Factors Affecting Either the Voluntary Exit or Forced Eviction of Borrowers from Microfinance Loan Networks

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ABSTRACT

This paper seeks to analyse the issue of loan repayment in microfinance institutions and examine the factors that affect the exit of borrowers from microfinance borrowing networks. This paper presents the analysis of the borrower-level data of agricultural microfinance household borrowers in the Philippines from 2000 to 2010. Results show varied set of reasons to explain both the continued, sustained relationship of MFI borrowers with their lenders as well as the strained relationship with some borrowers who were inevitably evicted from the MFI system or had voluntarily exited the system. The study also indicates that MFI borrowers' poor repayment records and eventual exit from the MFI system are attributed to borrowers' weaknesses and uncontrollable circumstances.

BACKGROUND

In the midst of economic crisis, there is often less confidence in the resilience and endurance of the agricultural sector in weathering business survival challenges. The farm sector, especially those from developing countries, is too vulnerable to business and financial risks. The operating conditions of farm businesses usually subject them to unique sources of risk and uncertainty often not faced by other industries.

Farms' capability to weather such crises and remain viable operations, they usually will depend on, among others, the availability of borrowed capital to supplement existing funds to finance their operating infrastructure and working capital requirements. Lending institutions, however, have traditionally tailored their financial services after the needs of large conventional farming systems. These farms end up relying on microfinance institutions (MFIs) that extend smaller loans to their clients compared with commercial lending institutions.

Microfinance borrowers tend to have no properties to offer as loan security (collateral) as they are poor and low-income, and thus would constitute a considerable risk to lenders once they default. MFIs, therefore, have to device a system to ensure that loan defaults are as low as possible in order to maintain their financial sustainability, without which they would resort to higher interest rates that would only defeat the original intent of their microfinance lending philosophy

OBJECTIVES

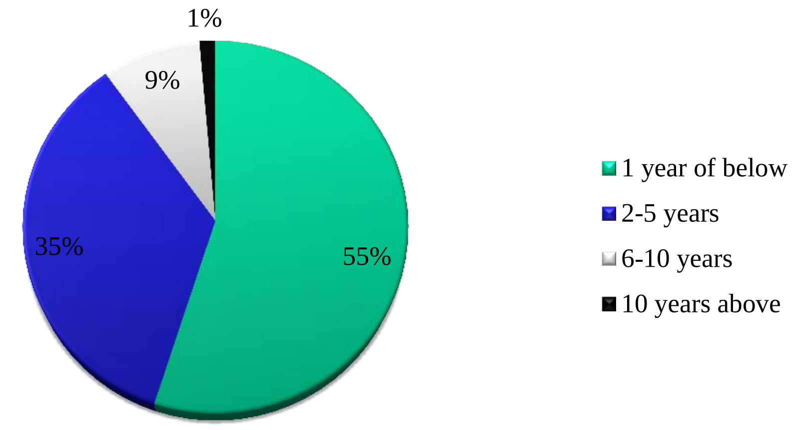
- To identify factors that affect the voluntary exits or forced eviction of Philippine borrowers from microfinance lending networks focusing on indicators that are both internal to the borrowers' personal circumstances and business operating environments as well as those that capture the microfinance institutions' loan delivery operations.

DATA

The analysis will use data compiled by the Social Enterprise Development Partnerships, Inc. (SEDPI) on micro-insurance borrowers in the Philippines from 2000 to 2010. The data set covers a national scope of data on financial characteristics and socio-demographic characteristics of defaulted microfinance clients.

ANALYSIS OF DATA

Borrower's Tenure



Loan Cycle

	Obs	Percentage	Mean	Std. Dev	Min	Max
1 year of below	160	54.98%	1.89	0.94	0	6
2-5 years	102	35.05%	4.92	2.35	1	15
6-10 years	25	8.59%	7.56	4.81	1	20
10 years above	4	1.37%	16.50	7.05	7	24
Total	291	100.00%	3.64	3.27	0	24

