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Community-Based Savings Groups: An Alternative Model for Resilience

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ABSTRACT

This study explores the potential of internal and contextual factors that contribute to the formation of village savings and loan associations and provides a testimonial of individuals that benefit from those groups in northern Mozambique, part of the community-based savings groups (CBSG). The CBSG is the improved mechanism of that community initiative aiming to facilitate the expansion of these groups; promote a savings culture through raising awareness around the importance of saving and borrowing practices as well as creating linkages for the groups to undertake other development activities. Therefore, the groups are an integrated initiative that is distinct from but complementary to common microfinance initiatives. The groups not only can enable people to access to financial services but also serves as a space for members to participate in community issues and to discuss challenges in a collective manner. The main findings of the research show a replication effect resulting from the increase of members and new groups contributes to the promotion of effective financial inclusion.

Keywords: Community-based savings groups, Aga Khan, Resilience, Africa, Mozambique, financial capacity, vulnerable people, risk, credit, microfinance

INTRODUCTION

Many policy makers and businesses erroneously believe that rural populations, particularly in Africa, have no margin for savings over consumption needs. This study examines the potential for financial savings in rural Mozambique by investigating a rural household's savings scheme by the Aga Khan Foundation in the province of Cabo Delgado located in Northern Mozambique.

Microsavings as component of microfinance has widely been recognized as a strategy that enables financial inclusion for non-bankable people who do not have access to more formal financial services. However, some concerns have arisen regarding the real outreach of microfinance institutions (MFIs) to the poor whether MFIs are actually playing a decisive role in increasing the poor's access to financial services. There are a number of reasons why poor people continue to find it difficult to access finance, or, banks find it risky to provide such services to the poor.

FIs face a classical principal agent problem in which the 'principal' (the MFI) is unable to obtain accurate information about 'agent' (the poor individual) including their characteristics and life context (Armendáriz & Morduch, 2010a). As a result, inefficiencies arise in their relationship, such as the prevalence of segmented markets and high transaction costs due to the considerable cost of gathering clients' information. On the other hand, many people especially those in remote rural communities do not have easy access to MFIs due to structural problems / or infrastructure limitations such as distance (e.g., poor roads) the level of financial literacy, and the lack of understanding about the products and services that MFIs offer. Given that, the limited access of the poor to financial services remains along with a problem of trust between the two parties - MFIs and clients. This fact leads individuals to look for alternative arrangements within their communities, often with conditions (e.g., more usurious interest rates) that do little to address issues of poverty.

This paper studies a community initiative known as Community Based Savings Groups (CBSGs). These groups are believed to be convenient and safe places to save and to obtain access to credit. Savings groups services are much less expensive and accessible than other approaches, especially, because the group is known by all members and the groups are formed on the basis of already existing community trust networks. Moreover, social development agencies also find these groups attractive strategies to provide financial services as it does not require setting up expensive branches and paying high personnel overheads especially in the remote disadvantaged communities. This can be seen as a cooperative strategy to achieve engagement among community members (Santos & Laureano, 2021b).

The study goes further by exploring the potential of internal and contextual factors that contribute to the formation of SGs. It examines how CBSGs can be leveraged for other development activities, how linkages to other services take place, and associated costs, benefits and risks to group members.

It is the purpose of the study to focus on participants in this scheme in the community-based savings programme (CBSG) of the Aga Khan Foundation in Northern Mozambique.

According to the available report's findings it shows a replication effect resulting from the increase of members and new groups contributing to the promotion of effective financial inclusion. In terms of social development, the groups foster trust among members and enhancement a culture of savings by motivates members to save in a regular basis and improving financial management skills. Eventually, these groups are shown to have a positive impact in household and within communities by promoting social cohesion and undertake development activities. Policymakers and development agencies in Mozambique are seeing CBSG as a low-cost and sustainable strategies/ or fashion for economic development.

LITERATURE REVIEW

Microfinance has widely been recognized as a credible development and financial inclusion strategy for non-bankable people who do not have access to traditional financial services. Microfinance envisions a world in which everyone has access to a range of high quality and affordable financial services offered by a range of retail providers to finance income-producing activities, help individuals and households build their assets base, stabilize consumption and protect against risk. Microfinance institutions (MFIs) are the financial intermediaries that meet the needs of those who are usually unable to access the formal financial sector (Khawari, 2004). They provide financial services such as microcredit, insurance, savings, as well as deposit services (Addae-Korankye, 2014).

