Kyrgyz Republic: Borrowing by Individuals

A Review of the Attitudes and Capacity for Indebtedness

Summary Issues and Observations

In partnership with:

Schweizerische Eidgenossenschaft
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INTRODUCTION

A survey was undertaken in September / October 2013 to gain insights into the experience of borrowing by individuals in Kyrgyzstan. The principal dimensions were to assess:

- The broad demographic profile of individual borrowers;
- The major characteristics of their financial and budgetary position; and,
- Their attitudes towards borrowing and the lending institutions.

A core objective of the survey was to gain greater insights into the extent, and impact, of over-indebtedness amongst borrowers. The structure of the survey was designed towards this goal. The objective of the survey is not, therefore, primarily to review the commercial and social performances of the lending industry, but only to the extent that such issues impact upon the budget and lifestyle of the individual borrower.

4,000 individuals responded to the survey and spanned borrowers from microfinance and bank institutions, together with some non-borrowers. The methodology of the survey is outlined in Attachment 1, and the survey questionnaire is shown in Attachment 3.

The major focus of the survey is to relate 'over-indebtedness' to the affordability of debt and the adequacy of income to meet expenditure needs. On this basis, lending is undertaken against the capacity of the borrower to meet loan repayments in a timely manner – and not against any 'forced sale' realisation of assets or payments by a guarantor. A key dimension is to gain better insights of the interaction between the quantitative dimensions of the borrowers' financial position and qualitative dimensions of the feelings of the borrower in relation to financial confidence, risk vulnerability and the impact of debt on their lifestyles.

It is understood that this type and range of survey has not been undertaken previously in Kyrgyzstan. The survey provides some dimensions of the financial, demographic and social profiles of borrowers. This will enable stakeholders to relate the survey findings to their respective interests or to the particular portfolio structure of individual lending institutions.

Similar studies have been undertaken in a range of other countries, most recently in Bosnia and Herzegovina. Whilst it may be inappropriate to undertake detailed comparisons between countries, such research does provide a useful additional perspective by which to consider the findings in Kyrgyzstan.

This paper provides four sections:

1. **'Headlines'** of the principal findings from the survey (page 3);
2. **'Summary Observations'** to provide some dimensions of the principal findings (pages 4 – 7);
3. **'Issues for Consideration'** to identify factors which impact upon over-indebtedness (pages 8 – 10);
4. **'Questions and Answers'** to provide some insights and survey response data into a range of issues raised by the survey responses (pages 11 – 80);

Attachment 1. Survey methodology (pages 81 – 82);
Attachment 2. Risk categorisation methodology (pages 83 – 84);
Attachment 3. Survey questionnaire (pages 85 – 87).

It is hoped that this research will contribute additional perspectives to the development of financial services and support for individuals in a manner which reflects the diversity of individual characteristics, needs and attitudes amongst the borrower client base.

SURVEY HEADLINES

The following issues are highlighted from the responses to the survey on indebtedness of individuals.

1. Microfinance institutions (MFIs) extend greater outreach of financial inclusion to lower income households and female borrowers than commercial banks;

2. 53% of all borrowers have a monthly household income less than KGS 20,000;

3. About 65% of MFIs and bank borrowers overlap in the mid-range of household incomes between KGS 15,000 and 40,000;

4. Expenditures on basic household essentials represent 50% of households with low incomes, compared with 30% of those with monthly incomes over KGS 40,000;

5. Household expenditures are generally below the level of national estimates, and 25% of all borrowers have reduced food expenditure in order to meet loan repayments;

6. 50% of loan usage was undertaken for 'asset acquisition' purposes, whilst only 30% was used for domestic consumption;

7. Loan leverage is high: loan repayments account for 47% of net disposable income of MFI borrowers and 60% of net disposable income of bank borrowers;

8. 35% of borrowing households have a monthly net disposable income (after loan repayments) of less than KGS 2,000 (approx. US$ 40);

9. Both MFIs and banks strongly support 'own business' clients with similar portfolio distributions across the trade sectors;

10. 60-70% of borrowers recognise a positive impact of borrowing upon their lives;

11. Only 2% of borrowers have loan arrears, and only 4% have arrears with utility payments … but …

12. 30-40% of borrowers recognise that they have loan repayment difficulties, despite low loan arrears – a further 30% have committed expenditures (household essentials, utilities, and loan repayment) greater than 75% of income;

13. Major differences in risk profiles occur between city and rural borrowers, and between household incomes below KGS 20,000 and over KGS 40,000;

14. 40% of borrowers considered that it is difficult to resolve debt problems with their lending institution, but only about half of these wanted additional assistance in such negotiations;

15. 80% of borrowers have remained with only one lender during the last two years – those who move between lenders borrow more and have higher risk profiles;

16. 30% of borrowers have savings, the majority of which is undertaken with non-formal financial savings institutions;
17. A large majority of borrowers have a positive view of the reputation of lending institutions and the 'mores' of their business cultures.

SUMMARY REVIEW OF A STUDY OF THE INDEBTEDNESS AND ATTITUDES OF INDIVIDUALS

SUMMARY OBSERVATIONS

Financial Inclusion

Three core dimensions of 'financial inclusion' are often characterised as the provision of loan services to lower income groups, wider inclusion and empowerment of female clients, and respect for the individual by the lending institution.

- The microfinance institutions (MFIs) have a greater proportion of clients (32%) with monthly incomes less than KGS 15,000 compared with 22% of bank clients.
- The majority (56%) of MFI clients were female, compared with 46% in the bank portfolios.
- 95% of respondents considered that lending institutions treated their clients with respect.
- MFIs provide lending to 43% of their borrowers by the group loan methodology (compared to 9% of bank clients).

However, the financial positions of the lower income segments is particularly strained. This reflects the colliding pressures of relatively high household expenditure and also high loan repayments (as a percentage of income). This results in an average residual household monthly net disposable income of KGS 7,000 (equivalent to KGS 1,600 for each household member). The financial pressures upon this segment of marginal 'financial inclusion' clients are significant.

Lender / Borrower Relationship

The relationship between the lending institutions and borrowers was reviewed in two perspectives – first, the 'values' which the institution portrays in the standards by which it acts, and secondly, the operational relationship with the clients.

There was an over-whelming recognition (95%) that clients are treated with respect, and the values of 'trustworthiness' and 'integrity' were widely perceived by about 85% of clients. This may be considered to be a strong response, recognising that those clients with payment difficulties will have necessarily faced problematic situations. There is also a strong perception (by about 80% of clients) that the lending institutions understand client needs and seek to improve the lives of clients. Such client opinions are more favourable than was identified in Bosnia and Herzegovina.

The operational interaction between lender and borrower presents a somewhat different perspective. There appears to be a high transparency in the available information of the clients' financial position and needs, but about 30-40% of clients indicate that the loan amount was "too much", repayments were "more than can be afforded", and that problem resolution was "difficult" with the lender. Such problems cannot be fully attributed to exceptional adverse events affecting the financial borrower, but should also be considered against the high level of loan repayment / leverage in relation to income (see below).

The low level of loan arrears (about 2%) may be contrasted with the 30-40% of borrowers who recognise that they have lending problems. This difference is further reflected by the recourse to informal funding / loan sources by a minority of borrowers, domestic problems resulting from borrowing, and reductions in food expenditure to meet loan repayments. This suggests that, for some reason, borrowers feel a particularly strong motivation to maintain timely loan repayments rather than incur loan arrears.

Impact of Lending

60-70% of clients indicated that borrowing had a positive impact on the quality of their lives. This was recognised at similar levels by both MFI and bank borrowers and also across the range of income segments (despite the financial constraints identified by the lowest income segments). This positive response may also be considered in conjunction with the wider financial inclusion which MFIs had achieved in relation to lower income and female clients. Despite a higher recognition of difficulties by rural borrowers resulting from debt, such clients reflected a more positive impact of borrowing upon their lives than was perceived by city clients.

Client Segmentation

The individual borrower market is not homogenous but, rather, consists a various significant segments with distinct characteristics, and financial needs and capacities. The principal client segments which impact upon structural risk exposure for the lender and financial vulnerability of the client are [i] household income, [ii] income source structure (own business, regular monthly and less regular frequency), [iii] city and rural locations, [iv] clients who recognise financial difficulties, and those who do not acknowledge their financial constraints, and [v] clients who remain with a single lender, and those who change lenders.

Despite the different characteristics of these various client segments, standard loan products appear to be widely used, rather than aligned to the particular needs of each major segment. This may reflect the different needs of, for example, [i] 'own business' in relation to asset acquisition finance in contrast to the cash-flow fluctuations of trading finance; [ii] the loan period term for domestic asset finance appears to similar to that of loans used for domestic consumption purposes; and, [iii] the potential opportunities for a selective extension of the loan term under refinance arrangement for appropriate borrowers who recognise their repayment difficulties, but who currently have a normal repayment term.

Loan Leverage

The overall levels of loan repayment / leverage in relation to income are much higher (30%) in Kyrgyzstan than in Bosnia and Herzegovina (18%). Including average domestic expenditures (household and utility) of 44% of income, the high leverage of committed basic expenditures in the budget of the average borrower in Kyrgyzstan (about 75%) can be identified.

The average loan leverage is lower amongst MFI clients (26%) than bank clients (34%). However, the greatest impact occurs with the lowest income segments (up to KGS 15,000) which represent 28% of all clients (and 21% of MFI outstanding loans; 8% of bank outstanding loans). The loan leverage of this borrower segment is 39% of income, which when taken with domestic expenditures of 56%, results in an overall level of committed monthly expenditures of 95%.

This highlights the particular challenge for the lending institution to provide a meaningful loan to the marginal income borrower. Despite the arrears by this income segment being low at about 2%, borrower responses show that in addition to much lower levels of domestic expenditure, this segment has a greater reliance informal loan sources. This increases the effective total leverage of these people. However, whilst it is difficult for the lending institution to identify the scale and range of such additional dependencies with individual clients, it is important to recognise, and adjust the service proposition to, the impact of such pressures.

Over-indebtedness

Whilst over-indebtedness may be popularly reflected in the level of loan arrears (only 2% amongst survey respondents), the scale of loan leverage demonstrates the low levels of net disposable income and budget pressures which are experienced by a majority of borrowers after meeting their committed basic expenditures. Over-indebtedness may, therefore, be most appropriately related to the capacity of the borrower to meet financial commitments without undue adverse impacts (financial or social) upon their lives.

In this broader context of 'over-indebtedness', about 30-40% of clients acknowledge the adverse impacts of debt on their lives (such as, difficulty to meet loan repayments, reduction in food expenditure, cause of family problems). Whilst the superficial budget positions of some of these borrowers may appear satisfactory, their responses show an underlying 'concern', or risk aversion to the level of financial commitments which they face. An additional 30% of borrowers, with committed expenditures over 75% of income, have only KGS 750 of net monthly disposable income (KGS 175 per household person) which shows the extreme budgetary constraints of those people. It is appropriate, therefore, to consider 'over-indebtedness' as an interaction of both a quantitative financial capacity and a qualitative evaluation of the individuals' feeling of vulnerability.

A risk categorisation framework suggests that about 50% of borrowers are in an 'exposed' indebted situation reflecting both their financial position and also the level of their concern.

Location

The location of borrowers is widely spread across city, rural and urban locations. The profile of borrowers varies significantly in these locations. The survey gains insights of the different client segments in each location. (Each institution will have a difference portfolio 'mix' of such constituent segments across locations and different cities).

The real cost-of-living was higher in city locations than rural – whilst average incomes were 15% higher, the cost of household essentials was 30% higher. Additionally, average outstanding loans were higher in the city (particularly for bank clients). Consequently, there was much less differentiation in the average net disposable incomes in the cities compared with rural, than applied to household incomes.

However, the rural borrowers consistently reported a higher recognition of 'debt problems' (compared to city borrowers) in relation to 'borrow too much', 'repayments more than can afford', and debt causes problems in family'. Additionally, there was a greater incidence of informal loans amongst rural borrowers. There was, however, no difference in the levels of those borrowers who reduced food expenditure to meet loan repayments, even amongst those employed in the agricultural sector.

Comparison of Microfinance Institutions and Commercial Banks

Whilst the basic demographics profiles of MFIs and banks (age, household size, consumer and own business, trade sectors) are very similar and about 60% of clients of each type of institution have mid-range incomes (KGS 15,001-40,000), the principal differences between the institutions relate to [i] the higher loan amounts and leverage provided by the banks, [ii] the higher level of debt problems being reported by bank clients, [iii] the greater use of the ‘group loan’ product by MFIs and individual loans by banks, and [iv] the greater share of lowest income households in MFIs in contrast to the larger share of highest incomes by the banks.

There appear, therefore, to be substantive differences in relation to the business case dynamics of core client segments and loan products, and the sensitivity of underlying risk profiles to economic change.

