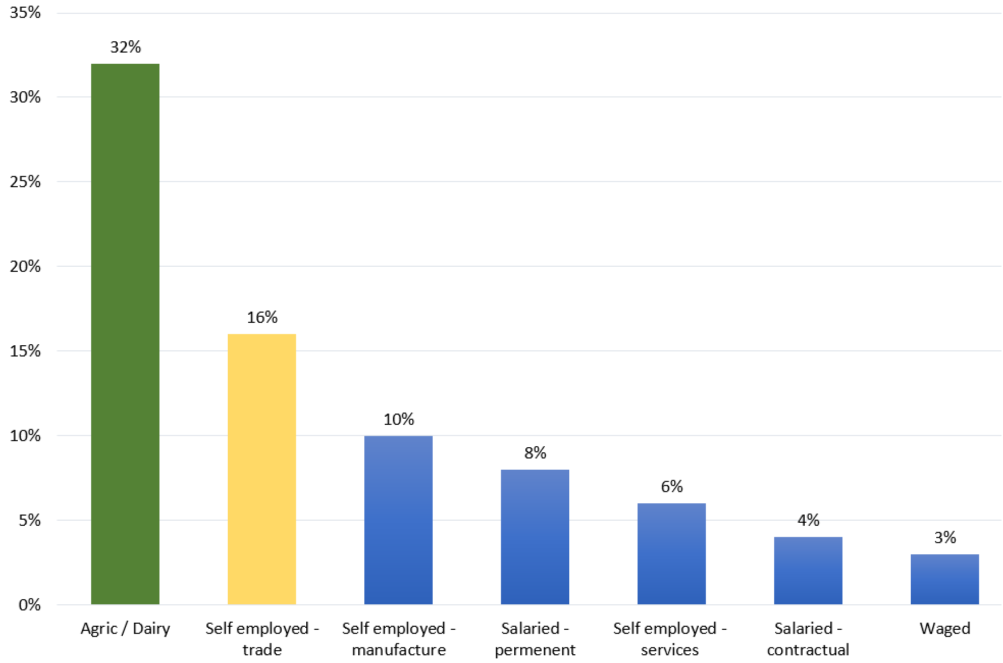
In the survey, just 0.5% of clients had family members ill with COVID 19. The main effect of COVID was the market lockdown.

Reported income source – before and after lockdown



Clients who said they can continue to repay their loans on time – by income source

way of structuring a conversation that relevant to loan repayment, but also reflecting a concern about the family circumstances and what was happening.



[Effect of COVID 19 and the lockdown on clients. Telephonic survey of 20,910 clients by an urban India MFI]

A second round of the telephone survey during July/August was used to explain the repayment options after the moratorium ended, to ask clients their preference, and how long they would need before they could start repayments. The responses are clear that for most clients, at least a further one month would be appropriate. Clients were willing to continue with the same equal instalments as before the lockdown, but they asked for these to be extended over a longer period of repayment (to cover the additional interest due); several requested a reduced instalment after lockdown that would increase gradually.

After the moratorium ends, how long will it take before you can continue loan repayments?	
Total respondents	20,907
	100%
Already paid	6%
After a week	3%
1 month	67%
2 months	16%
Don't know	7%

These responses make sense in the context of market uncertainty, and incomes only gradually picking up as things return to normal. Normality – with regular repayments of outstanding loans - will not be immediate. The market feedback is clear in showing which clients are unable to pay and that immediate collection of the entire interest incurred during a moratorium would represent undue pressure on many clients as their earnings begin to recover.

People stand in queue maintaining social distance to get free food during nationwide lock down imposed in the wake of COVID 19 Coronavirus pandemic on May 18,2020 in Calcutta, India. Photo credit: Shutterstock

This information is important for MFIs not only as they figure out their strategies for their clients, but also as they navigate the repayment requirement on funds from their lenders (banks, investors). MFIs are of course under pressure to collect as soon as they can – liquidity is under threat as they try to cover continuing expenses. Payments to their own lenders or funders are also due.

MFIs may consider incentives – to their clients (through a small reduction in interest if they repay sooner) and to staff if they can reach a certain level of collections. Loan restructuring that is tailored to expected cash flows seems more responsible than a cash incentive to clients. Whilst any incentives considered for staff must have the checks to ensure that clients are not being unduly pressurized. Such checks would include, ensuring an effective complaints mechanism, and also having internal audit follow up proactively with a sample of clients who are paying their instalments: Are they comfortable making the repayments? Are their earnings on track to recovery? Can they meet their household needs?

There are issues still to be resolved, as we look for recovery. But it is clear that genuine commitment to client protection cannot just be ticking a set of normal indicator boxes, but goes beyond this to having the core principles of client protection principles embedded in governance and informing operational decisions, responding to the feedback from the market. We are also seeing that the principles of client protection cascade across the value chain of financial investment – from the MFIs lending to low income households, to the banks and investors who provide funding to MFIs. Funders to MFIs also have to be responsible. Can they adjust repayments and agreements, in the same way that MFIs are having to adjust for their clients?