

BRIEF 6

Savings for Risk Mitigation and Crisis Recovery

Emerging Lessons:

- Many MFIs promote savings through mandatory and sometimes voluntary schemes, to help the poor accumulate cash resources and help reduce vulnerability to crises;
- Not all MFI clients seek to withdraw their savings in the immediate aftermath of a disaster.
- The poor are more likely to withdraw savings to meet personal emergencies such as sickness, accidents and death than to cope with major disasters that affect many people.
- In areas frequently affected by disasters, personal savings are generally used for disaster preparation and during late recovery stages, rather than for coping during the relief stage;
- Demand exists for deposit services even during relief and early recovery stages;
- Not all MFIs can offer flexible 'on-demand' savings products.

Cash savings help the poor prepare for, cope with, and recover from crises including natural disasters. Cash deposits made in financial institutions may reduce a person's vulnerability to disaster-related crises in a number of ways:

Physical assets converted to safer, liquid savings

Exposure to losses can be reduced if a person can maintain his/her excess income or precautionary savings at a financial institution rather than in physical assets that may, for example, be indivisible, not easily liquidated, or stolen.

Savings used to invest in risk-reducing measures

An MFI client may be able to accumulate sufficient savings to invest in risk-reducing measures such as water-harvesting devices in drought-prone areas, purchasing a boat in flood-prone areas, improving housing structures in earthquake and typhoon-prone areas, and others.

Savings used to replace lost or damaged assets

Savings can play a substantial role immediately following a natural disaster, allowing people to replace income-generating assets. Savings can also serve as a deposit towards securing finance to replace larger assets in the post-disaster reconstruction phase.

In India, household savings are found to be significantly larger in places frequently affected by natural disasters by comparison with other areas. The poor consider precautionary savings as insurance to cope with crises (Nagarajan and Brown, 2000).

WHAT SAVINGS PRODUCTS ARE USEFUL FOR RISK MITIGATION?

MFIs may offer various types of savings mechanisms and products. Savings may be mandatory or voluntary, and may be held as demand deposits, contractual deposits for special purposes such as funerals, fixed-term



deposits, illiquid group deposits that allow access to emergency loans, and group emergency funds that help cover delinquent loans.

In general, MFIs that collect mandatory deposits only allow for a small and fixed amount of cash to be deposited. These funds are usually only available for withdrawal when the member leaves the program. Even if these funds are available following a natural disaster, this type of savings product is not observed to help cope with crises, since the amount accumulated in members' accounts is usually very small.

Studies now show that appropriate savings strategies for disaster management for the poor comprise both highly liquid accounts that allow frequent, small deposits and withdrawals and time-bound accounts that allow people to save for specific objectives.

Savings have proven more effective in disaster management when used in combination with other financial products such as loans, insurance, leasing, remittances/money transfers and pawn services (Rutherford 2000).

CAN ALL MFIs PROVIDE DEPOSIT SERVICES?

While mandatory deposits are relatively easy to manage, more flexible savings products involve significant management and cost implications—and not many MFIs have the requisite capacity. Also, most countries only allow licensed banks (including MFIs that have obtained a license) to mobilise voluntary deposits from the public.

The criteria determining that an MFI qualifies for provision of deposit services include the following (CGAP 2005):

- appropriate governance, ownership and institutional structure;
- strong management of credit, liquidity and interest rate risks;
- sound internal controls;
- financial capacity to withstand external shocks (inflation and devaluation);
- adequate capital;
- regulatory framework and supervision focused on depositor safety;
- commitment to expanding access.

CAN MFI CLIENTS SAVE EVEN AFTER A MAJOR DISASTER?

Yes! The poor can save soon after a disaster both in financial and non-financial forms. Whether or not savings are deposited with MFIs depends on clients' trust of the MFI, transaction costs and accessibility.

MFIs operating in Tsunami-affected areas of Sri Lanka reported larger total savings balances in March 2005 compared with March 2004. They also recorded larger total savings balances in December 2005 compared with December 2004 (field research by FDC team, March 2006). An assessment in Batticaloa district showed that around 35% of cash grants and cash-for-work (CFW) payments received by beneficiaries were saved in MFIs (Aheeyar, 2006).



The above trends can be explained by the availability of cash grants, CFW, and subsidised loans in the aftermath of the Tsunami. Most MFIs experienced significant growth in their membership base, and some MFIs also increased the minimum savings required for membership. As a result, many MFIs in Sri Lanka experienced an increase in total savings in 2005 despite the Tsunami.

Similar trends were also observed in Aceh, Indonesia. Mercy Corps implemented a CFW program in Tsunami-affected areas that benefited nearly 18,000 participants and disbursed over US\$4.5 million in direct payments. The program began on 7 January 2005 and was gradually phased out by 31 July 2005 in favour of other programs aimed at building livelihoods and more sustainable sources of income. Exit surveys of CFW participants showed that 29% of households had deposited cash savings and 26% of households had purchased gold in lieu of cash savings.

HOW CAN MFIs CAPTURE SAVINGS AFTER A DISASTER?

There are opportunities for MFIs to capture savings by partnering with relief agencies and offering low-cost savings products. Numerous relief agencies in Sri Lanka and India, and some in Aceh, used banks and MFIs to pay their CFW and cash-grant beneficiaries (see Brief 4: Microfinance and Cash-for-Work in Livelihood Restoration following a Natural Disaster).

WHAT ARE THE ISSUES FOR MFIs TO CONSIDER FOR PARTNERSHIPS WITH RELIEF AGENCIES?

MFIs need to negotiate the following with relief agencies to provide payment services efficiently:

- commission rate for payment services;
- security arrangement for cash delivery;
- time schedule of cash payments;
- mechanisms for cash withdrawal;
- service charges for withdrawals;
- minimum savings balance for account holders.

This brief was written in May 2006 by Dr. Geetha Nagarajan, Research Coordinator, Capacity-Building for Microfinance Institutions for Post Tsunami Reconstruction, Foundation for Development Cooperation, Brisbane, Australia. The author acknowledges all the sources in Sri Lanka, Indonesia and India that contributed to this brief.

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SUGGESTED WEBSITES

- Savings Resource Center at Microfinance Gateway: www.microfinancegateway.com/resource_centers/savings?PHPSESSID=76c188bc1d47733cb281a52d0797604a
- Product Development for Savings: www.microsave-africa.com