Outlook for Lending to Current Borrowers

The outstanding loan amounts and repayment levels shown by borrowers suggest that about 80% should reach maturity during the following 12 months. This highlights the immediacy of the renewal decisions to be faced by both borrowers and lending institutions. The client characteristics have indicated that the dynamics of such decisions are likely to vary significantly across the major borrower segments.

Segments such as [i] repayment difficulty, [ii] expenditures over 75% of income, and [iii] financial confidence (each with about 30% of clients) have both different experiences of the impact of the current loan and different financial capacities with which to accommodate repayments. About 60% of such current borrowers are either first-time, or non-recurrent, borrowers which suggests that a culture of debt-dependency may not yet be firmly established. Additionally, about 50% of current loans were used for some asset acquisition (either business or domestic) and such borrowing was, therefore, very ‘purpose driven’, rather than for general trading or consumption needs. This further suggests that a significant level of impending loan decisions will be based upon a balance of need and financial capacity.

Against the different needs, dependencies, financial capacities and attitudes of these client segments, the lending institutions may need to further develop and explain their product and service propositions to recognise, and respond to, such differentiated positions.

ISSUES FOR CONSIDERATION

The survey responses indicate a range of issues which have significant strategic or operational implications for the lending institutions and other institutional stakeholders. The following comments provide some observations based only on the findings of the survey. Whilst such issues may have been addressed by lending institutions and other stakeholders, it is hoped that these observations, based upon the responses of clients, will provide a useful additional perspective.

Risk Profile and Social Impact

The performance of the lending portfolios of the MFIs and banks appears to be strong, with only about 2% of clients in loan arrears. However, there is a range of indicators which suggest an underlying client situation which reflects some adverse risk dimensions impacting upon the potential vulnerability / sensitivity of loan performance. These include [i] high leverage by both MFIs and [particularly] banks, [ii] the sensitivity of the lowest income segment (up to KGS 15,000) to even a modest increase in the real cost-of-living, [iii] the recognition by about 30-40% of borrowers that their financial position is under pressure and that debt repayments are more than they can afford, and paradoxically [iv] the 'non-recognition' or non-acknowledgment by many with minimal net disposable income of their vulnerable financial position.

Conversely, the average period for the residual repayment of existing loans is relatively short (less than 12 months for the large majority of borrowers). This enables both lending institutions and borrowers to have greater flexibility in managing their respective risk exposures and adapting to changing economic conditions. This represents a strong position from which to manage the risk stability of the lending portfolios.

Despite their budget constraints, a majority of borrowers recognise the beneficial impact of borrowing upon their lives and this applies across all income segments. However, about 30% of borrowers recognise their dependency upon debt in order to maintain the lifestyles of their families. Such dependencies are concentrated (not surprisingly) upon those borrower segments which indicate greatest budget pressure and difficulty to meet loan repayments.

This presents the inevitable challenge to gain an appropriate 'balance' between [i] the capacity to adjust the volume and risk profile of the lending portfolios (as a result of the relatively short-term maturity profiles), and [ii] the social impact of the potential withdrawal of loan availability to those borrowers with greatest financial vulnerability – (a segment of borrowers which include the more marginal 'financially included'). This dynamic impacts the microfinance institutions to a greater extent than the banks because of its higher exposure to the lowest income segments.

Issue: The extent to which the interaction between the lending institution and the borrower should be based primarily upon a series of individual and short-term decisions, or if the core objective is to establish a basis for a longer-term relationship. The development of such market positions may be considered to vary in relation to the different characteristics of the major client segments, and also impacts upon the manner in which 'financial inclusion' and 'understanding of financial services' can be extended.

Client Segmentation

The survey has identified certain major client segments, which display some distinctive financial (quantitative) and attitudinal (qualitative) characteristics. Some principal dimensions of segmentation have included [i] income ranges, [ii] recognition, and non-recognition, of financial pressures, [iii] source of income, and [iv] mobility of borrowers between lenders.

The relative composition / mix of such client segments will vary between the loan portfolios of individual lending institutions. However, the structure and dynamics of these client segments will not only impact the financial performance of the institutions, but also impact the marketing, product and service delivery strategies of each institution.

The survey demonstrates the different financial and behavioural dynamics which occur across the client segments. Such segmentation identifies the need for, and demands of:

- Debt problem resolution mechanisms
- Loan structure and budget management guidelines for the lowest income segments
- Alignment of product structure and cash flow with the purpose of the loan and the borrowers' cash flow
- The identification of the financial services for those with greater financial capacity and confidence

This may be perceived to affect particularly the microfinance sector and its role in increasing financial access and experience.

Issue: The extent to which the capacity, needs and impact of the major client segments can be identified and addressed by lending institutions. In addition, the extent to which marketing strategy aligns such variations in capacity and needs to a differentiation in product and service propositions.

Low Income Households and Budget Management

The survey shows that households with the lowest incomes (up to KGS 15,000) represent a significant segment (28%) of all borrowers.

Whilst the nominal amount being spent on basic household expenditures is lower than that by other client segments, such expenditure is the highest, in real terms, when compared with the available household income. Similar financial dynamics apply to borrowings in relation to the amount, the level of repayment and the leverage of such payment in relation to income. The residual amount of net disposable income is minimal.

This is a client segment which is targeted to benefit from financial inclusion and the majority of borrowers recognise that the loan has improved the quality of their life. However, for many of these clients, there does not appear to be a full self-recognition of the vulnerability of their financial situation.

The particular characteristics of this most marginal segment of clients suggest that the 'normal' service and product proposition will not fully address their needs.

- Whilst the assessment of debt 'affordability' is usually primarily related to household income, it is important to recognise that, for the lowest income segment, it is particularly dependent upon the net disposable income, after expenditures on household essentials and utility costs. The level of such expenditures varies considerably. It may be appropriate to consider the establishment of 'expenditure guidelines' to provide a framework of the normal parameters for such costs, and thereby identify opportunities for potential economies. This would enable a standard 'cost basket' to be established for different locations and would thereby enable a regular review of such standard costs. This would identify the scale of any price changes and, thereby, the sensitivity impact upon the budget and debt affordability of this client segment.

- Against average expenditure on household essentials of KGS 5,800 (for a household of 4 persons), 25% of such low income families reduced their household expenditures in order to make loan repayments. This may suggest (*and this is simply an inference*) that the lower levels of household expenditure may have an adverse impact on the nutritional standards of the food expenditure of such low income families. It may be appropriate, therefore, to consider possible guidelines for an optimal nutritional diet, within the limits of the expenditure guidelines for household essentials.

Such budget assessments would enable a closer integration of the particular demands and sensitivities of the lower income clients with the real impact of loan leverage.

Issue: The development of holistic assessments of the particular financial capacities and needs of those lowest incomes segments which are part of the 'financial inclusion' undertaken by the lending institutions – and how these can be incorporated into the product and service proposition for this segment.

SOME QUESTIONS AND ANSWERS …

Some Questions

A range of substantive issues have been raised by the responses of borrowers in the survey conducted during September / October 2013. The following questions reflect these issues and the related dimensions are set out in the following 'Question and Answer' section. It is not intended that the following comments provide an exhaustive review of the particular issue, but rather enable brief 'cameo' insights. A more detailed review can be undertaken with the relevant data analysis spreadsheets.

It is hoped that the reader will find this list of questions / issues a useful basis by which to select those dimensions which are of particular interest.

The observations in the 'Questions and Answers' section are based entirely upon the responses to the survey. These have not been discussed with lending institutions, and no management information has been obtained from such lenders to provide a comparison with the survey responses. It would be ideal if the survey findings could be reviewed with the lending institutions and other institutional stakeholders in order to identify those areas of consistency and conversely those issues on which there are the greatest 'gaps' between the perceptions and data of borrowers and lenders.

Within the Q & A observations, occasional references are made to the corresponding responses which were shown in the recent survey[1] of individual indebtedness which was undertaken in Bosnia and Herzegovina (BiH). Whilst the differences in the markets and cultures of the two countries will limit the opportunities for detailed and strict assessments, such comparisons do provide a useful identification of some core issues which enable consideration to be focused on particular dimensions of financial situation and attitudes of both borrowers and lending institutions.

Survey respondents identified their respective lending institutions. The sample sizes varied and few were sufficiently large to provide a strong basis for detailed comment. However, from the available data, it can be seen that the distribution of borrower segments within the loan portfolio structures varies between lending institutions. As such, individual lending institutions will need to assess the implications of the different segments in relation to the respective compositions of their loan portfolios.

[1] Survey of indebtedness by individuals was undertaken in BiH in September / October 2013. This involved direct interviews with 3,780 individuals, involving borrowers from MFIs, banks and also non-borrowers. Similar surveys had been undertaken in BiH in 2012 (3,757 respondents) and 2011 (3,856 respondents)

1. **Survey Respondent Demographics**

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1. SURVEY RESPONDENT DEMOGRAPHICS

1.1 What is the domestic profile of borrowers?

Consistency of personal demographic profiles across MFIs and banks – household sizes lowest in city locations.

- The average number of people in a 'borrower' household is 4.4:
  - Osh Oblast has the highest (5.4) and Bishkek the lowest (4.0);
  - Average household size increases with average income;
  - Household sizes are higher in rural areas (4.9) compared with city (4.1).

- The majority (76%) of borrowers are married, and 17% single.

- The sources of income varied significantly between rural and city locations with about 55-60% self-employed in rural communities (about 46% in city), compared with 46% in regular employment in cities (25% in rural).

- Comparison between MFIs and banks indicates minimal structural differences:
  - Minimal difference in the age profile;
  - Household size and number of dependents are also similarly distributed;
  - The trading activity which underlies the source of income is also similar.

	Agriculture	Retail	Service	Public Sector	Other
City : MFI	9%	31%	18%	32%	16%
City : Bank	9%	30%	17%	34%	18%
Rural : MFI	42%	27%	12%	19%	14%
Rural : Bank	40%	24%	10%	20%	17%

1.2 What are the income profiles of borrowers?

MFIs have greater proportion of clients with lower incomes than banks – incomes higher in city locations than rural – an overlap of outreach by the MFIs and banks to about 60-65% of clients (those with mid-range incomes).

- The overall average household income of all respondents was KGS 26,450. With an average of 2.1 income earners per household, this represents an average individual income of KGS 12,750[2].
  - Average incomes of bank clients (KGS29,800) was 25% higher than that of MFI clients (KGS23,700) – average individual incomes were KGS14,200 (bank) and KGS11,500 (MFI);
  - Such income differentials were stretched further in comparisons of locations.

Income KGS	City		Rural		Urban
	MFI	Bank	MFI	Bank	All
Household	25,400	31,350	21,350	28,250	20,300
Individual	12,550	15,350	10,200	12,900	9,500

[2] Average income : National statistics indicate that the average monthly income is KGS 10,250

- Within MFI rural clients, 41% had household income less than KGS15,000 (compared with 22% of bank clients) – whilst in cities, banks had 31% of clients with household incomes over KGS30,000 (compared with 19% of MFI clients).

- The distribution of borrowers across the income ranges showed that the MFIs have a greater client focus towards the lower income segments than in bank portfolios:

Income Range	< 15,000	15,001 – 20,000	20,001 – 30,000	30,001 – 40,000	> 40,000
MFI	32 %	27 %	26 %	8 %	8 %
Bank	22 %	23 %	29 %	11 %	15 %

  - There is, therefore, a substantive overlap of mid-income ranges in the target client bases of MFIs and banks. This need to be contrasted below with the respective borrowing levels of each group of clients.

- The different segmentation of incomes between MFI and bank clients is shown particularly in a comparison of clients using different loan products:

Average Income KGS	Group Loan	Business Loan	Individual Loan	Agricultural Loan
MFI	22,850	27,900	24,000	21,600
Bank	24,650	40,450	27,900	30,100

  - This table provides an interesting comparative market positioning of these products, in which the income levels of group and individual loans are relatively closely aligned – however, the distribution of such loans highlights the sharply different product distributions:

Distribution of loans	Group Loan	Business Loan	Individual Loan	Agricultural Loan
MFI	43 %	9 %	43 %	5 %
Bank	9 %	17 %	70 %	4 %

This shows the alignment of the group loan product with the lowest-income MFI clients.

1.3 What is the dependency upon multiple incomes to a household budget?

An average of 2.1 income-earners in each household – lowest income households have lowest level of multiple earners – little difference in the multiples of MFI and bank households.

- There is a frequent occurrence of multiple income-earners within a household with an overall average of 2.1 amongst all borrowing households, within which 24% are single income and 22% have more than 2 incomes.

- Whilst there is minimal difference between the multiple earning profiles of MFIs and banks, there are some interesting differences in relation to various client segments:
  - The level of household income relates directly to the level of multiple together with the average individual income.

Income Range	< 15,000	15,001 – 20,000	20,001 – 30,000	30,001 – 40,000	> 40,000
Multiple	1.73	2.00	2.23	2.39	2.42
Ave. Individual Income	6,800	9,500	12,100	15,500	29,600
Clients : 1 earner	40%	23%	14%	13%	17%
Clients : 2 earners	49%	60%	57%	50%	47%
Clients >2 earners	11%	17%	29%	37%	36%

- The agriculture and retail trade segments have [slightly] the highest multiple (with 24% of households with more than 2 incomes). The engineering and property sectors have the lowest at 19%.
- Rural locations have higher levels of multiple incomes than cities, although 25% of rural MFI clients are single income compared with only 18% of bank clients.

