



Multiple Borrowing by MFI Clients

Multiple Borrowing (Overlapping) : The Background

Rapid expansion and diversification of microcredit/microfinance programmes have been accompanied by borrowing of the same individual from multiple microfinance institutions (MFIs). This phenomenon of multiple borrowing is sometimes referred to as overlapping or multiple borrowing. In recent times, the term is used to indicate multiple microfinance membership at the level of individual or household. Any household with more than one membership is termed as '**household overlapping**', and any individual member having membership with more than one institute is defined as '**membership overlapping**'.

The overlapping phenomenon has raised some concerns and controversies. These concerns can be summed up as follows:

1. Aiming to increase business volumes, some MFIs either inadequately check or ignore client borrowing habits. This adversely affects the quality of the loan portfolio as clients put themselves at a higher default risk.
2. In some areas, clients borrow from more than one MFI at a given time. The absorption capability is not assessed; consequently, loans are misdirected.
3. With increasing debts and misdirected funds, clients turn to informal sources (friends, relatives, money lenders etc.) for further credit, further aggravating the debt trap. Several clients, in this situation, have held distress sales of movable assets. In extreme cases, mental depression resulting from the financial pressure causes some to commit suicide. These situations taint the image of microfinance sector.
4. Non-repayments and delayed repayments adversely affect the portfolio at risk of MFI. If the impact moves beyond acceptance levels, lenders will rethink their future investments, making it difficult for MFIs to access credit.

A well-rounded understanding of the situation and coordinated efforts of MFIs can help in taking viable steps to prevent a major crisis for MFIs that may occur due to multiple borrowing. This brief is an attempt to serve such a purpose.

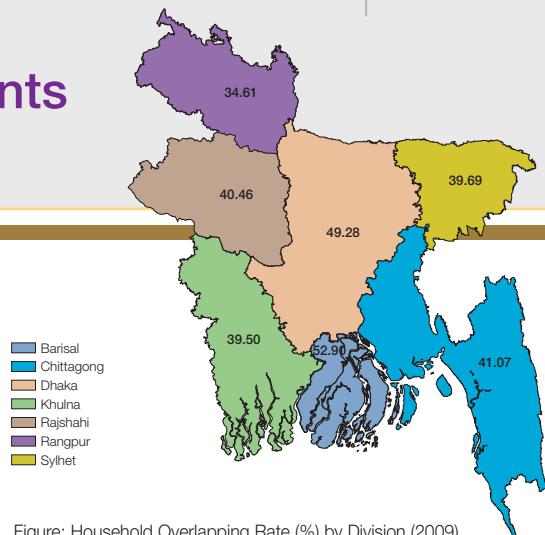


Figure: Household Overlapping Rate (%) by Division (2009)

Multiple Borrowing: Nature and Extent

Different sources seem to indicate that currently the rate would vary between 40-60 percent in Bangladesh.

Household Surveys by InM

Pilot Study in Pathrail Union

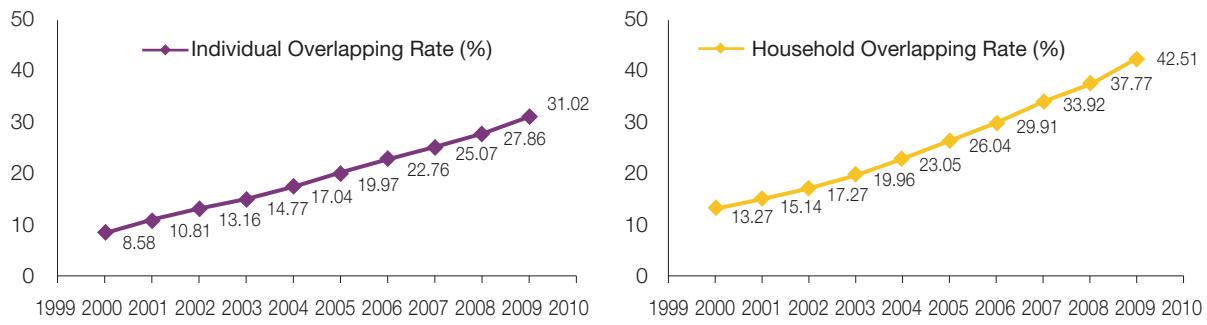
A pilot study was carried out in Pathrail Union where Professor M. Yunus replicated his Grameen Bank model in late seventies. The results of the study show that:

- Around 59 percent of the households had multiple membership (Household Overlapping), of them around 33 percentage point had single overlapping and the rest had more than one overlapping.
- Around 31 percent of the individual members had multiple memberships (membership overlapping).
- Around 40 percent of the borrowers take a second loan within the period of one year.
- Overlapping households remain better off in terms of the positive net worth and positive incremental change in assets and net savings.
- It appears that it is due to demand for larger amount of loans which are used mostly for productive purposes.
- Traditional concerns that overlapping may lead to over indebtedness are probably not fully justified.

National Study

The national survey was conducted over randomly selected 4143 households from 118 villages in 17 upazilas of randomly selected 12 districts of 6 divisions. That survey gives the trend in individual membership by overlapping household memberships over the past ten years.

Trend in Overlapping, 2000-2009 (Percent)



Source: Khalily and Faridi (2011)

Causes of Multiple Borrowing

Major Hypotheses

Clients' Perspective

- The client's business needs exceed the loan offered by a single microfinance provider (to support growth, or a small business)
- Interest rates may vary across the sector, encouraging clients to go to a second microfinance provider
- The client's credit needs are not fulfilled by one MFI's product ranges (some MFIs may only specialised in micro-crop loans, while others may excel in micro-insurance)
- The client may want to use additional microloans for consumption purposes or for an emergency
- In case of default, the client can take out a second loan to repay an earlier loan or simply start over after the first microfinance provider refuses to advance another loan due to a tarnished credit history.

MFIs' Perspective

- MFIs' aggressive growth plans force poaching the existing clients of other MFIs as the members have proved their credit history and they have fair knowledge of joint liability group norms and credit discipline
- Clients do not reveal their borrowings/membership with other providers (and also MFIs do not share the information with other MFIs)
- Loan sizes are based on cycle rather than cash flow
- Different members from the same family or household take loans
- Borrowers avail multiple loans by taking advantage of multiple spellings/names on multiple identity cards
- Front line staff want to reach their monthly targets and thus ignore multiple borrowing

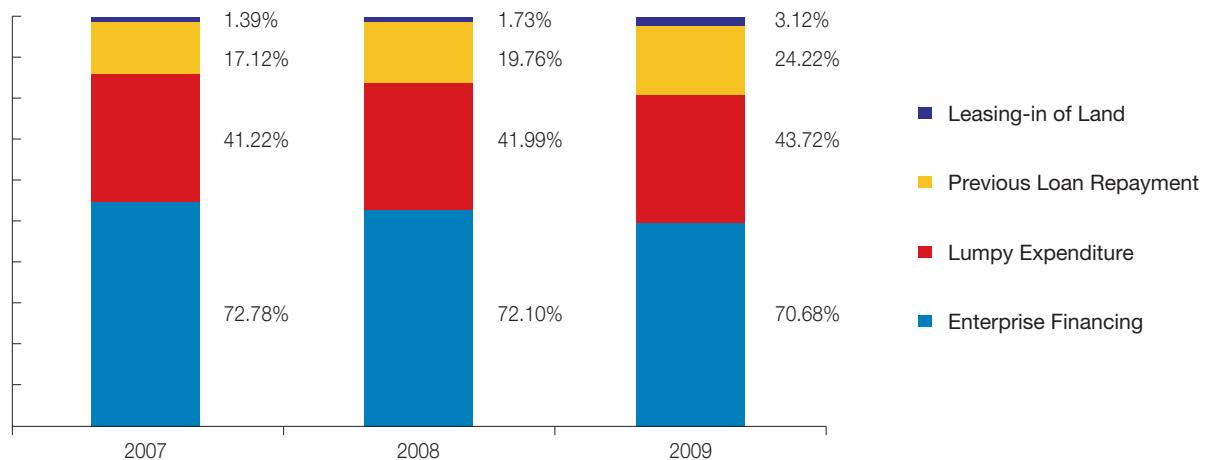
Empirical Findings

The latest research study (Khalily and Faridi, 2011) of Institute of Microfinance (InM) explores possible roles of 4 factors in causing multiple borrowing:

1. Enterprise Financing
2. Lumpy Expenditure
3. Leasing-in of Land
4. Previous Loan Repayment

The study finds that enterprise financing is the dominant head in the microcredit loan, followed by lumpy expenditure. However, household overlapping rate was found comparatively higher for those who used loan for the purposes of lease-in of land and repayment of previous loan. But the percentage of loans used for repayment of loans was quite low. These results are also reported in the following tables.