The industry of microfinance has grown in terms of the numbers of institutions involved and products available. This results in a fair amount of research that has assessed the success of MFIs (Khandker, 2003; Nagarajan & Meyer, 2005; Vanroose, 2007, Cortijo, M. J. A., & Kabeer, N. 2005) and the impact of microfinance on households life (Ledgerwood et al., 2013). In recent years, the pressures of commercialization have raised concerns with regard to high interest rates and the exclusion of individuals, particularly in rural remote areas. MFIs seems to be more successful in economically dynamic urban areas where business opportunities flourish, income streams are regular, and diverse; and the cost of reaching clients is low (Demirgüç-Kunt & Klapper, 2012; VSL Associates, 2007). This fact, and the challenge of balancing market attractiveness on the part of the MFI versus the needs of the most excluded market segments, remains one of the major challenges in the quest for sustainable financial development (Bateman, 2010; Berger et al., 1997; Cameron & Ananga, 2015; Hulme, 2000; Navajas et al., 2000; Zeller, 2006).

Carbó et al. (2005) highlight that financial exclusion in developing countries is linked to poverty levels and the absence of capital resources. This is in addition to the inherent risk MFIs are exposed which includes: type of business that clients are involved in but which lack reliable income streams, client characteristics (e.g. individuals whose incomes are typically geared toward current and future consumption) (Banerjee & Duflo, 2007) and operational risk (i.e. remote and underdeveloped infrastructures areas), institutions are subjected to high asymmetric information costs (Armendariz & Morduch, 2005; Giné et al., 2010; Mersland & Strøm, 2007).

Information asymmetry poses significant challenges in terms of profitability and sustainability of MFIs because it leads to high transaction costs associated with gathering and evaluating information for institutions to extend and monitor financial services (Armendáriz & Morduch, 2010b). Baklouti and Bouri (2013) note that the exclusion of the poor from the formal financial system "can be explained by the high level of asymmetric information such as adverse selection and moral hazard, which rise problems of screening, monitoring and enforcement. For example, improper appraisal (i.e. adverse selection) by MFIs is one of the leading causes of loan default (Ahmad, 1999; Berger & DeYoung, 1997). Bigambah (1997) cited by Addae-Korankye (2014) notes that loan appraisal has been identified as the main cause for loan defaults in Uganda.

According to Morduch, 1999; Armendariz and Morduch, 2000 a technique that helps to screen out undisciplined borrower at an early stage is the regular repayment schedule, particularly institutions modeled after Grameen Bank[1].

The absence of registered collateral is another problem for MFIs. Scholars (Armendáriz & Morduch, 2010b; Machauer & Weber, 1998; Warue, 2012) acknowledge that collateral is commonly used as a mechanism for reducing both the screening and the enforcement problems that regular financial institutions operating in developing countries face.[2] In microfinance however, clients often have insufficient collateral to cover the risk of the loan. As a result, riskier customers are charged high interest rates (risk-premium), which raises questions about whether microfinance has poverty alleviation effects in the first place (Santos & Laureano, 2021a). The problem would further be compounded in environments where there is a weak enforcement of contracts and a weak judicial system.

From a demand side perspective, besides the difficulties in accessing the financial system – both in terms of physical access as well as poor people's lack of knowledge in understanding financial products and services, there is also the considerable issue of financial literacy and the inability of many 'unbanked' people to effectively make and apply decisions around utilizing money (Ledgerwood et al., 2013). Klapper et al. (2012) have found that financial literacy is negatively related to the use of informal sources of borrowing and is an impediment for financial inclusion and a reason for financial exclusion (Carbó et al., 2005a). Sebstad and Cohen's (2003) study make a case for financial literacy for the poor and argues in favour of supporting financial literacy programs that lead to a *win-win* situation where poor people benefit from better understanding and awareness about financial products and services and, once they acquire that knowledge, providers will benefit from a larger market of clients.