• The level of household income is shown throughout this review and Q & As to be a significant differentiating dimension of borrower performance, together with the particular financial constraints upon the lowest income segments. The following table provides some insights of the impact of the number of income-earners.

% of clients in the income multiple	Income <KGS 15,000	Income >KGS 30,000	My loan repayments are more than I can afford	Household expenditure as % of Income	Utility expenditure as % of Income	Net Disposable Income (after Loan Payment)
One income	47%	13%	34%	42%	5%	4,400
Two income	25%	18%	33%	41%	4%	5,900
Over 2 incomes	13%	34%	34%	41%	4%	9,700

- There is a clear concentration of lowest incomes amongst the single earners.
- However, it does not appear that 'single earner' is, in itself, a major discriminating factor in the risk performance of the borrower or the feeling of well-being in the client.

1.4 What is the level of expenditure on household essentials and utility costs?

Significant variations in the levels of household expenditure across different borrower segments – majority of households indicate expenditure levels which are less than the national estimate for the cost-of-living – household essential costs represent between 30-50% of income.

• The overall monthly expenditure by borrowing households on domestic needs (food, family and domestic essentials, but excluding utilities) was KGS 10,400, equivalent to an average of KGS 2,350 per household person. Average utility costs amounted to KGS1,200:
  - This contrasts with formal national statistics which indicate a need for an average cost-of-living of about KGS4-5,000 per person. Local comments indicate that the survey response levels are probably just about enough to cover basic essentials;

- About 15% of respondents identified expenditures at a level which is consistent with the national statistics.

- The cost-of-living varied significantly between city (40% of income) and rural locations (35% of income).

Household Expenditure KGS	City		Rural		Urban
	MFI	Bank	MFI	Bank	All
Household	10,400	12,500	8,000	9,600	8,800
Individual	2,500	3,000	1,600	1,900	1,900

- Food expenditures had been reduced in all locations by about 25% of clients in order to afford loan repayments.

- There were significant variations in the levels of expenditure in the major trade sectors, which were also shown in the range of utility costs:

Ave. Household Expenditure	Service	Retail	Public Sector	Agriculture
Household	11,300	10,400	10,100	8,900
Utility	1,450	1,200	1,100	900

- The levels of domestic expenditure increased as household incomes increased, but at a slower rate. The proportion of such domestic costs was greater, therefore for lower income segments:

Ave. Household Expenditure	< 15,000	15,001 – 20,000	20,001 – 30,000	30,001 – 40,000	> 40,000
Household	5,800	8,600	10,900	15,000	21,200
% of income	50 %	45 %	40 %	40 %	30 %

- Within the lowest income band, reductions in food expenditure had been undertaken by 25% MFI clients and 28% bank clients in order to make their loan repayments.

1.5 What are the principal differences between city and rural borrower profiles?

Household size larger in rural locations than in city – real cost-of-living higher in the city, despite higher incomes – loan amounts higher amongst city borrowers – rural borrowers show higher adverse pressures from borrowing.

- The average household sizes showed some significant differences
  - Rural were larger (average 5.0 persons) compared with city (average 4.1 persons);
  - The number of dependents was also higher (rural 2.8 – city 2.1);
  - Slightly more borrowers were single in the city (21% of all borrowers) – rural 11 %.

- Income levels (see above) were, on average, 15% higher in city locations, whilst expenditure on domestic household essentials (such as food and cleaning) was 30% higher:
  - o Recent increases in the cost-of-living of household essentials (greater than income) was more widely experienced by rural clients.

- The range of trading activities was diverse in all locations, even in rural areas despite the dominance of agriculture:

	Retail	Agriculture	Service	Public Sector	Other
MFI – City	31%	9%	18%	32%	16%
Bank – City	30%	9%	17%	34%	18%
Rural – MFI	27%	42%	12%	19%	14%
Rural – Bank	24%	40%	10%	20%	17%
Urban – All	33%	23%	17%	23%	14%

- A comparison of lending between city and rural provides some significant dynamics and shows the extent of overlap across microfinance and bank portfolios.
  - o Overall average loan balances of all borrowers varied significantly:

	City		Rural		Urban
	MFI	Bank	MFI	Bank	All
Ave. Loan	53,800	140,600	48,500	96,600	50,000

  - o MFIs provided a greater share of the small loans (up to KGS 15,000) : 26% of MFI rural borrowers, compared with 18% of bank rural borrowers – in contrast, banks had a much higher exposure to larger outstanding loans over KGS 100,000 (27% of bank city borrowers in contrast to 9% of MFI city borrowers);

  - o However, there was a substantial proportion of both MFI and bank borrowers with outstanding loans between KGS 15,000 and 100,000 – in city locations : 65% of MFI and 57% of bank – in rural locations : 66% of MFI and 63% of banks;

  - o Borrowing from informal lenders (family, retailers and moneylenders) was higher amongst rural clients than in the cities.

- Net disposable incomes (average) were significantly affected by the level of loan repayments and there was little substantive difference in the residual net disposable incomes, except in urban areas which were significantly lower.

Expenditures as % of Income	Household expenditure as % of Income	Utility expenditure as % of Income	Loan repayment as % of Income	Net Monthly Disposable Income	Net Monthly Disposable Income KGS
MFI – City	41%	5%	24%	30%	7,678
Bank – City	40%	5%	34%	21%	6,643
Rural – MFI	37%	4%	29%	30%	6,353
Rural - Bank	34%	4%	35%	28%	7,801
Urban - All	43%	4%	31%	21%	4,347

- Whilst rural clients were more positive than city clients that 'loans improved the quality of life', this was contrasted by a range of responses in relation to pressures on repayment capacity which appear to be stronger amongst rural borrowers than those in the city locations.

% of respondents who agree with the statement	MFI		Bank	
	City	Rural	City	Rural
I borrowed too much	32 %	48 %	34 %	52 %
It is / was difficult to resolve debt problems with my lender	39 %	46 %	40 %	51 %
Debt repayments cause problems within my family	36 %	47 %	35 %	52 %
My loan repayments are / were more than I can afford	28 %	43 %	28 %	49 %
I would like help to resolve debt problems with my lending institution	24 %	36 %	26 %	38 %

  - These responses must be contrasted with the low level of loan arrears (c. 2%) amongst rural borrowers.

1.6 Is the loan structure consistent with the income cash flow of the borrower and the usage of the loan funds?

High usage of fixed term, fixed repayment loans with little apparent variation to reflect usage need or underlying cash flow characteristics – wide usage of group and individual loans by MFIs, whilst banks primarily use individual loans – low usage of specific 'agricultural' loans.

- The distribution of the principal loan products reflects a strong emphasis towards the group and individual loans, although the pattern of usage differed substantially between MFIs and banks.

	Group Loan	Business Loan	Individual Loan	Agricultural Loan
MFI	43 %	9 %	43 %	5 %
Bank	9 %	17 %	70 %	4 %

- The principal loan products were reflected in different lending practices by the MFIs and the banks. There was a high level of overlap between the overall client characteristics of 'group' and 'individual' loan products within the MFIs, but there were significant contrasts between the client profiles of such products provided by the banks.

KGS	Group Loan		Individual Loan	
	Average Income	Average Outstanding Loan	Average Income	Average Outstanding Loan
MFI	22,800	48,400	24,000	54,800
Bank	24,700	42,600	27,900	106,600

- However, the pattern of loan usage may be set against this profile of product distribution. This shows that fixed-term, fixed repayment loans were widely used for purposes in which the underlying cash flow was unlikely to be consistent with that of the loan structure.

	Asset acquisition: Business	Other Business needs	Asset acquisition: Domestic	Other Domestic	Property
Microfinance Institutions					
Group	26%	15%	25%	33%	7%
Business	65%	24%	8%	6%	3%
Individual	21%	10%	29%	34%	11%
Agricultural	23%	18%	26%	16%	21%

Banks					
Group	23%	5%	38%	28%	9%
Business	54%	34%	7%	7%	5%
Individual	21%	14%	22%	36%	15%
Agricultural	11%	27%	15%	27%	24%

- This apparent inconsistency between the types of loan, the implicit period of the loan term and the underlying cash flow dynamics of the different major trade sectors is further illustrated in relation to certain principal trading activities in the table below.

	Retail	Service	Agriculture	Public Sector	Implied Ave. Loan Term (months)
Microfinance Institutions					
Group	32%	16%	19%	27%	16
Business	57%	14%	14%	8%	20
Individual	24%	18%	19%	32%	18
Agricultural	21%	1%	76%	24%	11
Banks					
Group	19%	9%	16%	49%	14
Business	47%	14%	14%	13%	26
Individual	27%	18%	18%	30%	24
Agricultural	13%	10%	73%	6%	26

- The differences between the variations of the underlying cash flow of the 'own business' borrower with the rigidity of the fixed-term, fixed-repayment loan are shown in the following table, relating to the types of loan used by 'own business' clients during the last two years.

Distribution[3]	Group Loan	Business Loan	Individual Loan	Agricultural Loan
MFI	49%	15%	37%	5%
Bank	6%	26%	68%	4%

[3] The total of percentages exceeds 100% and reflects that some borrowers will have used more than one loan during this two year period.

2 FINANCIAL PROFILE OF BORROWERS

2.1 What is the impact of loan repayments on net disposable income?

Loan repayments show high leverage by borrowers – loan repayments account for over 80% of net disposable incomes of lowest income segment – bank borrowers have higher leverage than MFI borrowers – level of loan repayments in Kyrgyzstan much higher than in Bosnia and Herzegovina.

- The overall average household income of all respondents was KGS 26,450. With an average of 2.1 income earners per household, this represents an average individual income of KGS 12,750[4].
    - Average incomes of bank clients (KGS29,800) was 25% higher than that of MFI clients (KGS23,700) – average individual incomes were KGS14,200 (bank) and KGS11,500 (MFI);
    - Such income differentials were stretched further in comparisons of locations.

Income KGS	City		Rural		Urban
	MFI	Bank	MFI	Bank	All
Household	25,400	31,350	21,350	28,250	20,300
Individual	12,550	15,350	10,200	12,900	9,500

- The overall average net disposable incomes for MFI and bank clients were similar and reflect the much higher average loan repayments being undertaken by bank clients.

Net Disposable Income KGS	Income	Household costs	Utility costs	Loan Repayments	Net Disposable Income (after Loan)
MFI	23,700	9,500	1,150	6,100	6,950
Bank	29,800	11,400	1,250	10,250	6,900
Non-Borrower	22,900	10,200	1,250		11,450

- However, among the lower income segments, the impact of committed expenditures was particularly strong. The table below highlights the delicate vulnerability of the financial position of a significant proportion of borrowers.

[4] Average income: National statistics indicate that the average monthly income is KGS 10,250 per earner

Household Income Segments	Household and Utility costs	Loan Repayments	Net Disposable Income NDI (after Loan)	Distribution of Loans: Value	Distribution of Borrowers
< 15,000	6,600	4,650	600	12%	28%
15,001 - 20,000	9,700	6,050	3,300	16%	25%
20,001 - 30,000	12,200	7,050	7,900	23%	27%
30,001 - 40,000	16,500	9,800	10,900	13%	9%
> 40,000	23,400	20,050	28,100	36%	11%

- o This table highlights the particular vulnerability of about 50% of borrowers to only modest increases in the real cost-of-living (see also Q & A 5.2). The costs in this table reflect only the committed essential expenditures – other costs such a clothing, medical, transport, education are not included.
    - Within the income segment up to KGS 15,000, 76% of borrowers reported committed expenditures in excess of 75% of income;
    - Within the income segment up to KGS 15,001-20,000, 57% of borrowers reported committed expenditures in excess of 75% of income.

- Whilst the amount of loan repayments in relation to household income appears reasonable and relatively consistent across the range of incomes, the real cost of loan repayments is sharply different in relation to net disposable income after domestic costs (in which the cost of food and essentials is proportionately higher for low income households).

Household Income Segments	MFI		Bank	
	Loan repayment as % of household income	Loan repayment as % of Net Disposable Income (pre loan)	Loan repayment as % of household income	Loan repayment as % of Net Disposable Income (pre loan)
< 15,000	37%	83%	43%	99%
15,001 - 20,000	28%	57%	37%	74%
20,001 - 30,000	22%	40%	30%	56%
30,001 - 40,000	21%	37%	31%	56%
> 40,000	21%	32%	32%	48%

- This highlights the significantly different credit risk characteristics across the range of income segments, and also between the MFIs and the banks:
  - The structural risk profiles of the loan portfolios of individual MFIs and banks will clearly be affected by the particular distribution of their respective loan portfolios;
  - The potential vulnerability resulting from the impact of the amount of loan repayments on the lower income segments is further increased by the level of borrowing from informal lenders by these segments.

