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Interest Rates in Savings Groups: Thrift or Threat?

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SUMMARY

Savings group (SG) models are praised for achieving financial inclusion for the poorest at a very low cost. Promoted by international NGOs, SG models are inspired by indigenous savings and credit associations (ROSCAs). SG models however differ in that they prescribe lending the pooled savings to group members for an interest. The interest rate aims to (1) boost capital accumulation, (2) allocate scarce capital efficiently, and (3) remunerate and incentivize savers. This paper builds on a six-month fieldwork conducted in DR Congo consisting of direct observations of SG meetings and interviews with SG participants and practitioners. We study the gaps between SG practitioners' objectives and SG participants' perceptions and practices related to the interest rate. Our research pays particular attention to the local context and local norms that interfere with SG practitioners' objectives. Our analysis highlights three gaps. First, SG participants turn savings into credit for security purposes rather for rapid capital accumulation. Second, credit allocation decisions are guided by fairness and security concerns rather than efficiency. Third, SG participants often regard the accumulated interest as belonging to the group and to active borrowers rather than to passive savers. Our results invite development actors to pay greater attention to the potential risks of the SG approach for its participants. Despite the common appellation "savings groups", this microfinance innovation builds upon credit and strongly encourages its members to go into debt.

1. Introduction

Access to financial services for all is one of the key targets to "*promote sustained, inclusive and sustainable economic growth and employment*" (United Nations, 2015). To achieve financial inclusion, an increasing number of international NGOs in Africa are embracing the Savings Groups (SGs) approach, also called a "*small wonder*" in the field of microfinance (The Economist, 2011). The Village Savings and Loan Association (VSLA) initiated by CARE International; Savings and Internal Lending Communities (SILC) by Catholic Relief Services and Savings for Changes (SfC) promoted by Oxfam/Freedom from Hunger are the best-known SG models. A SG typically consists of 15–30 self-selected members whose savings are recurrently pooled and accumulated for the purpose of lending money to its members. SGs are self-managed but facilitated by NGOs. The appeal of the savings groups approach for NGOs lies in its decentralized, self-managed, savings-led approach and its low cost/target beneficiary ratio—no external expense is involved except the training costs (Allen, 2006; Johnson, Mule, Hickson, & Mwangi, 2002). In 2016, the number of SG participants in Africa was estimated to be over nine million people.[1]

SG models are inspired by indigenous savings associations, but in contrast to the widespread rotating savings and credit associations (ROSCAs), accumulated savings here are turned into short-term loans to be repaid with interest (see Section 2 for details). Hence, for the SG participants, who are widely accustomed to the traditional ROSCA institution, a peculiarity of the savings groups approach is its systematic interest mechanism.[2]

Drawing on qualitative research conducted in South Kivu (DR Congo) in 2013 and 2014, this paper studies three interrelated questions. What objectives do SG practitioners pursue when promoting the use of an interest rate in SGs? Are the stated objectives of the interest rate mechanism observed in the field? If not, which local norms and contextual elements explain the deviations from stated objectives, and what are the unintended consequences of these deviations? Our qualitative field enquiry consists of direct observations of SG groups, as well as interviews with SG participants, nonparticipants, and SG practitioners (see Section 3 for details). In line with Morvant-Roux, Guérin, Roesch, and Moisseron (2014, p. 305), we indeed consider that qualitative analysis "*is best suited to disentangle and analyse cognitive and social*

[1] This estimate was retrieved from the SEEP Network, a network of practitioner organizations combating poverty through improving financial inclusion. See http://www.seepnetwork.org/savings-groups-global-outreach-pages-20015.php.

[2] In a few ROSCAs, allocation is determined through a bidding process, which can be assimilated to an interest mechanism (Besley, Coate, & Loury, 1993).

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processes" involved in microfinance programmes and therefore "*is critical to analyse issues that are difficult to summarize with numbers, as is clearly the case for norms, meanings, and social interactions, which pertain to the immediate context in which people live*". Our qualitative research usefully complements quantitative research by revealing the existence of economic, social, moral, and cultural logics that influence SG participants' appropriation and interfere with SG practitioners' expected objectives.

Our analysis of SG practitioners' documents, expounded in Section 4 shows that the interest is seen by SG practitioners as an essential strength of their model that aims to (1) boost the accumulation of capital, (2) allocate scarce capital resources efficiently, and (3) remunerate and incentivize savings. In Section 5, we then demonstrate the existence of three gaps between the expected objectives of interest rates and the observed practices of SG participants in South Kivu. First, SG practitioners expect that turning savings into loans that are paid back with interest will boost group capital accumulation. Our results, however, show that SG participants turn accumulated savings into credit for security reasons rather than to seek rapid capital growth. Second, we find that credit allocation decisions are not driven by expected credit performance but rather by concerns of fairness and credit risk diversification. This implies that credit amounts tend to be disconnected with credit performance and borrower repayment capacity. Third, we show that, while SG practitioners consider that interest should remunerate savers, SG participants consider that accumulated interest belongs to the group and should primarily serve the collective interest. Gaining interest just from saving is perceived as an unfair transfer from "active" borrowing members to "passive" savers. Such perceptions, in turn, encourage the emergence of coercive pressures to take credit so as to ensure that all members actively contribute to the collective surplus. These three gaps lead to unintended impacts, such as participants' exposure to increased indebtedness, risks of loss of savings and increased costs for participants.