In recent years, there has been a gradual reassessment of what microfinance is and whom it should serve (Ledgerwood et al., 2013). Some authors (Ledgerwood et al., 2013; Rutherford & Arora, 2009) believe that to continue delivering on its original promise, microfinance must focus on the needs of the poor and understand their ways of managing money – a client centered approach. Rutherford (2009) studied 250 poor families in Bangladesh, India and South Africa and found that the poor find many ways to access financial intermediation. Ledgerwood et al. (2013) confirmed that the poor rely on a set of informal mechanisms to manage their finances. The authors demonstrate a few examples of informal strategies used by the poor: the purchase of livestock as a form of savings, participation in community-based mechanisms such as a savings clubs, as well as use of moneylenders and pawnbrokers to face urgent liquidity needs or to turn small savings into large lump sums.

Given the exclusion to the formal or semi-formal sector providers (i.e. access to credit or insurance) poor people are forced to save in order to cope with unexpected emergencies such as

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[1] Grameen requires that borrower during the initial years of a given loan pay a certain percentage on a sliding scale into an emergency fund. This emergency fund is used as some form of insurance against loan default, death or disability (Morduch, 1999).

[2] Baklouti and Bouri (2013) refer to collateral as credit enhancement or credit transfer mechanism by providing a form of compensation in case of either involuntary or strategic default.

bad crop or illness, or to manage future large expenditures (e.g. house construction)[3]. Banerjee and Duflo (2012) make note of the importance of savings by providing a few real examples why the poor save even in small amounts or "*brick by brick"*. Rutherford (2001) examines, in great detail, how the poor manage their finances and in particular their motives for saving. Several other studies corroborates that author insight (Adjei et al., 2009; Lønborg & Rasmussen, 2014; van Rooyen et al., 2012) in terms of shifting microfinance more towards savings and less oriented to credit. Based on these principles, development organizations such as SafeSave[4] implement their projects by serving people based on their money-management resources and help them manage their household cash-flows.

One of the oldest and most innovative ways which people handle their money is through savings "clubs" in which individual community members come together in self-selected groups to promote a local-level financial savings forum. According to Global Financial Inclusion (Global Findex) database 2012 reports 48 percent of those who have reported any savings in the past 12 months used "community-based savings methods"; of these, 34 percent reported having saved using only community savings club. Those groups also give loans to their members out of the accumulated savings of the group. Several research have been undertaken around the topic of self-help groups (SHGs), particularly popular in India, to rotating savings and credit associations (ROSCAS) in Africa (Aliber, 2001; Gugerty, 2007). These associations essentially involve "a group of people who know and trust each other agreeing to contribute an amount at regular intervals to a fund". This fund is given in its entirety to one or more members of the group and often interest free. The order of rotation is determined in different ways". The group enables members to build higher sums of money than by saving alone (Gugerty, 2007). Furthermore, that savings are easily accessible (i.e., physically close), convenient and flexible to contract (Ledgerwood et al., 2013).

Though, microfinance providers and international and local NGOs have been able to overcome the challenges of asymmetric information and lack of collateral by exploring and improving these traditional groups through the adoption of group lending methods (Cameron & Ananga, 2015; Saloner, 2007). They facilitate the creation of those groups through mobilization of individuals, train members and assist them in their operations. This paper focuses on one specific model of microfinance along the lines of the village savings and loans association (VSLA) model introduced by CARE. The groups are formed through a process of peer selection which decreases the risk of adverse selection. Nevertheless, evidence in Uganda suggest that VSLAs limit the access to group to individuals with lower level of education and generally lower socio-economic status (Lowicki-Zucca et al., 2014). Individual loans are granted from their pooled (or accumulated) savings and the group monitors and ensures that each individual performs. Moral hazard is thereby addressed. Facilitators are therefore trainers rather than service providers (Ledgerwood et al., 2013).

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[3] Ledgerwood et al. (2013) recognize the financial needs of the poor in three broader domains. One is the daily needs related to consumption. The other is related to emergencies or crises such as floods. The last is to finance large life-cycle events, take advantage of an opportunity and to build up assets.

[4] One of the world's biggest and best MFIs that use the "Poor and Their Money" principles. It was founded by Rutherford in 1996 in Dhaka (Bangladesh).

These groups also have proven to serve as community platform from which individuals become active in village affairs while enhancing mutual trust (Sinha et al., 2010). Cameron and Ananga (2015) show that savings group have positive impact on educational expenditure in some countries. In a similar study conducted in Ksoll et al. (2016) found that VSLAs programme has a positive impact on household well-being (i.e., the number of meals consumed per day, total household consumption and number of room in the dwelling) thought the agriculture investment.

