Informal Financial Services Brief

A Deep Dive into Savings Groups and their Services

Funded by

fsdZambia
Expanding Financial Inclusion
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INTRODUCTION

Throughout history, informal financial services have been serving clients' financial needs. Informal financial services capture a range of collective savings, lending, and insurance mechanisms. Forms in Zambia include savings groups (VSLAs\(^1\), SILC\(^2\)), village banks\(^3\), kalobas and chilimbas\(^4\). Although access to formal financial services has been increasing, informal financial services remain relevant as their value to the users is a mix of social and financial elements. An increasing number of Zambians now use both formal and informal financial products\(^5\). In recent years, there have been various efforts to increase demand for and supply of formal services to these informal groups. Despite this, attempts so far have not yielded significant results. However, emerging trends and unforeseen circumstances such as the Covid-19 pandemic\(^6\) have provided a new twist to both formal and informal financial services.

For financial service providers (FSPs), offering the right product to the right market segment is key to the commercial viability of financial products. The right product provides value to its users by meeting their needs, being consistent with their beliefs and values, and fitting in with their habits and behaviours, while also being financially viable for the client and the FSP.

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1. Village Savings and Loan Associations
2. Savings and Internal Lending Communities
3. As defined by FINCA: “groups of low-income entrepreneurs who come together to share and guarantee one another’s loans”
4. ROSCA – Rotating Savings and Credit Associations
The Savings at the Frontier (SatF) programme in partnership with Zambian Financial Sector Deepening Zambia Limited (FSD Zambia) conducted a qualitative study of savings groups (SGs) and their members in the Copperbelt, Luapula and Lusaka provinces of Zambia in 2019. The study aimed to gain new insights regarding SG members in terms of how they perceive their groups and formal FSPs and what drives their decisions to use one service rather than another.

The purpose of this paper is to help formal FSPs (banks, microfinance institutions, mobile money providers, fintechs and insurance companies) and other stakeholders in Zambia to better understand what constitutes the right products for SGs and their members.

A. Characteristics of SGs

In understanding the scope and characteristics of SGs and their members, selected key findings showed:

1. **SG members are intelligent consumers who mix and match products** from different providers to meet their requirements. These members are always looking for the best solutions, and are quite willing to use a variety of products and services of SGs and FSPs in whatever proportion they think best meets their needs. These client demands include long and short term savings and loans, commitment savings devices, overdraft facilities, mobile banking, periodic share-outs, social insurance, transfers, and funding of group income-generating activities and businesses. Products, services, and terms and conditions of products that SGs offer are chosen through a collaborative process, sometimes chaotic and sometimes orderly and democratic.

2. **SGs offer a strong value proposition.** SGs provide commitment savings with an annual payback/share-out to the saver, quick access to loans, flexibility in repayment, transparency, social support, a feeling of community, networking opportunities, esteem within the community, and – most importantly – physical proximity. SGs allow members to save and borrow against the backdrop of previous achievements and successes. At their best, SGs create a virtuous circle in which ethical behaviour in using financial services serves not only the member but also the group, which in turn encourages members to be more committed.

3. While members appreciate their SGs, it is rare for SGs to meet every need of all members, and they do not find that SGs are perfect. One of the greatest unmet needs of many groups is better funds security. Other issues include bookkeeping; limits on borrowing and saving; and delays in annual share-outs due to loan arrears from some members, which frustrates members who count on receiving their pay-outs in a timely fashion.

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7. A partnership between Mastercard Foundation and Oxford Policy Management
8. The study was funded by SaTF and FSD Zambia and conducted by Oxford Policy Management in collaboration with Paul Rippey and IPSOS Zambia.
9. SGs collect money from members, usually variable amounts, to capitalise a group loan fund from which members may borrow.
11. Provide a means of saving for a particular goal
4. Perceptions and reputation matter significantly. Many of the SG members have high regard for mobile money and banking agents because of their proximity, transparency, and the fact that they are local people who understand them and speak their language. However, SG members also have unfavourable attitudes about FSPs, especially concerning transparency, social distance, the ways fees are charged, and paperwork requirements.

B. SG Membership

SG members are typically women. Similar to global trends, evidence from studies conducted by FSD Zambia reveal that SGs have more than 80% female participation. These members are primarily within the economically active bracket and aged between 21 and 60 years. SG membership varies enormously in wealth, including every stage from rural poor to urban professionals. They join SGs to fulfill hugely different financial needs, from urgent immediate needs to investing in life goals such as businesses and housing. Regardless of the financial requirements and use, SG members almost universally find social benefits too, including a sense of belonging and heightened esteem in the community. Some members come to groups only to save, while others take a series of loans at every opportunity. Some are net contributors to the social fund as a form of self-insurance, while others find that the fund helps alleviate life's hardships.

C. SG Member Needs

SGs are designed by their members to meet needs within their general membership. Therefore it is not surprising that members are generally happy with their groups. SG members look for financial services that will meet their needs, and they act in their perceived self-interest. While they tend to have positive feelings towards their group, they are always in the market. If alternatives meet their needs better and are affordable, the SG clients will use the other services offered.