% of Borrowers re : Informal Loans	Family and Friends		Retail Shop	
	MFI	Bank	MFI	Bank
< 15,000	12%	21%	8%	10%
15,001 - 20,000	10%	15%	6%	9%
20,001 - 30,000	9%	11%	7%	6%
30,001 - 40,000	7%	11%	7%	6%
> 40,000	5%	8%	4%	3%

- Whilst the markets and cultures are, of course, different, it may be useful to consider these positions of Kyrgyzstan borrowers in comparison with those in Bosnia and Herzegovina (BiH)

  - The impact of expenditures as a percentage of household may be compared:

Average of all borrowers	Household expenditure as % of Income		Loan repayment as % of Income		Total expenditures as % of Income	
	Kyrgyzstan	BiH	Kyrgyzstan	BiH	Kyrgyzstan	BiH
MFI	40%	33%	26%	13%	71%	60%
Bank	38%	32%	34%	16%	77%	61%

  - These lower levels of net disposable income (after loan costs) may suggest a greater incidence of loan arrears in Kyrgyzstan than BiH. This is not the situation. (Loan arrears in Kyrgyzstan are 2%, compared with about 8-10% in BiH);
  - Utility costs (as identified by respondents) are higher in BiH than Kyrgyzstan.

2.2 How does the frequency and regularity of income impact upon borrower performance and attitude?

Borrowers with 'regular monthly income' and 'own business' represent 85% of all borrowers – 'regular monthly income' clients show lower risk characteristics, but lowest incomes – 'other income' segments show highest risk characteristics.

- The distribution of borrowers is broadly similar in MFIs and banks across the different income characteristics: 'regular monthly income' 40%; 'own business' 50%; and 'other [less regular] income' 15%[5];

- The average level of net disposable income may be shown in relation to those with regular monthly income, self-employed and those with other, less regular frequency of income. The resultant net disposable incomes are reasonably similar which highlights:

[5] The total of income characteristics exceeds 100% because some borrowers report more than one source of income

- The importance of the 'added-value' dimension of the loan which should be recognised by those higher-income, higher-loan clients in view of the higher risk which they incur;
- The greater vulnerability of those clients with higher leverage.

Net Disposable Income KGS	Income	Household costs	Utility costs	Loan Repayments	Net Disposable Income (after Loan)
Microfinance Institutions					
Regular Monthly	22,400	9,500	1,150	5,100	6,650
Own Business	25,100	9,600	1,150	7,050	7,300
Other	23,300	9,500	1,200	5,500	7,100
Bank					
Regular Monthly	25,400	11,000	1,200	7,000	6,200
Own Business	34,200	12,000	1,300	13,100	7,800
Other	26,900	10,500	1,300	7,500	7,600

- Although average direct loan arrears are low across these income segments, informal borrowings are undertaken particularly by the 'other income' segment, with about 15% of clients borrowing from family and 13% from retailers. (This applies to both MFI and bank clients).

- The above table indicated the potential importance of the 'added-value' being created by the loan, either directly financial or its impact on lifestyle. The following table shows that about 30-40% of borrowers had adverse attitudes towards the loan repayment capacity and wider loan experience.

% of respondents who **agreed** with the following statement	Regular Monthly		Own Business		Other Income	
	MFI	Bank	MFI	Bank	MFI	Bank
Loans [do not] improve the quality of life	29 %	29 %	30 %	25 %	29 %	32 %
I borrowed too much	33 %	35 %	41 %	46 %	40%	42 %
My loan repayments are more than I can afford	29 %	30 %	34 %	36 %	36 %	42 %
Debt repayments cause problems within my family	37 %	37 %	41 %	41 %	43 %	48 %
It is / was difficult to resolve debt problems with my lender	40 %	43 %	43 %	43 %	47 %	49 %

2.3 What proportion of borrowers reflect some recognition of debt repayment pressures?

About 30-40% of borrowers recognise financial pressure and difficulty in making loan repayments – a further 30+% have committed basic expenditures more than 75% of income but do not acknowledge financial pressures.

- The level of direct loan arrears is low (measured in the survey as any loan arrears, not simply over 30 days). However, other surrogate measures may be used to provide some indication of the possible levels of repayment pressures which borrowers may be experiencing. These are summarised in the following table in which each segment is exclusive (no borrower is included in more than one segment).

Repayment Characteristic	Household Income KGS	Average Outstanding Loan Balance	Net Disposable Income NDI (after Loan)	Distribution of Loans : Value	Distribution of Borrowers
Arrears	25,650	83,400	6,250	2%	2%
Lender Refusal	25,700	82,200	5,600	8%	8%
Repayment Difficulty[6]	27,250	102,500	7,000	34%	27%
Expenditure >75% Income	22,350	89,000	750	34%	32%
Remainder	30,200	60,700	13,550	22%	31%

  - This table indicates that there is a significant level of pressure being experienced by borrowers which is not transparent in lending performance reporting.
- These characteristics of repayment pressure are further demonstrated in the following additional dimensions of borrower profile.

Repayment Characteristic	Food expenditure has been reduced to make loan repayments	I (or my spouse) have taken additional work to make loan repayments	Friends or family provided money to repay my loan	Loan from Family and Friends	Loan from Retailer	Loan from Moneylender or Pawnbroker
Arrears	47%	37%	29%	23%	10%	15%
Lender Refusal	32%	32%	16%	21%	16%	10%
Repayment Difficulty	32%	35%	19%	15%	7%	8%
Expenditure >75% Income	19%	18%	7%	10%	5%	5%
Remainder	20%	15%	6%	5%	4%	4%

[6] 'Repayment Difficulty' : Based upon those borrowers who agreed (Question 66) that "my loan repayments are more than I can afford", and excluding those who have loan arrears or had been refused a loan by a lender in the last 12 months.

- The above characteristics demonstrate the range of actions which have been taken by those borrowers who have recognised the financial pressures which they must address;

- The level of reduction of monthly food expenditure may be particularly significant. Current expenditures on food by the first three 'problem' segments is about KGS 2,300 per person. This may be contrasted with the national statistics which indicate a monthly budget of about KGS 4,000. If these borrowers are experiencing repayment problems, and many have already taken the actions indicated above, there may be minimal scope for further domestic budget economies or external borrowing;

- It may be suggested that the amount, or continuation, of support from family is likely to be limited for many of these problem debt situations. As 'problem debt' is such a sizeable segment, it is appropriate to seek to identify and address such problems, either by a review of budget expenditures, or possible refinance / restructure of the debt.

- The impact of problem lending extends across all income segments, but impacts particularly upon the lowest income groups.

Income Range	< 15,000	15,001 - 20,000	20,001 - 30,000	30,001 - 40,000	> 40,000
Arrears	2 %	2 %	2 %	3 %	3 %
Lender Refusal	11 %	11 %	10 %	7 %	11 %
Repayment Difficulty	37 %	30 %	33 %	30 %	37 %
Expenditure >75% Income	76 %	57 %	39 %	38 %	39 %

  - *These figures show the total share of clients in each income segment for each 'problem' category.*

2.4 To what extent do borrowers use more than one lender, and do these clients show different characteristics?

About 80% of borrowers have used only one lender in the last two years – about 30% of former clients of MFIs and banks subsequently take loans from the other type of institution - only 5% of borrowers have multiple concurrent loans.

- This issue can be considered in three principal dimensions:
  - The extent to which borrowers leave an MFI institution and move to a bank (or vice versa);
  - The extent to which borrowers hold more than one loan at any single time;
  - The extent to which borrowers move between lending institutions when they renew their loan.

- The movement between MFIs and banks occurs both ways at similar levels (see also Q & A 2.8):
  - 19% of former bank borrowers now have a loan with an MFI and an additional 17% have borrowed from an MFI in the last 2 years;

- 18% of former MFI borrowers now have a loan with a bank, and an additional 12% have borrowed from a bank in the last two years;
- The value of outstanding loans differs considerably. This suggests that the motivation for the change in lender was driven by different factors, in which:
  - Former bank borrowers now have an average outstanding debt of about KGS 40,000 with an MFI, compared to an overall average MFI debt of KGS 51,500
    - These borrowers show a higher risk profile with 10% of borrowers in loan arrears with the MFI and 22% with a loan application refusal in the last 12 months.
  - Former MFI borrowers now have an average debt of KGS 109,100 with a bank
    - These borrowers show a higher risk profile with 5% of borrowers in loan arrears with the MFI and 22% with a loan application refusal in the last 12 months.
- Note: the survey did not seek to determine the overall scale of client attrition within either MFIs or banks. It identified former borrowers in order to determine their profile characteristics for comparison with current borrowers and their borrowing actions after leaving either an MFI or bank.

- The level of borrowers with multiple concurrent loans is low and relates to only 5% of borrowers in both MFIs and banks.

- The level of movement between lenders during the preceding two-year period identified a reasonable scale of movement. This must be considered also in the context of the average loan terms of 12-24 months for the majority of loans and the limits which this places on the opportunities to move between lenders.

Number of Lenders	One	Two	Three	More than three
MFI	78%	18%	3%	1%
Bank	77%	19%	4%	1%

- Except those borrowers with loan arrears, there was minimal difference in the 'multiple lender' characteristics of the other problem repayment segments.

- In response to a separate, direct question, over 75% of both MFI and bank clients agreed that "It is better to borrow from only one institution, rather than to change lenders".

2.5 How often are debt repayment problems caused by exceptional adverse events?

Exceptional adverse events impact rural clients more frequently than those city locations – lowest income segment (up to KGS 15,000 per month) suffers more adverse events than higher incomes.

- The incidence of exceptional events upon an individual during the previous six months did not occur consistently across the various client segments;
- Such adverse events occurred more frequently in rural areas.

Adverse Events during the previous 6 months	Lifestyle				Financial Action	
	I lost my job	My spouse / partner lost his/her job	My business was not successful	Major illness of self or family	I had to sell a major asset to repay a loan	Friends or family provided money to repay my loan
MFI - City	5%	5%	8%	11%	4%	9%
Bank - City	5%	5%	9%	9%	4%	11%
Rural - MFI	13%	18%	14%	22%	6%	15%
Rural - Bank	9%	15%	12%	23%	5%	10%
Urban - All	9%	15%	10%	20%	3%	15%

- There was minimal overall difference between MFI and bank clients, although the incidence was slightly greater amongst borrowers than non-borrowers.

Adverse Events during the previous 6 months	Lifestyle				Financial Action	
	I lost my job	My spouse / partner lost his/her job	My business was not successful	Major illness of self or family	I had to sell a major asset to repay a loan	Friends or family provided money to repay my loan
MFI	8%	10%	10%	15%	5%	11%
Bank	9%	9%	10%	15%	4%	11%
Non-Borrower[7]	6%	7%	8%	13%		

 - Only 3% of bank and MFI clients with regular incomes had lost their jobs;
 - About 15% of ‘own business’ clients had experienced an unsuccessful business;
 - Clients with ‘other sources’ of income reported (perhaps unsurprisingly) the highest levels of lost jobs for the borrower (MFI 14% and bank 18%) and spouse (MFI 16% and bank 18%), together with higher levels of financial support from their families to assist loan repayments.

- Such events were particularly impactful upon the lowest income segment, although there was a relatively high level of financial support being provided by families to the loan repayments of higher income segments.

[7] This includes former borrowers of MFIs and banks

Adverse Events during the previous 6 months	Lifestyle				Financial Action	
	I lost my job	My spouse / partner lost his/her job	My business was not successful	Major illness of self or family	I had to sell a major asset to repay a loan	Friends or family provided money to repay my loan
< 15,000	13%	12%	12%	18%	6%	17%
15,001 - 20,000	7%	9%	10%	16%	5%	9%
20,001 - 30,000	5%	7%	9%	14%	3%	7%
30,001 - 40,000	3%	5%	7%	9%	4%	11%
> 40,000	3%	5%	10%	7%	3%	11%

- The lower income segments show a much higher level of illness within the family. These segments also reported a low average level of expenditure on domestic essentials, including food. Although low in amount (KGS 5,800), this basic expenditure represented 50% of income, with loan repayments taking a further 37%. Whilst the survey can make no direct causality between these dimensions, it may be appropriate to consider the opportunities to review the guidelines for food costs within the credit assessment process – and to consider the development of nutritional guidelines for low income households.

- Adverse events occurred most frequently with borrowers operating in the following trade sectors

Adverse Events during the previous 6 months	Lifestyle				Financial Action	
	I lost my job	My spouse / partner lost his/her job	My business was not successful	Major illness of self or family	I had to sell a major asset to repay a loan	Friends or family provided money to repay my loan
Agriculture	12%	15%	15%	19%	6%	13%
Building-Property	15%	16%	11%	13%	3%	10%
Engineering	15%	12%	13%	18%	5%	16%
Food Production	10%	6%	15%	23%	12%	17%
Manufacturing	11%	8%	11%	12%	5%	11%

2.6. How does the profile of 'employed' borrowers compare with that of 'own business' borrowers?

'Own business' clients have higher income than 'employed' clients – borrowing by 'own business' is significantly higher than that by those in 'regular employment' – 'own business' show higher recognition of problems with loan repayment and debt.