Our research contributes to the growing body of the literature in microfinance that stresses the importance of taking into account the impact of social, economic and cultural specific contexts on the (mis)use and (mis)appropriation of microfinance services (Guérin, Morvant-Roux, & Servet, 2011; Guérin, Morvant-Roux, & Villarreal, 2013; Johnson, 2004; Lont & Hospes, 2005; Shipton, 2010). For example, Rahman (1999) showed that women's positional vulnerability in a patriarchal society explains how female microcredit borrowers are pressured to achieve high repayment rates in Bangladesh. Morvant-Roux *et al.* (2014) found that debt-related norms and local perceptions of sanctions in the case of default induce a low microcredit uptake in Morocco. Expanding on this literature, our research highlights the recurrent gaps between, on the one hand, the three objectives of the interest rate, as stated by SG practitioners, and on the other hand, SG members' own experiences, perceptions, and practices related to this mechanism. We explain the observed deviations in light of the economic, social and cultural specificities of the context of South Kivu.

Our research also contributes to the burgeoning literature on SGs, which is mostly limited to a recent wave of randomized controlled trials (RCTs) on particular SG programs. A review of seven of these RCTs[3] suggests that SG programs increase savings and credit, as well as resilience and food security (Gash & Odell, 2013). However, mixed results are found on asset ownership, business-related spending and profits, health and education spending and school enrollment, while no effect is found on income, consumption, community engagement or individual empowerment. While useful to measure the impact of SGs (or lack thereof), existing RCTs were not guided by prior theory and hence do not explain why and how these impacts are met or not (Deaton, 2010). They consider the SG model as exogenous and fixed and therefore fail to critically examine the constituting elements and the processes of the SG model once it is applied. Our key contribution is to open up the black box of the SG model and to provide insights into one of its key elements: interest.

This paper is organized as follows. Section 2 describes the principles of the SG programs promoted in South Kivu. Section 3 outlines the research methodology used. Section 4 identifies three objectives of the interest rate as stated by SG practitioners. Section 5 presents three gaps between SG practitioners' objectives and SG participants' perceptions and practices. Section 6 describes the unintended consequences. Section 7 provides a conclusion.

2. Savings groups programs in South Kivu

Located in the Democratic Republic of Congo, South Kivu has been the scene of successive conflicts since the 1990s. In this fragile context, the savings groups' approach has gained rapid popularity among international actors operating in the province, especially among international NGOs seeking to move away from humanitarian assistance toward development programs. In addition, poor communication infrastructures and a generalized mistrust of conventional microfinance institutions (MFIs)—some leading MFIs having gone bankrupt over recent years—render the decentralized approach which characterizes savings groups' models particularly attractive. By the end of 2014, nine international NGOs were promoting savings groups[4] in South Kivu.

Different development actors are involved in the promotion of SGs and facilitate the adoption of the model consisting in a set of standardized rules. In what follows, we distinguish four types of actors. (1) SG advocates are the authors of the SG guidelines and the academic scholars promoting the SG approach. (2) SG program managers work for international NGOs and implement SG programs. (3) SG facilitators are hired by NGOs to create and train SGs. (4) SG village agents are paid by the groups to supervise and assist complex operations after the end of NGO assistance. We use the term "SG practitioners" to refer jointly to SG advocates, SG program managers, and SG facilitators.

One SG consists of a group of 15–30 people who agree to meet up and save regularly. Joining the SG is voluntary but governed by the principle of self-selection. Members' contributions are pooled into two distinct funds. The savings and credit fund is the larger fund and pools recoverable savings and turns them into short-term loans for members. The social fund pools regular but unrecoverable contributions to assist members temporarily in need. Each group usually decides in advance the types of emergencies and life-cycle events leading to financial compensation under this social fund (usually granted for weddings, childbirth, hospitalization, and funerals). All financial operations take place during meetings only, in order to allow members to monitor and have control over fund management. To ensure safety, contributions are deposited in a metallic box, which is secured with multiple locks. Keys to the locks are kept by separate group members to avoid boxes being opened outside of the scheduled meetings. SGs are accepted by

[3] The seven RCTs included in this review evaluated the following SGs: (1) CARE USA's Save Up Village Savings and Loan Association (VSLA) program in Malawi; (2) CARE USA's Save Up VSLA program in Uganda; (3) CARE Ghana's ESCAPE VSLA program; (4) DanChurchAid's (DCA) VSLA program in Malawi (see Ksoll, Lilleør, Lønborg, and Rasmussen (2016)); (5) Oxfam America, Freedom from Hunger, and the Strømme Foundation's (OA/FFH) Saving for Change (SfC) program in Mali; (6) Catholic Relief Services' (CRS) Private Service Provider (PSP) program within its Savings and Internal Lending Communities (SILC) programs in Kenya, Tanzania, and Uganda; and (7) the International Rescue Committee's (IRC) New Generation VSLA program in Burundi.

[4] CARE International, Food for the Hungry, International Rescue Committee, Women for Women and ZOA International promote VSLAs. CARITAS and Catholic Relief Services promote SILCs. Louvain Coopération and Solidarité Internationale pour le Développement et l'Investissement promote MUSOs.