MATERIAL AND METHODS

In this chapter, we describe an innovative microfinance intervention designed to help community development practitioners work more effectively with financing programs. Documental and observation techniques were applied to describe a community-based savings group practices, namely all phases of the process: the program planning, monitoring, and evaluation process.

For better understanding of the context challenges and resources, an introductory note is presented regarding Cabo Delgado city, where the program was experienced. Relevant reports from financial institutions were analysed and cited for providing a picture of financial and economic constraints faced by people living there, who apply for microfinance instruments.

CASE STUDY

Local context

The province of Cabo Delgado is located in Northern Mozambique, far from country's political and economic power base in Maputo. The region has suffered from a legacy of underinvestment, government neglect, and poor access to services. On a wide range of indicators, Cabo Delgado has traditionally scored worse than the national average. While 54% of Mozambique's population lives below the national poverty line in 2010 according to the National Statistics Institute, this figure was 63% for Cabo Delgado in 2013. In terms adult literacy the rates among those aged 15 years and older are low with literacy rates abysmally low among rural women, with only about a fifth being able to read and write. While agriculture remains the main source of rural livelihoods, fewer people are engaging in farming than in the past. This is especially true of youths, who increasingly want to earn income through business. It is formal employment that many people looked for, but secure salaried jobs are seen as rare and are mainly the preserve of urban men.

Reinforcing this state of underdevelopment, Mozambique has a very low level of access to financial services, particularly in rural areas. The 2009 Finscope Study (de Vletter et al., 2009) showed that only 22.2% of adults have access to any form of financial services (formal or informal). This has been confirmed by studies such as (Larson et al., 1994) and (Chidzero et al., 1998). Commercial and State banks most of which were established after 1996 are unable to provide financial services to micro, small and medium scale enterprises especially rural farming households. The province of Cabo Delgado has the second lowest level of financial service penetration in the country, but it still has a wide range of financial services offered by a heterogeneous variety of providers. The failure of banks to manage credit and saving lines for small savers and borrowers has encouraged donor organizations to consider using non-government

organizations (NGOs) to reach target groups including small agricultural producers, micro and small entrepreneurs and rural traders. Banks operate primarily as deposit institutions for a few, large depositors and borrowers in urban areas and as providers of deposit services for the government In a bid to create access, donor organizations have resorted to the use of NGOs to reach those who are credit constrained. (). Although private sector credit from the country's banking system showed a huge increase, from 15 % in 2000 to 23% in 2012, a preponderance of this is wholesale credit effectively reducing the access of poor rural dwellers to credit.

The existent traditional association schemes are: *Xitiques*[5], which are the most important and compulsory savings contracts among their members; funeral associations[6]; a group of family members sharing an account (*conta da familia*). In general, these informal groups do not have any linkage to the formal banking system (*e.g.* a bank account) and are used mainly for savings.

The most common practice of households is to keep savings at home. Banks are also used as a savings location for urban men while the traditional savings group (*Xitique*) remained important savings locations for women. In fact, while rural women continued to lag behind in terms of their possession of savings, they are very much at the forefront of savings groups, whether they are *Xitique* or savings group.

Regarding credit, family and friends remained the main source of funds, followed by informal schemes with commercial banks providing credit to only a small percentage of adults. Though, there have been grown in importance of *Xitique* among rural women with debts.

However, there is a perceived level of default risk in Cabo Delgado which limits the provision of credit. The poor repayment mentality is partially explained by the poor local management and supervision from loan providers and donor behavior. As an example, the Fund for District Development (FDD) provided by Government as part of its poverty reduction strategy to the rural poor, has presented problems since loans were not expected to be repaid[7]. Once individuals had access to loans that they were not expected to repay, it became increasingly difficult for professional loan providers to enforce loan contracts, thus reducing their incentive to provide finance. Other bad credit experiences relating to the First MicroBank (FMB), previously the province's largest formal microfinance provider had also contributed to the formation of negative attitudes towards credit.