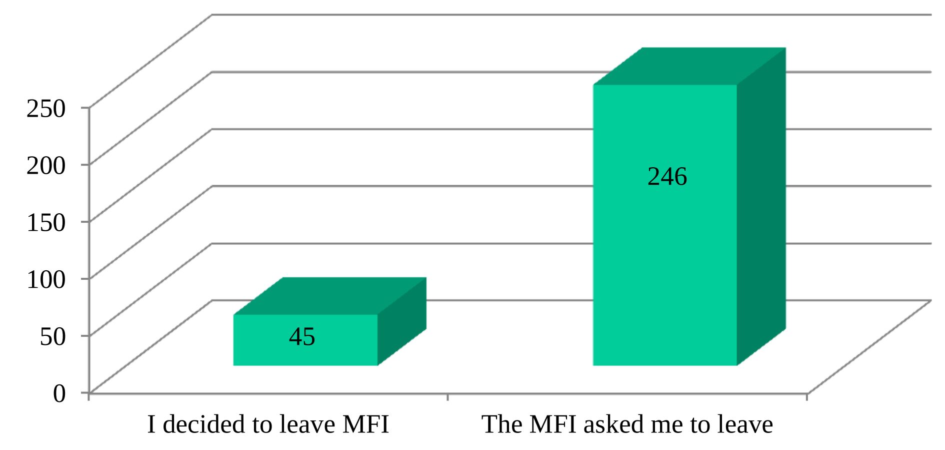
Amount of Latest loan

	Obs	Percentage	Mean	Std. Dev	Min	Max
1 year of below	160	54.98%	7712.50	9063.81	0	70000
2-5 years	102	35.05%	17666.67	39369.87	3000	300000
6-10 years	25	8.59%	28300.00	36865.75	2000	150000
10 years above	4	1.37%	8000.00	8041.56	3000	20000
Total	291	100.00%	12974.23	27232.69	0	300000

Experience of Repaying the Last Loan

	Good	%	Easy	%	Had Problems	%	Difficult	%
1 year of below	72	45.00%	37	23.13%	37	23.13%	13	8.13%
2-5 years	38	37.25%	25	24.51%	33	32.35%	6	5.88%
6-10 years	9	36.00%	7	28.00%	8	32.00%	2	8.00%
10 years above	2	50.00%	1	25.00%	1	25.00%	0	0.00%
Total	121	41.58%	70	24.05%	79	27.15%	21	7.22%

- **The tables associating various variables with the borrower's tenure (length of relationship) with their microfinance lender indicate the following:**
  - Borrowers with tenure ranging from 1 year to more than 10 years have availed of an average loan cycle of about 4x. Borrowers with shorter tenure tend to have availed of more loan cycles.
  - For borrowers with tenure ranging from 1 year to 10 years, the amount of loan tends to increase with the period of tenure.
  - Majority of the borrowers are engaged in trading business, with most borrowers in all business typology groups belonging to the lower two tenure groups.
  - Sixty six percent (66%) of the loan transactions had good or easy repayment experiences, while 27% experienced difficulty in repaying. In terms of tenure, the nature of loan repayment experience is felt during the lowest two tenure periods.
  - Majority of the clients experienced slightly increased and stabilized incomes as results of their borrowing relationships with the MFIs.
  - Those with about a year of relationship with their MFI have greater tendencies to refer their relatives to their lender.



- For borrowers whose relationship with their MFI lender was cut off, majority declared that such decision was their own (15.46%), while a few others claimed that they were asked by their MFI lender to leave the system (84.54%).

Personal Reasons	Number	Percentage
Problems related to policies and procedures	47	25.00%
Problems related to the Center	16	8.51%
Business-related reasons	57	30.32%
Personal reasons	61	32.45%
Economic and community-related reasons	7	3.72%
Total	188	100.00%

	Trading	Manufacturing	Service	Farming	Animal Raising	Fishing
Problems related to policies and procedures	78.72%	2.13%	10.64%	0.00%	4.26%	2.13%
Problems related to the Center	75.00%	6.25%	12.50%	0.00%	6.25%	0.00%
Business-related reasons	71.93%	5.26%	8.77%	1.75%	7.02%	5.26%
Personal reasons	59.02%	6.56%	13.11%	1.64%	9.84%	3.28%
Economic and community-related reasons	57.14%	0.00%	14.29%	0.00%	14.29%	0.00%

