MINUTES OF THE SAVINGS & CREDIT FORUM 29TH AUGUST 2008

Community-managed Savings and Lending Approaches: overview, VSLA model

The Savings & Credit Forum of 29 August 2007 presented a successful Community-based Savings and Lending Approach. Mr. Hans Ramm, Swiss Agency of Development and Cooperation (SDC) opened the forum by welcoming the participants and shortly introducing the speaker Hugh Allen, VSL Associates Ltd. Unfortunately, the second speaker, Mrs. Yetnayet Girmaw Bezabih, who was expected to present a case study from Ethiopia, could not make her way to Switzerland due to European transit visa issues.

VSL Associates Ltd. was founded specifically to promote the adoption of a particular approach to community-managed microfinance, known as the Village Savings and Loan Association (VSLA) model. Its founder Hugh Allen, has exclusively worked on the development of the model since 1995 and has actively facilitated its spread, from its beginnings in Niger to 11 other countries in Africa. Today, CARE, CRS and Plan International have adopted this model throughout their Africa programmes and in Asia.

The community-based savings and lending approach: This approach has been developed as a response to the traditional microfinance model, which often lacks outreach to the poor. It aims at being simple, cheap, and effective, as well as at targeting the most vulnerable. The approach is based on the fact that saving – and not lending - is the lower risk strategy to overcome crisis periods. A study on credit and savings behaviours in Uganda reveals that in most cases credit is not going to productive use, but is rather used to help managing the household cash flow. Moreover, figures of industrialised countries show that savings are used for managing most basic needs (housing, food, education, business capital), while credit is taken for consuming goods (house, car).

The approach is based on a few principles: the source of capital for loans comes from the people's savings (no external money flows to the group), and consequently there is a high social pressure for reimbursement; there are no central bookkeeping records (i.e. ledgers) and little management costs; every single transaction is made transparently in front of everyone; there is a high flexibility to pay back within a given period of time. This approach is a solution for remote areas where MFI are unable to work profitably. The one-time costs per client for setting up the group and making it work in a sustainable way (transport, administrative and structural costs, consulting) range from 5 to 50 Euro depending on the region. The main downside of the approach is the limited capital growth, which restricts the possibility for lending larger amounts for small enterprise growth.

Debates presently turn around whether it is a necessity to link these VSL Associations to banks for making use of additional savings and capital. Building up a link to a bank is a long and difficult process (6-10 years), due to the complex bank requirements. Moreover, the profit is taken by the bank and is thus lost for the community; the group is not able anymore to independently manage its fund and needs long term outside assistance. Therefore, VSL Associations does not see a bank linkage as important. It is up to the group's own decision, if the need for diversified financial services is worth the increase in complexity and costs.

At the question whether a VSLA federation could bring advantages in terms of efficiency for capital use, Mr. Allen answered cautiously that the advantages should be carefully evaluated. Federating VSLA can indeed fail because of decreased transparency and increased complexity.

The VSLA method: A villagers' group first defines its constitution (frequency of meetings, use and priority for loans, value of shares and token, etc). Five persons are elected as management committee. For transparency reasons, every transaction is made in front of the whole group. The unused money and the member passbooks are stored in a safe deposit with three padlocks, the keys of which are held by three members.

The savings are registered individually in each member's savings passport as a number of fixed value shares[1]. Loans are disbursed only once a month and also registered in the member "passport". At each

[1] There is the possibility to save in-betweens meetings, by "buying" fixed value tokens at the box keeper's place and inserting the money through a slot into the three-fold locked box. At the next meeting, the tokens are exchanged for the money, which serves to buy new shares.

meeting, after having collected additional savings and loan reimbursement, every one announces his or her need for a loan (amount, desired loan period and loan use)[2]. Many different ways of using the loans have been observed, e.g. buying goods and selling them when the prices are high on the market. In case of hyper inflation like in Zimbabwe, it happened that the money is replaced by commodities.

The only central record kept is the total amount of remaining savings at the end of the session. Members can decide to withdraw his money at any time. At the end of a one year cycle, after reimbursement of all loans, the cash is counted and distributed per share. Each member receives his shares back in cash, including dividends. A new cycle then starts again.

The set up of a new group is done in three phases:

(1) Training phase (~12 weeks) to set up the group, elaborate the constitution and start first savings and first loan transactions in a very strict procedure through training by doing.

(2) Follow-up phase (~18 weeks): routine installation; the field officer is present at each single meeting and checks if the procedure is followed properly.

(3) Development phase (~18 weeks): disengagement of the field officer who assists now and then and reacts only if necessary. After one year (last meeting of cycle) a "graduation" is done through an action audit.

Impact: A study in Bangladesh, carried out after three years of functioning of a VSLA system, shows that 95% of the community used the VSLA system for saving instead of MFIs, which were as a consequence almost totally abandoned, and 39% borrowed from the VSLA system. An opposite symmetrical tendency is observed between amounts of savings and loans, implying that people tend to borrow less over time, since they can start using their own savings. Indicators on productive assets (land, number of cattle), household assets and other proxy indicators (children at school; number of meals/day) collected through individual households interviews showed significant improvement for VSLA members' households, while the situation for non-members households remained stable or even worsened over the same period of time. Money lending dependency decreased for VSLA members but increased for non members.

Discussion: According to the experience, the method works everywhere although it is less adapted to urban areas due to the lack of space for group meetings and higher risk of theft. The stability and motivation of the group is only at stake if the group is not able to mobilize a certain amount of money per week. However, according to Mr. Allen, the time investment in meetings for labourers is not considered as a too high transaction cost as agricultural labour is often concentrated in short periods. Moreover, there is a significant gain in terms of safety for a labourer to be part of a system where people know him or her.

The VLSA model addresses rather poor people because of its limitation in capital amount and financial services range; this is in a certain extent preventing "better-off" to take advantage of the system to the detriment of the poorer. The programme nevertheless defines its areas of intervention and is thus not fully demand driven, specified Mr. Allen.

The programme's initial investment to set up financial services delivery is a grant, which is justified in terms of sustainability of the VSLA groups: firstly, the people being the investor of their VLSA, the returns on equity benefit them directly; secondly the model is self replicated through identified local trainers who start training new groups and scale up their area of intervention. These trainers are fully paid locally by the groups. Mr. Allen justifies this initial grant by noting that nowadays only few very big MFI are financially sustainable. Two opposite camps argue that MFIs have a social purpose and do not need to be fully sustainable or in opposite, that MFIs have to be competitive in order to attract investments.

The democracy in decision taking of a group is being questioned in the African context. According to Mr. Allen, this problem does not occur, as people define together who they trust and like to include in the group.

To the question whether the methods offer a way to people to escape from poverty, Mr. Allen reminds the participants, that 20% of the demand for financial services falls after having started to save and lend through VSLA, which signals that financial services are a real need.

Mr. Ramm kindly thanked the speaker and the participants for contributing to rich discussions and the organisers of the forum. He referred to last *Inforesources* (Focus No 2/08) entitled "Accessing Financial Services in Rural Areas" available for hand-out and encouraged the participants to express at any time suggestions of topics of their interest for forthcoming S&C Fora.

On behalf of the Financial Sector Backstopping Team of SDC
Pascale Aubert, Intercooperation

[2] If the savings are sufficient, all loans are given. If not, the group sets the priority; unserved members would have priority next time. The maximal allowed loan amount is defined in the constitution: it is generally fixed at a maximum of three times the savings.