SG members do not form a homogenous group. Their needs vary widely (across groups and over time). Maslow's hierarchy helps categorise, examine, and understand member needs. Most importantly, it can help FSPs understand what the SGs know instinctively about member needs: the right product depends on the person's immediate needs. While there is a market for FSPs to aid members in meeting their life-goals at the highest level, FSPs need to understand that SG members place a priority on survival first, and security second.

Further, SG members benchmark their expectations of financial services available from FSPs based on their experience with their SGs.

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14. Maslow's hierarchy looks at human needs from physiological needs, safety and security, love and belonging, self-esteem, to self-actualization
D. Member Experiences of SGs

Findings from the SATF study and other FSD Zambia studies highlight member experiences of SGs as outlined below:

1. SGs offer their members outstanding proximity, administrative simplicity, rapid responsiveness, and flexibility.
2. Members are not particularly concerned about interest rates, which they may not fully understand, and they acknowledge that banks need to make money. However, they care about the appearance of fairness, and are particularly sensitive about seeing their balance decrease when they have not withdrawn funds.
3. SG members are sensitive to the people they are dealing with and prefer people who are “just like us” in language, class, and culture. Both mobile money and banking agents, located nearby, are strongly appreciated because of these characteristics. Mobile money has an excellent reputation for pricing transparency.
4. The success of SGs has been accompanied by growth in the amount of cash groups manage. Thus security of funds has become a huge issue, one that few SGs have entirely solved. Many respondents look to FSPs to help but may be daunted by distance or other factors. Mobile money agents were cited as a good option for them and will probably continue to play an increasing role, although they are affected by liquidity issues.
5. While many SG members would like to use the additional services of FSPs, issues around travel, additional and complex paperwork, time and cost stand in the way.

E. Formal Financial Services as Seen by SG Members

SG member perceptions drive their decision making about formal financial institutions. At the same time, some of these observations on formal financial services are inaccurate or are driven by outdated information. SG members are benchmarked by their experience with their groups, which for many people are the only financial service mechanisms they have ever experienced. FinScope and other FSD Zambia studies have revealed that SGs are an entry point for financial services for many Zambians especially women.

It is noteworthy that the negative remarks about interest rates at banks came from people who paid as much as ten percent per month to borrow in their SGs. The issue is not the absolute cost of borrowing, so much as the frequency of charges and the relative lack of transparency in communicating them. In contrast with SGs, the fact that all the money is paid into the bank does not give the members any sense of motivation to pay the high cost. While none of the respondents mentioned loan size as a factor in the perceived fairness of interest rates, the interest rate on the small

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18. Ibid
loans within SGs is perceived to be typically higher than the interest rate applied to somewhat larger bank loans.

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\text{SG members place as high a value on where they will “feel at home” as they do on product-specific factors such as interest rates and fees. Distance is not only measured in kilometres, but in language, hospitality, attitude – all the non-financial issues that help people feel connected to an organisation.}
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Members of one group reported an extreme case in which, due to lack of reliability, they needed to ask someone in Lusaka to withdraw money for them from the bank and send it through mobile channels. Members reported how it is much easier to find a mobile money agent, although liquidity challenges remain.

**SG Member Experiences of FSPs**

A collaborative study\(^\text{19}\) conducted by FSD Zambia and FSD Uganda on linked SGs in Uganda presented member experiences with formal financial services. It revealed that SGs linked to formal financial institutions realised significant benefits. These included **safe storage of large sums of money, increased sources of borrowing to meet individual financial demands, financial education/capacity building, better remittance services, and reduced costs of transactions.**

However, the story is far from perfect. Although formal financial services are an important approach to broader financial inclusion, they are still riddled with transactional challenges which inhibit them from providing services to SG members at scale. Growing FSP services requires additional investments and interventions that address transactional constraints. SGs and their members still experienced challenges with regards to the following:

- The time it takes to access savings and loans
- Distance to banks
- Having to carry large sums of money when depositing and after making withdrawals
- Not receiving interest on savings
- Service fee and minimum balance requirements on the accounts
- Long banking queues
- Network problems (at ATMs and with mobile banking)
- Language barriers and low levels of financial literacy amongst group members

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Conclusion

Formal financial inclusion, especially for very poor rural communities, remains a challenge. However, the existence of a growing informal financial sector provides a tremendous opportunity for formal financial service providers to develop products that can be delivered and serviced profitably. Product features, security, customer engagement and proximity are key factors that can be considered by FSPs to accommodate more informal finance users. Barriers to formal financial service linkage are to do with perception first, then experience. Therefore, change of perception may be the first step needed to get SG members to a level where they fully understand product and service offerings of FSPs and feel comfortable to try them. FSPs also need to deepen their understanding of the varying needs of SGs and their members, using client-centric methods to customise their products to suit these clients. FSPs (both mobile money operators and banks) can leverage on opportunities for agent distribution networks, as such appears to be an initial formal financial service that SG members and others can accommodate.