Experience of Repaying the Last Loan

Personal Reasons	Good	%	Easy	%	Had Problems	%	Difficult	%
Problems related to policies and procedures	21	44.68%	12	25.53%	11	23.40%	2	4.26%
Problems related to the Center	11	68.75%	3	18.75%	2	12.50%	0	0.00%
Business-related reasons	17	29.82%	10	17.54%	26	45.61%	4	7.02%
Personal reasons	26	42.62%	21	34.43%	8	13.11%	6	9.84%
Economic and community-related reasons	0	0.00%	2	28.57%	5	71.43%	0	0.00%

Income Change as they Invested the Loan

Personal Reasons	Inc subs	%	Inc slightly	%	Stable	%	Dec Slightly	%	Dec subs	%
Problems related to policies and procedures	6	12.77	17	36.17	0	0.00	22	46.81	1	2.13
Problems related to the Center	4	25.00	3	18.75	9	56.25	0	0.00	0	0.0
Business-related reasons	2	3.51	27	47.37	22	38.60	1	1.75	5	8.77
Personal reasons	3	4.92	33	54.10	34	55.74	0	0.00	1	1.64
Economic and community-related reasons	0	0.00	2	28.57	5	71.43	0	0.00	0	0.00

- **Among borrowers that declared personal reasons for leaving the MFI borrowing system, the following trends are noted:**
  - Trading businesses usually cite a mix of personal and business reasons as well as problems with MFI policies and procedures for leaving the MFI borrowing network.
  - Borrowers with good and easy repayment experiences cite personal and business reasons, in addition to problems related to policies and procedures, as basis for their decisions to leave the MFI system.
  - Borrowers with difficulty in repaying their loans cited business reasons and problems with MFI policies and procedures, as basis for their exit from the system.
  - The highest frequencies among the reasons for exiting the system among classes of income changes were recorded for business and personal reasons (for those with stable or slightly increased incomes) while problems with MFI policies and procedures had a high frequency for borrowers who experienced a slight decrease in incomes.
- **Among those that cited problems with MFI policies and procedures, the following are the popularly cited reasons:**
  - Longer disbursement periods
  - Too small loan amounts
  - High interest rates
  - Unpleasant treatment by loan officers
- **Problems cited that are related to the operation of the loan center are mostly due to:**
  - Relationship problem with specific Center personnel
  - Center's decision to evict the borrower
  - Dissolution of the Center
  - Failure to follow Center policies, including attendance in meetings.
- **The most predominant business related issues cited for leaving the MFI system are:**
  - Deteriorating business profits
  - Accumulation of adequate working capital
- **The most predominant personal related issues for leaving the MFI system are:**
  - Risk or loan aversion
  - Pregnancy or need to care for others
  - Relocation
- **A unanimously cited reason for leaving the MFI system is the general economic slowdown that affected business profits and viability.**

SUMMARY AND CONCLUSIONS

- **This analysis has shown a varied set of reasons to explain both the continued, sustained relationship of Philippine MFI borrowers with their lenders as well as the strained relationship with some borrowers who were inevitably evicted from the MFI system or had voluntarily exited the system.**
- **The most often cited reason for borrowers' voluntary exit from the system comprise of personal, business, Center-related, and macroeconomic factors.**
  - Sudden changes in personal circumstances of certain borrowers (physical and economic) may lead to their exit.
  - Business viability issues, often related by majority to general macroeconomic conditions, can lead to deterioration of profits and operating challenges.
  - Center-related problems are usually relationship-related where complaints are more focused on the MFI staff's treatment of borrowers and efficiency issues.
- **The results of this study indicate that while most reasons for MFI borrowers' poor repayment records and eventual exit from the MFI system are attributed to borrowers' weaknesses and uncontrollable circumstances (personal and macroeconomic), there are also factors that may need to be addressed to avoid the surge of borrower exits.**
  - Factors internal to the operation of the Center need to be addressed.
  - MFI staff members need to be educated on proper customer care and service to avoid complaints on unpleasant and unfriendly relations.
  - Greater efficiency in loan delivery can be addressed by exploring strategies to minimize loan processing times and increase the quality of loan servicing.
    - *Increase in personnel could definitely relieve overworked employees with large client servicing burdens.*
    - *Use of more efficient and reliable technological systems can improve loan processing procedures.*