- The overall distribution of borrowers is broadly similar in MFIs and banks across the different income characteristics: 'regular monthly income' 40%; 'own business' 50%; and 'other [less regular] income' 15% [8];
- The profile of income sources may be summarised in relation to the different locational profiles.

Distribution of all Income Sources	Employed : Monthly Income		Own Business		Other Income	
	MFI	Bank	MFI	Bank	MFI	Bank
City	45%	44%	47%	48%	14%	14%
Rural	32%	27%	56%	62%	19%	22%
Urban (all)	36%		55%		17%	
Non-Borrowers	43%		42%		19%	

  - The distribution percentages relate to respondents only in the respective location;
  - MFIs have a lower proportion of 'own business' clients in rural locations.

- Average incomes of bank clients are consistently higher than those of MFI clients.

KGS	Employed : Monthly Income		Own Business		Other Income	
	MFI	Bank	MFI	Bank	MFI	Bank
H'hold Income	22,400	25,400	25,100	34,200	23,300	26,900
Net Income. inc Loan Repay	6,650	6,200	7,300	7,850	7,100	7,550

  - However, the costs of higher levels of bank lending are reflected in the greater similarity of net income levels after loan repayments.

- The impact on net disposable income reflects the different levels of average borrowings and leverage.

KGS	Employed : Monthly Income		Own Business		Other Income	
	MFI	Bank	MFI	Bank	MFI	Bank
Average loan	42,600	81,600	60,700	159,300	41,600	73,700
Ave. repayment	5,100	7,000	7,000	13,100	5,500	7,500
Leverage[9]	23%	28%	28%	38%	24%	28%

  - The leverage of bank borrowers is significantly higher;
  - The average loan of 'own business' is significantly higher than that for 'regular employment': MFI + 40% and bank + 95%;
  - The revenue streams to bank lending institutions will, therefore, be substantially higher than those for the MFIs. The comparative service and delivery propositions are not known in detail, other than the greater use of group loans, which will favourably impact upon the operating costs for that product;

[8] The total of income characteristics exceeds 100% because some borrowers report more than one source of income
[9] Leverage: Loan repayment as a percentage of household income

- These tables suggest quite different business case propositions for the MFIs and banks in relation to the different loan products and client segments.

- Informal borrowings and budget adjustment initiatives suggest the actions being undertaken by individuals to maintain up-to-date loan repayments.

	Employed : Monthly Income		Own Business		Other Income	
	MFI	Bank	MFI	Bank	MFI	Bank
Loan : Family / Friends	11%	13%	7%	12%	15%	17%
Loan : Retailer	6%	7%	6%	6%	12%	13%
Friends or family provided money to repay my loan	10%	9%	12%	10%	13%	15%
Food expenditure has been reduced to make loan repayments	21%	23%	24%	26%	32%	37%
I (or my spouse) have taken additional work to make loan repayments	21%	22%	22%	24%	36%	38%

The different levels of loan repayment problems are shown in the following table:

% in sub-segment : 'income source'	Employed : Monthly Income		Own Business		Other Income	
	MFI	Bank	MFI	Bank	MFI	Bank
Arrears	3%	1%	3%	3%	2%	4%
Lender Refusal	9%	14%	7%	11%	9%	17%
Repayment Difficulty	29%	30%	34%	36%	36%	42%
Expenditure >75% Income	50%	59%	49%	55%	51%	60%

- *These figures show the total responses for each income segment. Expenditure (>75%) as % of income includes loan repayments*;

- The levels problem lending clients are consistently higher amongst bank clients (than MFI clients) in each of the segments;

- 'Other Income' clients represent the highest risk but account for only 15% of borrowers for each of MFIs and banks.

2.7. To what extent are loans used to support basic domestic expenditure needs?

Only 30% of loan funds are used for domestic consumption purposes – domestic usage is highest amongst lower income segments

- The profile of loan funds does not show any excessive overall concentrations of usage / purpose:

	Domestic		Business		Property
	Asset Acq'n	Other	Asset Acq'n	Other	
City : MFI	26%	30%	24%	14%	8%
City : Bank	20%	31%	24%	16%	13%
Rural : MFI	27%	32%	25%	14%	13%
Rural : Bank	22%	29%	25%	20%	15%
Urban (All)	22%	29%	41%	8%	6%

- o There does not appear to be any excessive overall use of loan funds to support basic living costs (but see also below re loan usage in relation to income);
- o There appears to be a balanced distribution across different loan purposes;
- o It is possibly surprising that city and rural profiles are so similar.

- The usage of loan funds changes in relation to the level of household income:

	Domestic		Business		Property
	Asset Acq'n	Other	Asset Acq'n	Other	
< 15,000	27%	39%	25%	9%	9%
15,001 - 20,000	23%	33%	26%	11%	11%
20,001 - 30,000	23%	26%	25%	17%	12%
30,001 - 40,000	22%	26%	22%	23%	10%
> 40,000	12%	18%	33%	27%	14%

- o The lower income segments are clearly more dependent upon loans to support their basic domestic expenditures, both for asset acquisition and other consumable expenditures;
- o The higher income groups show a greater focus towards business usage;
- o The credit assessment process and loan structure will need to reflect these different dynamics, as 53% of borrowers have household incomes up to KGS 20,000.

- The impact of problem lending clients does not vary greatly in relation to loan usage:

	Domestic		Business		Property
	Asset Acq'n	Other	Asset Acq'n	Other	
Arrears	2%	2%	2%	4%	5%
Lender Refusal	9%	12%	9%	12%	9%
Repayment Difficulty	36%	33%	36%	35%	33%
Expenditure >75% Income	53%	55%	50%	53%	56%

- The profile of loan usage by the major trade sector activities is shown below:

Distribution by Trade Sector	Domestic		Business		Property
	Asset Acq'n	Other	Asset Acq'n	Other	
Agriculture	25%	26%	24%	18%	14%
Retail	10%	16%	49%	25%	6%
Service	23%	34%	20%	11%	15%
Public Sector	36%	43%	10%	4%	11%

- This highlights the substantial differences between the trade sectors and thereby the different economic dynamics which will affect the underlying credit performances;
- This profile of loan usage may be compared with that shown by borrowers in BiH:
  - Amongst 'own business' borrowers in BiH about 25-30% of loan funds were used for general domestic (non-asset) consumer purposes compared with about 18% in Kyrgyzstan;
  - About 70% of 'own business' borrowers' in BiH used loan funds for trading (non-asset) purposes in contrast to 30% in Kyrgyzstan (where there was a greater emphasis towards asset acquisition finance);
  - Amongst those borrowers with 'regular monthly income', the comparable levels of consumer (non-asset) expenditures were about 70% in BiH compared with 40-45% in Kyrgyzstan.

2.8. What do former borrowers do after they leave an institution?

65-70% of clients leaving either MFIs or banks cease to borrow – those who switch from MFI to bank, or vice versa, and continue to borrow show higher risk performance after changing – former MFI clients increase substantially their indebtedness with the new bank lender – those who cease to borrow have (on average) lower incomes and lower savings than those who continue to borrow.

- Former clients of both MFIs and banks were identified (see also Q & A 2.4):

  - 19% of former bank borrowers now have a loan with an MFI and an additional 17% have borrowed from an MFI in the last 2 years;

  - 18% of former MFI borrowers now have a loan with a bank, and an additional 12% have borrowed from a bank in the last two years;

  - The level of outstanding loans differs considerably. This suggests that the motivation for the change in lender was driven by different factors, in which:

    - Former bank borrowers now have an average outstanding debt of about KGS 40,000 with an MFI, compared to an overall average MFI debt of KGS 51,500:
      - These borrowers show a higher risk profile with 10% of borrowers in loan arrears with the MFI and 22% with a loan application refusal in the last 12 months.

    - Former MFI borrowers now have an average debt of KGS 109,100 with a bank:
      - These borrowers show a higher risk profile with 5% of borrowers in loan arrears with the MFI and 22% with a loan application refusal in the last 12 months.

  - Note: the survey did not seek to determine the overall scale of client attrition at either MFI or banks. It identified former borrowers in order to determine their borrowing actions after leaving either an MFI or bank.

- The resultant level of 'former' borrowers who did not undertake a loan are:
    - 64% of former bank borrowers;
    - 70% of former MFI borrowers.

- The financial profiles of the 'former borrowers' show a contrasting position for MFIs and banks:

	Household Income KGS	Household & Utility Costs	Net Disposable Income NDI (pre Loan)	Average Outstanding Loan Balance	Net Disposable Income NDI (after Loan)
Former MFI : Now Bank Borrower	25,700	12,700	13,000	109,100	3,800
Former Bank : Now MFI Borrower	20,500	9,600	10,900	40,000	5,500
Former MFI : Non Borrower	22,600	11,500	11,100		11,100
Former Bank : Non Borrower	25,300	12,300	13,000		13,000

- This table[10] suggests that those MFI clients who move to a bank have a higher-than-MFI average income. In contrast, those bank borrowers who change to MFIs have a much lower household income than the overall bank average (KGS 29,800);
- Those former borrowers who cease to borrow (both MFI and bank) have lower household incomes than the averages of current borrowers.

- Those 'former borrowers' who continue to borrow have a higher level of savings than those who do not (see also Q & A 4.8):

	Former MFI Borrowers		Former Bank Borrowers	
	Bank Borrower	Non-Borrower	MFI Borrower	Non-Borrower
Savings with a financial institution	9&	10%	27%	12%
Other savings	46%	28%	45%	38%
Insurance product(s) from financial institution	5%	3%	14%	1%

- This is a further indication of the apparently stronger financial position of those clients (particularly former MFI) who continue to borrow.

[10] Care : Sample sizes are small for those Former Borrowers who change from an MFI lender to a bank, or vice versa. These segments should be considered simply as possible indicators and do **not** have a strong statistical confidence

3. LENDING INSTITUTIONS AND LENDING PORTFOLIOS

3.1 What are the principal demographic characteristics of borrowers?

Major traditional demographic segments relate to [i] trade activity; [ii] region; [iii] age; and [iv] loan amount – some differences but not the principal drivers of risk profile.

(Client segments and risk indicators are reviewed in the following Q & A 3.2)

- The following comments relate to the major generic client segments across the borrowing population and thereby span both MFIs and banks. (The following section looks more closely at the major differences between MFI and bank clients within various segments). The tables in this section show the quantitative financial profile and also indications of risk which have been recognised by the borrower.
    - In relation to a more detailed review of income and expenditure, it may be noted that:
        - There is a significant extent of overlap between MFI and bank client bases, with 61% of MFI clients and 53% of bank clients having incomes of between KGS 15,001 and 40,000;
        - The principal dimensions of the income profiles have been shown above (see Q & A 1.2, 2.1 and 2.2) and will be included in the following comparison of bank and MFI;
        - A review of the sources of income is shown in Q & A 2.2.
- **Trade Activity** : Financial : the principal trading activities which underpin the income of borrowers are agriculture, retail, service, and public sector:

	Household Income KGS	Household & Utility Costs	Net Disposable Income NDI (pre Loan)	Average Outstanding Loan Balance	Net Disposable Income NDI (after Loan)
Agriculture	24,100	9,900	14,200	68,100	7,000
Retail	27,000	11,600	15,400	90,900	6,700
Service	30,700	12,800	17,900	116,500	8,200
Public Sector	22,800	11,200	11,600	56,000	5,800

- The greater financial constraints on the employed, public sector borrowers are apparent.

- Trade Activity : the scale of 'problem repayment' borrowers varies between these major sectors and is reflected in the following indicators (see also separate Q & A 4.3 re 'arrears'):

	My loan repayments are more than I can afford	Friends or family provided money to repay my loan	Debt repayments cause problems within my family	Food expenditure reduced for loan repay	I (or my spouse) have taken additional work to make loan repayments
Agriculture	38%	13%	45%	31%	31%
Retail	35%	11%	40%	23%	23%
Service	24%	10%	33%	25%	23%
Public Sector	31%	9%	37%	21%	20%

  - The greater pressures being experienced and recognised by borrowers within the major sectors, agriculture and retail, are apparent.

- **Region**: Financial

	Household Income KGS	Household & Utility Costs	Net Disposable Income NDI (pre Loan)	Average Outstanding Loan Balance	Net Disposable Income NDI (after Loan)
Bishkek	33,600	14,500	19,100	119,000	9,000
Osh	28,700	12,900	15,800	108,000	7,600
Chui Oblast	29,000	11,600	17,400	92,000	7,200
Jalal-Abad	21,000	10,300	10,700	47,000	5,200
Osh Oblast	20,000	8,600	11,400	51,000	5,400

  - Major differences in these regional positions will impact upon the need for differentiated credit assessment processes and budget guidelines. (Separate analyses are available to review locational performance by city, rural and urban).