Figure: Percentage of Borrowing Households by Loan Use Type, 2007-09



Source: Khalily and Faridi (2011)

Note: Sum of column percentages will not be 100 because some households may have used loan for multiple purposes

Table : Household Overlapping Rate by Loan Use Type

Use of Loan Type	Loan used for	Household Overlapping Rate (%)		
		2007	2008	2009
Enterprise Financing	YES	32.49	42.13	48.94
	NO	28.69	33.95	42.31
Lumpy Expenditure	YES	41.40	46.09	53.57
	NO	24.67	35.34	41.88
Leasing-in of Land	YES	60.00	40.43	63.21
	NO	31.05	39.83	46.40
Previous Loan Repayment	YES	58.96	56.80	65.33
	NO	25.77	35.66	41.14

Source: Khalily and Faridi (2011)

Table : Percentage of Loan Used by Major Loan Type by Household Overlapping Status

Use of Loan Type	Overlapping Status	Percentage of Loan Used		
		2007	2008	2009
Enterprise Financing	YES	62.23	62.08	59.11
	NO	71.41	63.42	66.07
Lumpy Expenditure	YES	24.27	22.43	24.20
	NO	21.25	26.10	20.67
Leasing-in of Land	YES	0.91	1.08	2.14
	NO	1.05	2.18	2.16
Previous Loan Repayment	YES	12.59	14.41	14.55
	NO	6.40	8.30	11.10

Source: Khalily and Faridi (2011)

Impact of Multiple Borrowing

Major Hypotheses

For Clients

- On one hand, households may gain from multiple borrowing by using the credit for productive purposes.
- On other hand, households may fall into cycle of debt, leading to rising levels of delinquency and default.

For MFIs

- With increased competition, MFIs are experiencing a reduction in the loan recovery rate and drop-outs.

Empirical Findings

The study (Khalily and Faridi, 2011) reveals the following impacts:

1. There is no evidence of growing indebtedness for the overlapping households. Indebtedness has been defined here in the context of net worth. Average net worth for the non-overlapping households increased steadily from Taka 153000 in 2007 to Taka 196700 in 2009, while it increased from Taka 162000 in 2007 to Taka 2474000 in 2009 for the overlapping households. [All net worth values are expressed in 2009 price].
2. Self-employment days are higher for the overlapping households. Also there is a direct relationship between self-employment person days and intensity of overlapping. The non-overlapping households had an average 168 person days of self-employment as compared to 217 person days for the households with 3 multiple memberships and 237 person days for the households with 5 or more memberships.
3. Overall, there is positive impact of overlapping. It is found that overlapping households are better off in total assets, net worth, savings, consumption, employment days and non-food expenditures, than the non-overlapping households.

Overlapping is not a phenomenon unique to Bangladesh only. The experiences from other countries reveal that multiple borrowing is essentially sign of competition in credit market. Impact of multiple borrowing on loan default is ambiguous and the evidence is mixed. Impact of competition or multiple borrowing on indebtedness is not uniform. Clearly, overlapping itself is not a problem, it is how the borrowers use money. Poor households are vulnerable and whatever gains they derive from microcredit are lost, in many cases, because of high intensity of idiosyncratic and co-variate shocks. This is the reality.

Policy Recommendations

- It is often argued that credit bureau or clearing houses could be set up to avoid or minimise overlapping. While a cost-benefit analysis needs to be done for the clients' activities and monitoring, the findings confirm, at least for the next 10 years, loan officer and peer monitoring are more effective and cheaper than a credit bureau, particularly in rural areas.
- MFI credit policies need to be adjusted in a manner that allows minimum of overlapping. For example, microcredit for agriculture needs to adjust to size and repayment provide in a manner that is suitable for agriculture.
- MRA needs to take some actions to minimise overlapping or direct this to a productive route.
- Information sharing between MFIs would help in minimising the overlapping in lending to microcredit to members of MFIs.