To address this problem, in late 2010, the Aga Khan Foundation Mozambique (AKFM's) initiated Community-Based Savings Group (CBSG) programme to promote community managed financial services (promote basic savings and credit facilities) in the rural communities. The programme is

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[5] *Xitiques* are similar to Roscas in Kenya where members "agree to a schedule of regular payments in return of lump-sum payment at a future date" (Gugerty, 2007). They use to have fewer procedures and are simpler than ASCAs. The main difference between the two is that one accumulates funds while the other funds rotate immediately after formation of funds. Further difference are provided in Bouman (1995, pg. 377) study.

[6] This is a type of informal insurance that covers the members and their families.

[7] A statement "off the record" made by the Minister of Planning and Development in the Plenary Session on the FDD (then known as OIIL), of the National Meeting on Rural Development (Tete, 27 August 2009) to all participants - including Administrators and others responsible for the administration of the FDD.

part of Coastal Rural Support Programme (CRSP) which is a multi-year and multi-input area development (MIAD) programme[8] that aim to contribute for the development of the region.

In essence, CBSG programme applies the Village Savings and Loans Association (VSLA) methodology for which the generic term used is usually ASCAs (Accumulative Savings and Loans Associations). The main objective is to provide a mean of small amounts of local capital for life-cycle events – which may or not include income generation – to rural poor. The principle of these VSLA systems is that members voluntarily form into self-selected groups which usually comprises between 15-25 members and save money. The savings are invested in a loan fund that is managed by the community from which members can borrow and pay back with a service charged.

The CBSG programme was implemented in four phases:

1. preparatory phase where field officers or facilitator met with local leaders, potential members and develop an understanding of the area;
2. the intensive phase when field officer is actively involved in guiding procedures and provided training;
3. the development; and finally
4. the maturity phase when field officer prepared the exit strategy and group is able to run independently.

After a period of four years the programme have contributed to a positive change of the beneficiaries' life.

The innovative program intervention

The microfinance intervention that we study is the community-based savings group which applies the Village Savings and Loans Association (VSLA)[9] methodology and their work complementary to microfinance. They usually serve the very poor people in remote rural areas and their main objective is to provide a mean of small amounts of local capital for life-cycle events – which may or not include income generation.

This is done at a very low risk and negligible cost as the group is known by all members which also create incentives to save.

The principle of these Village Savings and Loans (VSL) system is that members voluntarily form into self-selected groups which usually comprises between 15-25 members and save money. The savings are invested in a loan fund that is managed by the community from which members can borrow and pay back with a service charged.

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[8] It broadly focuses on a set of core themes such as agriculture, market development, civil society, health, education, and a number of cross cutting themes such CBSGs, infrastructure, gender, nutrition, and Early Childhood Development (ECD).

[9] Also know by Accumulative Savings and Credit Associations (ASCAs).

These groups are autonomous and self-managing that means that they are institutional and financially independent from the promoter (AKFM) that assists them to develop a constitution[10]. Figure 1 summarizes some of the practices applied. Besides technical assistance, AKFM provides in the establishment of the group a kit to support operations, that consists of a cash box, three padlocks, two bowls (to collect the savings, fees and social fund), one calculator, two pens, two rubber stamps, individual passbook, three money-bags to keep money[11], a ruler, a pillow and rubber stamp ink pad.

They meet at regular basis: every week during the first cycle in order to complete the training provided by the promoter; in future cycles, groups have meetings every two weeks or once a month. Their structure comprises of a General Assembly (GA) and a Management Committee (MC). The key positions of MC are: a chairperson, record-keeper, box-keeper and two money-counters.