- Region : Problem Lending

	My loan repayments are more than I can afford	Friends or family provided money to repay my loan	Debt repayments cause problems within my family	Food expenditure reduced for loan repay	I (or my spouse) have taken additional work to make loan repayments
Bishkek	39%	11%	48%	31%	30%
Osh	19%	13%	23%	23%	15%
Chui Oblast	36%	6%	46%	31%	23%
Jalal-Abad	21%	6%	31%	14%	16%
Osh Oblast	52%	20%	52%	23%	32%

- Some significant variations are evident across these regions. There appear to be particular pressures in the largely rural regions of Chui and Osh, not only in relation to financial constraints, but also in relation to the social impact of the indebtedness.

- **Age**: Financial

	Household Income KGS	Household & Utility Costs	Net Disposable Income NDI (pre Loan)	Average Outstanding Loan Balance	Net Disposable Income NDI (after Loan)
16-25	23,500	10,800	12,700	47,900	6,900
26-35	25,600	11,200	14,400	72,900	7,100
36-45	28,700	12,100	16,600	102,100	7,300
46-55	26,700	12,000	14,700	96,800	6,400
> 55	25,100	11,500	13,600	71,600	6,100

- Surprisingly little difference between the income levels across the age range. The higher debt levels of 36-55 years appear intuitively to be the appropriate segments to reflect a higher borrowing need.

- **Age:** Problem Lending

  - The following table shows, again, that there is little substantive difference in attitudes across the age ranges, and continues to show the consistent and pervasive adverse impact of debt upon the domestic situation for a significant minority of borrowers.

	My loan repayments are more than I can afford	Friends or family provided money to repay my loan	Debt repayments cause problems within my family	Food expenditure reduced for loan repay	I (or my spouse) have taken additional work to make loan repayments
16-25	28%	14%	36%	23%	21%
26-35	34%	11%	41%	25%	25%
36-45	36%	11%	42%	24%	23%
46-55	33%	11%	41%	24%	24%
> 55	29%	9%	34%	26%	18%

- **Loan Amount** : Financial

	Household Income KGS	Household & Utility Costs	Net Disposable Income NDI (pre Loan)	Average Outstanding Loan Balance	Net Disposable Income NDI (after Loan)
< 15,000	20,200	9,900	10,300	9,500	6,600
15,001 - 30,000	22,200	10,400	11,800	23,800	7,200
30,001 - 50,000	24,800	10,900	13,900	42,600	8,000
50,001 - 100,000	28,500	12,300	16,200	76,400	6,800
> 100,000	43,200	16,500	26,700	351,400	5,600

- Household incomes relate progressively to the size of the outstanding loan. However, there is a dramatic reversal of this apparent affordability in relation to the resultant net disposable incomes (after loan payments). This will have direct implications for the vulnerability of higher-income, higher-loan clients and their sensitivity (and capacity to respond) to external events and price changes.

- **Loan Amount:** Problem Lending

	My loan repayments are more than I can afford	Friends or family provided money to repay my loan	Debt repayments cause problems within my family	Food expenditure reduced for loan repay	I (or my spouse) have taken additional work to make loan repayments
< 15,000	28%	12%	39%	21%	20%
15,001 - 30,000	34%	13%	40%	22%	23%
30,001 - 50,000	32%	9%	37%	27%	23%
50,001 - 100,000	34%	10%	40%	26%	25%
> 100,000	39%	11%	45%	30%	26%

- The recognition of debt pressures are reflected across the range of loan sizes at broadly similar levels;
- The portfolio mix of the scale of such loan sizes within an individual lending institution may have a significant impact upon its relative risk profile, in comparison to its peers.

3.2 What are the principal similarities and differences between the loan portfolios of the MFIs and banks?

This section takes the previous dimensions of borrowers and provides a comparison between MFI and bank clients in relation to location, income, loan type, multiple lenders, and savings.

Loan amounts and leverage ratios are consistently higher amongst bank clients, in comparison with MFI clients with similar demographic and financial characteristics – problem lending / risk characteristics are usually higher amongst bank clients, again in comparison with MFI clients with similar demographic and financial characteristics – bank lending is dominated by the individual loan product, whilst MFIs provide similar levels of group loan and individual loans.

- **Location** : Financial

	Household Income KGS	Household & Utility Costs	Net Disposable Income NDI (pre Loan)	Average Outstanding Loan Balance	Net Disposable Income NDI (after Loan)
City : MFI	25,400	11,700	13,700	53,800	7,700
City : Bank	31,300	13,900	17,400	140,700	6,600
Rural : MFI	21,300	8,800	12,500	48,500	6,400
Rural : Bank	28,200	10,600	17,600	96,600	7,800
Urban	20,300	9,600	10,700	50,000	4,300

- Banks attract clients with higher net disposable incomes than the MFIs;
- However, the differentials of net disposable incomes are much changed by the impact of the higher loan amounts and repayment leverage.

- Location : Problem Lending (see also separate Q & A 4.2 and 4.3 re ‘over-indebtedness’ and ‘arrears’)

	My loan repayments are more than I can afford	Friends or family provided money to repay my loan	Debt repayments cause problems within my family	Food expenditure reduced for loan repay	I (or my spouse) have taken additional work to make loan repayments
City : MFI	28%	9%	36%	23%	20%
City : Bank	28%	11%	35%	26%	20%
Rural : MFI	43%	15%	47%	26%	28%
Rural : Bank	49%	10%	52%	29%	32%
Urban	32%	15%	42%	24%	31%

- Problem debt levels are similar for MFIs and bank clients in the respective locations;
- The recognition of debt problems is significantly higher in rural areas;
- This reflects only those clients who recognise the ‘problems’ – see also risk categorisation for an assessment of the interaction of quantitative financials with qualitative perceptions.

- **Income** : Range : Financial

This segmentation is based upon clients in the various income segments. See also Q & A 1.2 and 1.3 in relation to income and expenditure.

Income Range / KGS	Net Disposable Income NDI (pre Loan)		Average Outstanding Loan Balance		Net Disposable Income NDI (after Loan)	
	MFI	Bank	MFI	Bank	MFI	Bank
< 15,000	5,200	5,300	33,700	44,100	900	0
15,001 - 20,000	9,300	9,500	43,800	61,100	4,000	2,400
20,001 - 30,000	15,100	14,800	49,300	91,000	9,100	6,600
30,001 - 40,000	20,600	21,000	61,800	162,100	13,000	9,300
> 40,000	45,600	49,600	145,600	340,600	31,100	25,900

- The leverage of bank clients is significantly higher than that of MFI clients at all income levels;
- Against broadly similar demographic profiles, the MFIs and banks are presenting dramatically different loan product and service propositions;
- The previous dimension identified that these differentials are applied throughout the portfolios in both city and rural locations;
- The erosion of bank net disposable incomes, and the comparative strength of those of MFI clients, in the respective income ranges suggests a greater vulnerability amongst bank clients in the event of adverse economic changes.

See also separate assessment of sensitivity to any increases in the real cost-of-living (Q & A 5.2).

- **Income :** Range : Leverage of Loan Repayments

  - Lending by banks is undertaken at significantly higher leverage ratios than those undertaken by the MFIs:

Income Range / KGS	Net Disposable Income NDI (post Loan)		Loan repayment as % of household income		Loan repayment as % of net disposable income	
	MFI	Bank	MFI	Bank	MFI	Bank
< 15,000	900	0	37%	43%	83%	99%
15,001 - 20,000	4,000	2,400	28%	37%	57%	74%
20,001 - 30,000	9,100	6,600	22%	30%	40%	56%
30,001 - 40,000	13,000	9,300	21%	31%	37%	56%
> 40,000	31,100	25,900	21%	32%	32%	48%

  - This suggests a significantly higher risk profile / vulnerability at each of the respective borrower segments – but, it must be noted that the loan portfolios are structured differently in relation to the proportion of clients and outstanding loans for each of the respective segments.

- **Income :** Range : Problem Lending (see also separate Q & A 4.2 and 4.3 re 'arrears' and 'over-indebtedness'):

Income Range / KGS	My loan repayments are more than I can afford		Debt repayments cause problems within my family		Food expenditure reduced for loan repay	
	MFI	Bank	MFI	Bank	MFI	Bank
< 15,000	36%	40%	46%	47%	25%	28%
15,001 - 20,000	26%	35%	32%	40%	20%	26%
20,001 - 30,000	34%	33%	38%	36%	29%	29%
30,001 - 40,000	29%	31%	44%	42%	24%	27%
> 40,000	40%	35%	44%	39%	23%	21%

  - Loan repayment pressures are higher amongst bank clients in the lowest two income bands which represent [i] 59% of MFI clients and 47% of bank clients and [ii] 44% of MFI outstanding loan value and 20% of bank loan value;
  - The levels of problem lending indicators appear broadly similar between MFI and bank clients in relation to the respective segment – however, the distribution of the loan portfolios shows that the MFIs have a greater share of lower income clients.

Income Range / KGS	Distribution : Clients		Distribution : Loan Value	
	MFI	Bank	MFI	Bank
< 15,000	32%	22%	21%	8%
15,001 - 20,000	27%	23%	23%	12%
20,001 - 30,000	26%	29%	25%	22%
30,001 - 40,000	8%	11%	9%	15%
> 40,000	8%	15%	22%	42%

- **Income** : Source : Financial

	Net Disposable Income NDI (pre Loan)		Average Outstanding Loan Balance		Net Disposable Income NDI (after Loan)	
	MFI	Bank	MFI	Bank	MFI	Bank
Regular Monthly	11,800	13,200	42,614	81,600	6,700	6,200
Own Business	14,400	21,000	60,724	159,300	7,300	7,900
Other	12,600	15,100	41,596	73,300	7,100	7,600

  - The impact of higher loan leverage by bank borrowers is reflected in the similar levels of net disposable income of MFI and bank clients;
  - The market propositions of these types of institutions are clearly different – yet there is a high overlap (about 60-65%) of clients in the mid-range of incomes. This would suggest that there are different service and delivery propositions which attract different client segments (but these are not reflected in the traditional demographic characteristics).

- **Income** : Source : Problem Lending

	My loan repayments are more than I can afford		Debt repayments cause problems within my family		Food expenditure reduced for loan repay	
	MFI	Bank	MFI	MFI	Bank	MFI
Regular Monthly	29%	30%	37%	37%	21%	23%
Own Business	34%	36%	41%	41%	24%	26%
Other	36%	42%	43%	48%	32%	37%

  - Despite the higher leverage amongst bank borrowers, these indicators of problem lending again show similar levels between MFI and bank clients in the respective income source category;
  - However, such characteristics relate only to those clients who 'recognise', or admit to, their financial problems. The risk categorisation assessment (see Q & A 4.1 and Attachment 2).

- **Loan Type** : Financial

Note: Distribution of borrowers by largest product types: MFI Group 43%, Individual 43%; and Bank Individual 70%, Business 17%) (See also Q & A 1.6 re product type).

	Net Disposable Income NDI (pre Loan)		Average Outstanding Loan Balance		Net Disposable Income NDI (after Loan)	
	MFI	Bank	MFI	Bank	MFI	Bank
Group	12,500	13,200	48,400	42,600	6,700	7,400
Business	15,500	25,200	93,300	210,800	5,800	8,400
Individual	13,100	15,800	54,800	106,600	6,900	6,700
Agricultural	12,000	18,000	49,900	150,700	7,400	5,900

- Group lending is a small portfolio for the banks, representing only 9% of clients;
- The significantly higher leverage of bank clients is shown throughout the other products.

- **Loan Type** : Problem Lending (see also separate Q & A 4.2 re 'arrears')

	My loan repayments are more than I can afford		Debt repayments cause problems within my family		Food expenditure reduced for loan repay	
	MFI	Bank	MFI	Bank	MFI	Bank
Group	30%	39%	42%	41%	24%	23%
Business	39%	37%	37%	45%	18%	27%
Individual	32%	33%	38%	40%	26%	26%
Agricultural	26%	50%	31%	56%	30%	45%

  - Despite the higher leverage, the perceptions of loan repayment difficulty are similar for both MFI and bank clients;
  - However, the adverse social impact of indebtedness upon the family is more strongly recognised by bank clients. Nevertheless, clients of both MFIs and banks demonstrate a high level of domestic pressure (even within the group loan product) which cannot be reflected by the external reporting of lending performance by lending institutions.

- **Multiple Lenders**: Financial
  This relates to the current number of lenders used in the last two years by a borrower. The overwhelming majority remain within either MFIs or banks, rather than using both types of institution.

	Net Disposable Income NDI (pre Loan)		Average Outstanding Loan Balance		Net Disposable Income NDI (after Loan)	
	MFI	Bank	MFI	Bank	MFI	Bank
One lender	12,500	16,700	44,600	110,400	6,900	6,800
Two or more	15,000	18,500	75,900	161,600	7,300	7,300

  - The use of multiple lenders appears to relate directly to higher outstanding loan balances;
  - Although incomes (pre loan) are higher, net disposable incomes (after loan costs) result in minimal differences between MFIs and banks
  - Again, the higher leverage of the bank clients relates a greater sensitivity of this portfolio to any adverse economic change.

