MicroSave Briefing Note # 12

Two Perspectives on Savings Services[1]

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Savings Products and Services from a Saver's Perspective

Balancing Convenience, Risk and Returns

It is clear that most poor people do not have **access** to formal sector banks for reasons that include the:

1. Geographic distance from the financial institution;
2. Terms and conditions governing the available financial services it offers;
3. Disrespectful manner in which the staff treat poor clients;
4. Intimidating appearance of the financial institution; and
5. Complexity of the paper work and the difficult process necessary to make a transaction.

The poor look for some system to provide the **security** and accessibility necessary to save. Acceptable degrees of security are relative, dependent on the available programme, and are never 100 per cent. Almost every poor person has been in, or knows of, a failed Rotating Savings and Credit Association [RoSCA] or crooked deposit collector, but the accessibility of a regular opportunity to save in a disciplined manner is what makes RoSCAs and deposit collectors so popular worldwide.

Access is markedly different from **liquidity**, and often considered more important by poor people who have little time to make their transactions. While many authors have stressed that "liquidity is the key to local savings mobilization", it is important to note that in many circumstances the poor have a strong "illiquidity preference". This "illiquidity preference" is in response to the poor's self-imposed need for structured and committed savings mechanisms that prohibit them from withdrawing in response to trivial needs and allow them to fend off the demands of marauding relatives requesting "loans" or assistance.

With the exception of successful Accumulating Savings and Credit Associations (ASCAs) and auction RoSCAs, the **return** on savings in the informal sector is rarely above zero. Often the poor pay to save through a conveniently accessible system such a deposit collector who visits daily to collect savings.

Managing Liquidity and Duration: A Spectrum of Needs. All families require funds for different purposes that vary with respect to the amount that is needed and the immediacy with which the funds must be made available. Many emergencies or opportunities necessitate instant access to cash. This explains why almost all poor families keep some amount of emergency savings in the home, and why many do prefer highly liquid savings services. The "illiquidity preference" described above means that poor people have needs that require both liquid and illiquid services and those that save, often hold multiple accounts to do so. Similarly, poor people often use a strategy of "targeted savings", including some highly illiquid savings, (notably, in the absence of alternatives, MFIs' compulsory savings) to build-up large lump sums of money to purchase significant capital assets such as land and houses.

Compulsory, Locked-In Savings

The poor require little compulsion to save. They simply want a reasonable mechanism to do so and the assurance that they will be able to access those savings as needed. Indeed, there is evidence that compulsory savings, particularly those that are deducted from the loans issued, are simply viewed by clients as part of the cost of the credit. Some clients use these compulsory savings systems to build up useful, long-term lump sums of money. However, it is possible that well designed open access savings accounts and contractual savings agreement schemes could give clients the *option* of setting these funds aside. Furthermore, such systems would not force the clients to leave the MFI, or reduce their ability to access loans, if they need to liquidate their savings.

Designing Savings Products and Services from an MFI's Perspective

Balancing Convenience and Returns

As seen above, when deciding on savings services, poor people look for a mix of accessibility, security, liquidity and (ideally but not crucially) returns. The financial institution's perspective is almost the mirror opposite of that of the client. Financial institutions would like to maintain a few branches in densely populated areas to maximise the number of clients per branch and facilitate branch security. They would prefer to limit opening hours to allow the opportunity to keep up with the complex accounting and internal control procedures necessary to run a financial institution effectively, and to facilitate physical security arrangements. They would like to see large deposits made for as long as possible with a minimum of withdrawals so that the transaction and liquidity

[1]**Wright**, Graham A.N., "A Critical Review of Savings Services in Africa and Elsewhere", ***MicroSave*** 2000 and **Fiebig**, Micheal et al. "Savings in the Context of Microfinance – State of Knowledge" in Hannig Alfred and Sylvia Wisniwski (Eds), "Challenges of Microsavings Mobilisation – Concepts and Views from the Field", GTZ 1999

management costs are kept to a minimum and the funds available for on-lending are maximised. And of course, the profit-maximising goal of a financial institution encourages the payment of as little interest as possible. Nonetheless, there are many MFIs that offer micro-savings services on a profitable basis.

Managing the Costs of Small Savings Accounts

One of the chief fears voiced by MFIs revolves around the potential difficulties involved in dealing with the many small transactions often associated with the providing savings services to the poor. While this is indeed likely to be the case, several **important observations** should be made:

1. Generally, the majority of the transactions will be deposits. Indeed the poor are often remarkably unwilling to make withdrawals. However they do want to know that they <u>could</u> withdraw if a pressing need arose;
2. Poor people have a multiplicity of needs and are not always looking for a highly liquid account to use on a regular basis; and
3. Savings accounts targeted for medium and long-term needs are particularly attractive to MFIs in search of capital for on-lending, and appropriately designed products can encourage these.

There are also important and often over looked, **additional benefits** of offering savings services to the poor. In addition to providing capital for on-lending, savings services can:

1. Develop the client base (of borrowers) for the future;
2. Obtain information on the clients' abilities to save and (by implication) repay loans;
3. Facilitate repayments when clients are unable to meet repayments out of current income; and
4. Encourage repayments, as clients want to maintain a good reputation and their access to future services.

There are also many ways of **minimising the costs** of providing savings services, and possibly even deriving a profit from doing so. This can be done directly through carefully structured pricing to encourage savers to maximise deposits and minimise withdrawals. MFIs can elect to pay interest only on accounts with balances above a certain minimum. In view of the clear evidence that poor people are willing to pay for convenient savings services MFIs can charge fees for specific savings services. In order to reduce withdrawals, MFIs could limit the number of withdrawals per period, set minimum withdrawal amounts, require notice to withdraw or charge for withdrawals made.

In addition to the pricing structure, the MFI can reduce costs through its organisational approaches and work methods. Finally, it is important that MFIs offering savings services seek up-market, higher-value savers to spread the costs and make the service cost-effective to run.

Synthesis and Conclusions

Two different strategies are pursued by outside agencies (be they development or private sector) and by poor people themselves as they seek to design and deliver financial services. The former tend to use a strategy of "permanence and growth" and look to create sustainable institutions that deliver financial services to an ever-increasing number of clients – such as MFIs, banks, and co-operatives. By contrast, poor people generally use a strategy of "replication and multiplication" and look to create many small self-contained, often self-liquidating, schemes – such as RoSCAs and Christmas clubs.

Permanence and growth institutions tend to encourage the long-term build-up of funds through relatively slow, but steady, saving, and are therefore extremely well suited for addressing longer-term savings needs. Replication and multiplication schemes tend to encourage the rapid accumulation and disbursement of funds and are therefore better suited to meeting shorter-term savings needs. There is increasing evidence that providing client-responsive financial services can both serve the needs of poor people while maintaining or in fact improving the sustainability and profitability of the MFIs.

There are no magic formulas for designing appropriate savings products for poor people: it requires market research and careful, systematic product development. But the rewards for the MFIs that undertake these exercises in terms of profits and client loyalty can be remarkable, and well worth the investment.

<u>The Conditions Under Which Poor People Save</u>

From Rutherford[2], 1996

1. they feel their savings are *secure*
2. they feel they can get *access* to their savings (as withdrawals or as loans)
3. they have the opportunity to save *often and easily*
4. they see the *example* of others saving regularly
5. they feel under some *social pressure* to save
6. they feel they *own* their savings (the savings are not owned by a group)
7. they feel the savings are *growing* (by interest rates or bonuses) and protected from *inflation*

[2]**Rutherford**, Stuart "A Critical Typology of Financial Services for the Poor", *Action Aid and Oxfam*, London 1996