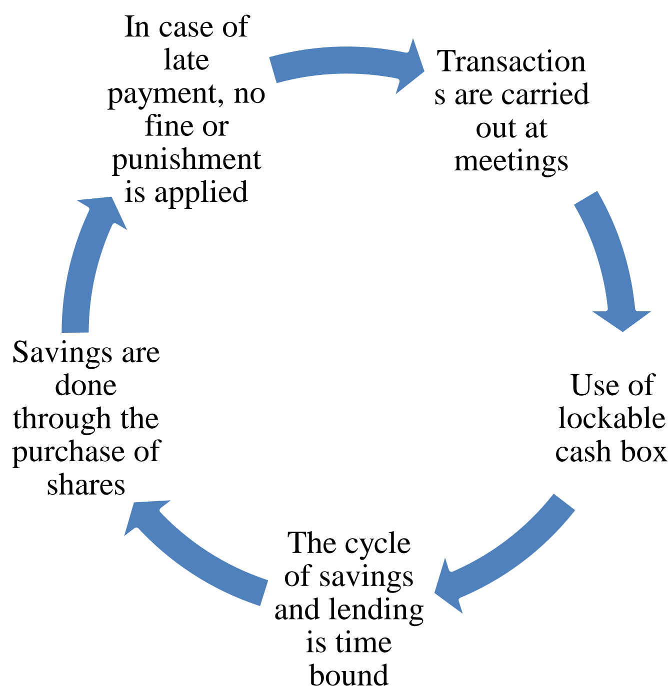

Figure 1. Some practices applied by Community-Based Savings Groups

All transactions, loan disbursements, payments and savings collection, are carried out at meetings in the presence of all members of the group to ensure transparency and accountability. The lockable cash box is used to prevent unauthorized use of money.

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[10] This constitution signed by every member provides a framework for managing the funds, among other relevant matters like settle the length of the operating cycle.

[11] One bag for the social fund, other for the loan fund and the remaining to hold the daily savings.

The cycle of savings and lending is time bound and do not last for more than one year (approx. 9 to 12 months) before the share-out. At the end of an agreed period – the ‘cycle’ – the accumulated savings and service charge earnings are shared out amongst the membership in proportion to the number of shares of each member.

The individual passbook tracks loan liabilities and register savings amount. The savings are done through the purchase of shares in meetings (at least one share per meeting), which constitute the core activity of the CBSG and the key factor for the mutual trust and success. The value of a share varies between groups and is set in the beginning of each cycle and depends on the group members financial capacity and source of income (i.e. fishing groups can set 3 USD per share while farming group set 1 USD per share). The group can allow a member to stop saving (purchase shares) in the case of financial difficulties like income variability or external factors (e.g. floods, illness or death of a family member). However, even if the group suspended savings, loans must continue to be repaid and can continue to be disbursed. This method intends to protect the cohesion of the group, solidarity and self-assistance that provide emergency assistance to members without hindering financial discipline.

All members of the group are entitled to borrow from the loan fund every four weeks and the conditions (i.e. length that is less than six months, instalments and rate of the service charge) are set by the MC. The amount of the loan cannot be more than three times the total value of all the shares he/she has bought in shares. The service charge on loans is applied to the balance of the loan every four-week[12] and must be paid when due regardless of whether or not the member repays loans principal.

In the case of late payment the group members does not fine or ‘punish’ member borrower. This attitude avoids increasing the financial distress but may influence the eligibility of that member for further loans.

In a later stage group members create a social fund through small contribution by each member as a form of self-insurance to cover occasional situation like funeral expenses. The disbursement of this social fund needs to be approved by GA.

In the beginning of a new cycle members can invite more new members to join, agreed on the initial contribution amount to the fund (to start lending) and set the value of the standard share which should be stamped onto passbooks (price).

FUTURE RESEARCH DIRECTIONS

The study of microfinance instruments in other developing countries are necessary to add new practices to the present case study. The lessons learned about the role of community saving groups in successful microfinance programs may be useful for scholars to develop quantitative and longitudinal studies for statistical generalization purposes.

CONCLUSION

[12] This means that after the member pays part of the balance due the remaining balance is treated as a new loan with the service charge percentage applied to the new amount.

The present study addresses the challenge of developing countries' rural communities in accessing to microfinance programs. An extensive literature review on the topic was conducted, providing to scholars a bird-eyes view on main academic contributions.

Based on the examination of the methodology of a CBSG practices of the Aga Khan Foundation in Northern Mozambique, this study provides an in-depth characterization of an innovative practice.

Main contributions entail the planning, monitoring and evaluation practices applied in theses saving groups as good practices for responding to the credit needs of households. These include avoiding punishments behaviors or creating social funds among community.

This study, thus, highlight recommendations within the context of the existing similar social economic environment.

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KEY TERMS AND DEFINITIONS

Microfinance institutions (MFIs): Financial intermediaries that meet the needs of those who are usually unable to access the formal financial sector.

Community Based Savings Groups (CBSGs): These groups are believed to be convenient and safe places to save and to obtain access to credit.