- Multiple Lenders : Problem Lending (see also separate Q & A 4.2 re 'arrears' and 2.8 re 'former borrowers'):

	My loan repayments are more than I can afford		Debt repayments cause problems within my family		Food expenditure reduced for loan repay	
	MFI	Bank	MFI	Bank	MFI	Bank
One lender	31%	36%	39%	40%	21%	24%
Two or more	38%	32%	44%	43%	34%	36%

- The multiple borrowers with MFIs show a greater recognition of debt repayment problems than those with the banks;
- Both multiple MFI and bank clients show much higher levels of reduction in food expenditure.

- **Savings**: Financial

  Note: The level of savings with a financial institution is relatively low. The following table relates to other, informal savings. See separate Q & A 4.8 for further review of savings.

	Net Disposable Income NDI (pre Loan)		Average Outstanding Loan Balance		Net Disposable Income NDI (after Loan)	
	MFI	Bank	MFI	Bank	MFI	Bank
'Other' savings	14,100	18,500	53,500	135,800	7,800	7,700
Non-Savers	12,700	16,500	50,900	113,100	6,600	6,800

- The proportion of clients undertaking 'informal' savings is similar for MFI clients (29%) and bank (32%);
- Both institutions show that 'savers' have a slightly higher level of net disposable income than 'non-savers'. However, the differential between MFI and bank clients is eroded by the costs of higher loan amounts.

- Savings : Problem Lending (see also separate Q & A 4.8)

	My loan repayments are more than I can afford		Debt repayments cause problems within my family		Food expenditure reduced for loan repay	
	MFI	Bank	MFI	Bank	MFI	Bank
'Other' savings	25%	28%	28%	29%	24%	23%
Non-Savers	35%	39%	45%	46%	24%	28%

- It may 'intuitively' be suggested that those clients with savings may have a stronger budgetary disciple than the 'non-savers';
- This is reflected in higher levels of 'problem' recognition by the 'non-savers'.

3.3 Do the survey responses indicate credit standards or criteria?

(See also Q & A 7.4 re "Do lenders understand the borrower's financial position")

Banks provide higher loans and higher leverage ratios than those taken by MFI borrowers – the leverage ratios are highest amongst the lowest income groups – leverage ratios across higher income segments (above KGS 20,000) are maintained at similar average levels.

The survey responses show the substantive differences in the leverage of MFI and bank clients. Whilst other reviews show the recognition by the borrowers of their capacity to manage their debt levels and loan repayments, the following tables demonstrate some characteristics of the relationship of debt to income.

- The level of debt repayments may be considered in relation to household income:

	Household and Utility costs as % of Household Income		Loan Repayment as % of Household Income		Total Committed Expenditures as % of Household Income	
	MFI	Bank	MFI	Bank	MFI	Bank
City	46%	44%	24%	34%	70%	79%
Rural	41%	38%	29%	35%	70%	72%

  - The overall impact of higher leverage is greater upon city bank clients

- These aggregate figures reflect a range of committed expenditures across the income ranges:

	Household and Utility costs as % of Household Income		Loan Repayment as % of Total Household Income		Loan Repayment as % of Net Disposable Income (pre loan repayments)	
	MFI	Bank	MFI	Bank	MFI	Bank
< 15,000	55%	57%	37%	43%	83%	99%
15,001 - 20,000	51%	50%	28%	37%	57%	74%
20,001 - 30,000	44%	45%	22%	30%	40%	56%
30,001 - 40,000	44%	44%	21%	31%	37%	56%
> 40,000	32%	33%	21%	32%	32%	48%

  - This table presents some critical perspectives of the credit risk process, based on the quantitative financial positions reported by borrowers;

  - The relative cost of basic household essentials is much greater, in real terms, for the lower income households. Whilst the nominal loan amounts to lower incomes are less, the real cost of loan repayments, in relation to available net disposable income, is significantly higher for low income groups (as shown in the final two columns of the above table);

  - 32% of MFI clients and 22% of bank clients are in the lowest income segment.

- There is a wide range in the distribution of the level of repayments as a percentage of household income which show the higher levels of amongst bank and lowest income clients:

% of borrowers	Loan Repayments as % of Household Income				
	<10%	11-20%	21-30%	31-40%	>40%
MFI : Total	14%	31%	22%	13%	20%
Bank : Total	9%	25%	20%	16%	30%
Income Segment					
MFI : <15,000	7%	19%	20%	20%	34%
Bank : <15,000	4%	15%	17%	24%	41%
MFI : 15-20,000	10%	30%	32%	10%	18%
Bank : 15-20,000	6%	24%	27%	15%	29%

  - The loan repayment leverage of low incomes is extremely high. In relation to the lowest income group (up to KGS 15,000), 54% of MFI clients and 65% of bank clients have loan repayments greater than 30% of monthly household income.

- It is not known if the lending institutions relate affordability to total household income, or net disposable income (after application of standard expenditure guidelines) – or if the borrowers provide the lending institutions with other ['more acceptable'] budgetary figures. Survey respondents were asked "When I drew my last loan, the lender knew what I could afford"
    - 87% of the lowest income agreed, compared with over 90% of incomes over KGS 30,000;
    - 74% of those with loan arrears agreed;
    - 83% of 'other income' sources agreed, compared with 89% by 'own business'.
  - These responses suggest that the lending process was transparent for the large majority of borrowers and that relevant information was provided.

3.4 Does the loan process adequately reflect the impact of basic cost-of-living expenditures?

Household expenditures increase in relation to increasing incomes (but at a lesser growth rate) – the proportionate cost of basic household needs is much higher for low income households – together with higher proportionate loan costs, the low income clients are left with minimal net disposable income – certain borrower segments reflect higher-than-average expenditure levels in higher debt repayment problems – expenditure levels on utility costs appear to be relatively low.

The above responses demonstrate the range of leverage ratios which are dominated by the cost of household essentials and the loan repayments in relation to income.

National Statistics indicate that the average cost-of-living per person is estimated at KGS 4,300 per month. This may be contrasted with the survey responses which indicate an overall average expenditure of KGS 2,750 (including utilities) per person. This is a significant difference, even allowing for inevitable differences in which expenditure items are included.

- Against this estimated national statistics level, which implies an average household monthly cost of about KGS17,000,
  - about 30% of borrowers would have a household income less than the estimated cost-of-living requirement;
  - about 80-85% of borrowers report expenditure levels (including utilities) less than the national estimate.

- The overall average expenditure by borrowers of essential household needs and utilities in KGS 11,600
    - Within this monthly expenditure, utilities (gas, electricity, water, garbage collection) averages KGS 1,200. *Local experience will review this level to determine if it reflects a reasonable monthly average, assess the extent to which this may increase in the colder months. However, it seems that any revision would be likely to increase this cost and would adversely impact further on the level of net disposable income;*
    - Such expenditures vary significantly in relation to different client portfolios:

Income : KGS		Problem Repayment : KGS		Location : KGS	
< 15,000	6,600	Arrears	11,100	MFI - City	11,700
15,001 - 20,000	9,700	Lender Refusal	12,400	Bank - City	13,900
20,001 - 30,000	12,200	Repayment Difficulty	11,200	Rural - MFI	8,800
30,001 - 40,000	16,500	Expenditure >75% Income	12,700	Rural - Bank	10,600
> 40,000	23,400	Remainder	10,600	Urban - All	9,600

        - Significantly different expenditure levels for the varying income segments. What 'standard expenditure cost' guidelines are used by the lending institutions to assess the affordability of loan commitments? – or to validate the budget figures presented by the borrower?;
        - Problem repayment segments suggest that there may be opportunities for improved budget economies to be made by some clients with financial pressures. It may be noted that those with no indication of financial pressure (the 'remainder' segment) have the lowest levels of expenditures – which may suggest that they exercise the strongest budgetary disciplines;
        - The locations show substantial variations in expenditure levels. Again, this suggests the need for a continuing review of comparative expenditure levels and trends – and the maintenance of appropriate guidelines / standards in the assessment of credit applications.

- The level of utility costs shows less variation between the client segments than household expenditure, but does increase in relation to income. There is no difference in this type of expenditure between MFI and bank clients. A monthly cost of about KGS 750 for the lowest income segment increases to KGS 2,250 for the highest income:

    - This represents only about 5% of household income (compared with about 15% in BiH);
    - The survey was undertaken in September / October 2013 and this utility cost may reflect summer, rather winter, usage levels. However, this utility cost appears to be very low and any increase to reflect higher winter usage would have a significant and disproportionate impact upon the net disposable incomes of the lowest income groups.

3.5 How does lending to 'own business' clients compare between MFIs and banks?

Similar distribution across trade sectors by both MFIs and banks – significant overlap of MFIs and banks in relation to income levels, although MFIs have a greater support of lower income clients – banks provide larger loan amounts than MFIs and allow higher leverage in repayment levels.

- A significant proportion of lending by both MFIs and banks is undertaken to 'own business' clients
  - MFI : 46% in city locations; 56% in rural locations; about 50-55% in urban locations;
  - Bank : 48% in city locations; 60% in rural locations; about 50-55% in urban locations.
- There is also a great similarity in the trade sectors which are supported:

	Manufacture	Food Production	Retail	Engineering	Building - Property	Service	Agriculture
MFI	3%	4%	52%	2%	3%	14%	26%
Bank	4%	6%	49%	4%	4%	14%	26%

  - The two dominant trade segments, agriculture and retail, are characterised by quite different trading characteristics – the seasonal cash flow dynamics of agriculture – and the lower entry-barriers and generally shorter-term trading cycles of the retail sector.

- There is also a significant level of 'overlap' across the clients of MFIs and banks in relation to the level of household income (as a general proxy for the scale of the underlying business activity):

% of borrowers	Household Income of 'Own Business' Borrowers : KGS				
	< 15,000	15,001 - 20,000	20,001 - 30,000	30,001 - 40,000	> 40,000
MFI	29%	27%	26%	9%	9%
Bank	16%	21%	30%	14%	19%

  - The average incomes for these 'own business' clients are [a] MFI KGS 25,100 and [b] Bank KGS 34,200;
  - Whilst the MFIs show a greater inclusion of lower income businesses and banks, in contrast, have a greater share of high incomes, there is a significant overlap in the mid-range incomes (KGS 15,001 – 40,000) of 62% of MFI and 65% bank borrowers.

- However, the product structure to deliver this lending differs substantially between MFIs and banks:

Type of Loan to 'Own Business'	Group	Business	Individual	Agricultural
MFI	49%	15%	37%	5%
Bank	6%	26%	68%	4%

- These represent quite different service and delivery propositions by the lender and different levels of flexibility to the borrower:
  - group loans are generally less responsive to individual needs;
  - the inflexibility of the fixed repayment cash-flow structures of these loans is unlikely to be consistent with trading cash flows and business cycles of many 'own business' clients.
- The underlying business case structures for each product will have different dynamics and impact the performance, skill base and flexibility of the different types of institution.

- The differences between the lending propositions of MFIs and banks are shown starkly in the levels of outstanding loan balance reported by survey respondents:

% of borrowers	Outstanding Loan Balance of 'Own Business' Borrowers : KGS				
	< 15,000	15,001 - 30,000	30,001 - 50,000	50,001 - 100,000	> 100,000
MFI	20%	27%	24%	17%	11%
Bank	11%	20%	22%	17%	29%

  - This results in substantial differences in the average outstanding loan balances : MFI average of KGS 60,700 and Bank average of KGS 159,300;
  - There is again an 'overlap' of mid-range loan amounts between KGS 15,001 – 100,000 of MFI 68% of clients and bank 59% of clients.

- However, this higher level of lending by the banks is directly reflected in the higher leverage of loan repayments in relation to income:

% of borrowers	Loan Repayment as % of Household Income : 'Own Business' Borrowers				
	<10%	11-20%	21-30%	31-40%	>40%
MFI	11%	29%	22%	14%	24%
Bank	9%	22%	19%	15%	36%

  - This appears to represent some significant differences (at the extreme) in the market position and trading practices of the MFIs and banks;
  - Nevertheless, there remains a significant level of overlap in the portfolio structures of the two types of institution;
  - It may be noted above that there were considerable similarities in the profiles of location and trade sector exposures.

4. RISK PROFILE AND PERFORMANCE

4.1 What proportion of borrowers are over-indebted?

About 30-40% of borrowers recognise that they have debt repayment problems – a significant proportion of other borrowers (a further 30+%) have committed expenditure of more than 75% of income and thereby with a low capacity to meet other expenditure needs and exceptional payments – financial support is provided to a significant minority by family and friends – risk categorisation indicates that only about 10% of borrowers are in a strong financial position after loan costs.

- Loan arrears are low (about 2%) and 93% of borrowers respond that they "feel in control of their financial situation". It is necessary, therefore, to consider alternative indicators of 'over-indebtedness' which may include :
  - Actions by the borrower to enable loan repayments which would be unlikely to be part of the original credit proposition;
  - Acknowledgement / recognition by the borrower that debt repayment problems exist;
  - Financial constraints which indicate that the borrower has minimal capacity to meet living costs beyond household essentials, utilities and loan repayment.

- 'Actions by the borrower to enable loan repayments which would be unlikely to be part of the original credit proposition' may be considered in relation to certain major borrower segments:

Household Income	Loan from family or friends	Friends or family provided money to repay loan	Debt Refinance	Reduced food expenditure to make loan repayments	Additional work to make loan repayments
< 15,000	15%	17%	2%	26%	26%
15,001 - 20,000	11%	9%	4%	21%	21%
20,001 - 30,000	9%	7%	5%	27%	23%
30,001 - 40,000	9%	11%	4%	26%	22%
> 40,000	6%	11%	4%	21%	24%

  - The involvement of family to make payments suggests the pressure on the borrower. However, it may be suggested that the scale of such support may be limited as those other family members need also to meet their own expenditure;
  - Actions such as reduced food expenditure or additional work are relatively easy actions for 'self-help' by the borrower and reflect the financial constraints being experienced.

- 'Acknowledgement / recognition by the borrower that debt repayment problems exist'

Household Income	I borrowed too much	My loan repayments are more than I can afford	Debt repayments cause problems within my family	It is difficult to resolve debt problems with my lender	I would like help to resolve debt problems with my lending institution
< 15,000	38%	37%	47%	50%	33%
15,001 – 20,000	39%	30%	35%	41%	28%
20,001 – 30,000	37%	33%	36%	42%	26%
30,001 – 40,000	36%	30%	42%	34%	23%
> 40,000	43%	37%	41%	40%	30%

  - These responses suggest an underlying acknowledgement of financial / budget constraints by about 30-40% of borrowers and that the debt repayment commitments are having an adverse impact upon lifestyle;

- The recognition of the need for external support in resolving repayment difficulties also reflects an inability to identify a constructive way forward from current financial pressures.

- 'Financial constraints which indicate that the borrower has minimal capacity to meet living costs beyond household essentials, utilities and loan repayment'

Household Income	Household and Utility Expenditure	Net monthly disposable income (pre loan)	Loan Repayment	Net monthly disposable Income (post loan)	Net monthly disposable income per person
< 15,000	6,600	5,200	4,600	600	150
15,001 – 20,000	9,700	9,300	6,000	3,300	750
20,001 – 30,000	12,200	14,900	7,000	7,900	1,700
30,001 – 40,000	16,500	20,700	9,800	10,900	2,300
> 40,000	23,400	48,100	20,000	28,100	6,000

- The available net disposable income is minimal at the lower income levels;
- The average loan term for the lower income segments is about 16 months;
- The net disposable income for the two lowest income segments is highly sensitive to any changes in the real cost of household essentials and the repayment period of the loan.

- The recognition of debt repayment difficulties is shown in the following segments.

	Income KGS	Net Disposable Income (after Loan) KGS	Outstanding Loan KGS	Distribution of Loans : Value	Distribution of Loans : Clients
Arrears	25,700	6,300	83,400	2%	2%
Lender Refusal	25,700	5,600	82,200	8%	8%
Repayment Difficulty	27,300	7,000	102,500	34%	27%
Expenditure >75% Income	22,300	800	89,000	34%	32%
Remainder	30,200	13,600	60,400	22%	31%

- The first three segments recognise that they have debt repayment problems and should, therefore, be considered to be 'over-indebted';
- Those other borrowers whose committed expenditures (household, utilities and loan) are greater than 75% have not directly acknowledged repayment pressures. Against such high levels of committed income, and consequent low levels of net disposable income (particularly amongst the lower income segments), it may be suggested that a proportion of these borrowers will also be 'over-indebted' but have not acknowledged this - and would be unable to respond to exceptional payment needs or adverse events in their lives.

- Attachment 2 outlines a process of risk categorisation which identifies the integration of the quantitative dimensions of expenditure as a % of income with the qualitative attitudes of individual borrowers to a range of factors of the impact of debt. This suggests that, after loan repayments, only 10% of all borrowers demonstrate a basis for confidence of their financial situation (see also Q & A 4.4 for a comparison of risk categorisation between Kyrgyzstan and Bosnia and Herzegovina).

- The risk categorisation shows the dramatic impact of the level of loan repayments / leverage upon the risk profile of borrowers:

Distribution of Borrowers (see attachment 2.)		Affordable	Concerned	Vulnerable	Exposed
MFI	Pre loan payment	33 %	21 %	35 %	11 %
	Post loan payment	10 %	5 %	34 %	51 %
Bank	Pre loan payment	33 %	24 %	32 %	11 %
	Post loan payment	9 %	5 %	27 %	59 %

  - The impact of the loan repayments is to increase significantly the level of committed expenditures as a percentage of income, thereby leaving less budgetary surplus to meet other payment needs and other irregular (and unexpected) costs.

- Because of the particularly high leverage ratios on the lower income borrowers, the risk categorisation (based on income segments) highlights the greater delicacy of their financial situation:

Distribution of Borrowers (see attachment 2.)	Affordable	Concerned	Vulnerable	Exposed
Pre Loan Repayment				
< 15,000	21%	21%	42%	16%
15,001 - 20,000	31%	15%	40%	13%
20,001 - 30,000	40%	25%	28%	7%
30,001 - 40,000	41%	21%	32%	7%
> 40,000	50%	28%	17%	6%
Post Loan Repayment				
< 15,000	2%	1%	20%	77%
15,001 - 20,000	5%	2%	34%	59%
20,001 - 30,000	14%	7%	38%	41%
30,001 - 40,000	15%	5%	42%	38%
> 40,000	20%	14%	27%	39%

  - The impact of high loan repayment leverage is demonstrated by the transition levels of the risk categorisation of loan portfolios before, and after, the cost of loan repayment;
  - This is most starkly shown in the lowest income segments (representing 53% of borrowers);
  - This highlights the significant social implications which arise from the indebtedness of this sector and the potential impact of, even modest, changes in the strategy and practice of lenders to these clients.

4.2 Which factors contribute to over-indebtedness amongst borrowers?

Leverage of loan repayments for certain borrower segments is high – borrowers have different risk appetites and confidence to manage their financial commitments – only 10% have both strong financial capacity and confidence in their financial situation.

- The levels of spending on domestic essentials (excluding utilities) is largely up to about 50% of income, and is similar for borrowers of both MFIs and banks:

Distribution of Borrowers	Household expenditure as % of Income : MFI			Household expenditure as % of Income : Bank		
	< 25%	26-50%	> 50%	< 25%	26-50%	> 50%
< 15,000	6%	56%	38%	3%	51%	46%
15,001 - 20,000	16%	60%	24%	16%	59%	24%
20,001 - 30,000	20%	60%	20%	20%	57%	24%
30,001 - 40,000	29%	47%	24%	30%	46%	24%
> 40,000	45%	43%	12%	39%	45%	16%

  - This table suggests that there may be some opportunity for budgetary economies to be achieved by the mid-range income segments (affecting about 20-25% of those borrower groups);
  - However, the higher impact of basic living costs upon the lowest income segment is again clear and emphasises further their vulnerability to any adverse changes in the real cost-of-living;
  - The earlier analysis identified that low income borrowers are spending much less than the national estimate for household essentials and this limits the potential for further budget economies by the lowest income group.

- This commitment of basic regular expenditures is further reflected in the range of loan payments in relation to income.

Distribution of Borrowers	Loan repayments as % of Income : MFI			Loan repayments as % of Income : Bank		
	< 20%	21-30%	> 30%	< 20%	21-30%	> 30%
< 15,000	26%	20%	54%	19%	17%	64%
15,001 - 20,000	40%	32%	28%	30%	27%	43%
20,001 - 30,000	63%	15%	22%	45%	19%	36%
30,001 - 40,000	61%	26%	23%	43%	17%	40%
> 40,000	60%	17%	23%	39%	16%	45%

  - This table highlights the higher financial exposure of the loan support being provided to lower income segments;
  - Together with the underlying greater proportion of income required for basic living needs, these two tables highlight the challenges and pressures of financial inclusion of marginal income / credit clients.

- The relative scale of loan repayments is shown strongly in relation to net disposable income and the residual levels of net disposable income:

	MFI			Bank		
	Net Income (pre loan) KGS	Loan repayment as % of net income	Net income (post loan) KGS	Net Income (pre loan) KGS	Loan repayment as % of net income	Net income (post loan) KGS
< 15,000	5,200	83%	900	5,300	99%	0
15,001 - 20,000	9,300	57%	4,000	9,500	74%	2,400
20,001 - 30,000	15,100	40%	9,100	14,800	56%	6,600
30,001 - 40,000	20,600	37%	13,000	20,900	56%	9,300
> 40,000	45,600	32%	31,100	49,600	48%	25,900

- o By contrast with the previous comparison of repayments with household income (the normal credit assessment methodology), this table highlights the disproportionate impact of basic household expenditures upon the lowest income segment – and thereby, the dramatically different impact of loan repayments upon those clients (which is otherwise somewhat distorted if considered only against household income).

- However, 'Problem Lending' cannot be linked exclusively to quantitative financial characteristics. Borrowers have a range of individual and different risk appetites, together with varying concerns about their capacity to manage debt;

- A process of risk categorisation is outlined in Attachment 2 which integrates the quantitative dimensions of financial capacity (expenditures (pre and post loan payments) as a percentage of income, with the qualitative dimensions of risk (based upon the responses to a range of questions reflecting the level of pressure being experienced by the borrower;
- The risk categorisation and the expenditure tables (above) highlight the interaction of factors in any assessment of 'over-indebtedness';

- As shown in Q & A 4.1 (above), the risk categorisation framework shows the dramatic impact of the level of loan repayments upon the risk profile of borrowers:

Distribution of Borrowers (see Attachment 2.)		Affordable	Concerned	Vulnerable	Exposed
MFI	Pre loan payment	33 %	21 %	35 %	11 %
	Post loan payment	10 %	5 %	34 %	51 %
Bank	Pre loan payment	33 %	24 %	32 %	11 %
	Post loan payment	9 %	5 %	27 %	59 %

- o The impact of the loan repayments is to increase significantly the level of committed expenditures as a percentage of income, thereby leaving less budgetary surplus to meet other payment needs and other periodic (and unexpected) costs.

- This distribution may be compared with that identified by borrowers in Bosnia and Herzegovina[11]

Distribution of Borrowers (see Attachment 2.)		Affordable	Concerned	Vulnerable	Exposed
MFI Pre loan	Kyrgyzstan	33 %	21 %	35 %	11 %
	B i H	36%	15%	26%	23%
Bank Pre loan	Kyrgyzstan	33 %	24 %	32 %	11 %
	B i H	39%	14%	26%	21%

  - The comparison of the structure of the risk profiles suggests a slightly favourable position across the borrowers in Kyrgyzstan, with a greater emphasis in Bosnia to the 'exposed' segment.

- However, the levels of loan repayments as a percentage of income are much higher in Kyrgyzstan than was reported in Bosnia and Herzegovina:

  - Kyrgyzstan MFI 26% Bank 34%
  - Bosnia and Herzegovina MFI 13% Bank 16%.

- The effect of these higher leverage ratios within Kyrgyzstan lending has a direct and substantive impact upon the structure and distribution of the comparative risk profiles.

Distribution of Borrowers (see Attachment 2.)		Affordable	Concerned	Vulnerable	Exposed
MFI Post loan	Kyrgyzstan	10 %	5 %	34 %	51 %
	B i H	20%	16%	24%	41%
Bank Post loan	Kyrgyzstan	9 %	5 %	27 %	59 %
	B i H	24%	11%	20%	44%

  - The level of repayments in Kyrgyzstan has caused a greater increase in the risk profile of the loan portfolios of both MFIs and banks;
  - The average repayment periods in Bosnia are longer and there has been a greater level of refinance / restructure of loan indebtedness.

- Whilst it is inappropriate to make disproportionate comparisons between quite different countries (with different economies, purchasing powers and different histories of the lending industries), it may be interesting to compare the impact of household essential and utility costs, and loan costs, in relation to available income.

[11] Risk Categorisation : Comparison of Kyrgyzstan and Bosnia and Herzegovina. The calculation of the quantitative assessment (expenditures as a percentage of income) were fully consistent in the risk analyses of both countries. There were some differences in the structure of the qualitative assessment. However, the core of this assessment was similar and it is not considered to have a material impact upon the conclusions being drawn in this review.

Income Ranges All Borrowers		Household & Utility Costs as % Income		Loan Repayment as % Income		Distribution of Clients	
Kyrgyzstan - KGS	BiH - BAM	Kyrgyz stan	BiH	Kyrgyz stan	BiH	Kyrgyzs tan	BiH
< 15,000 (<US$ 300)	< 1,000 (<US$700)	56%	67%	39%	23%	28%	26%
15,001 - 20,000 (US$300-400)	1,001 - 1,500 (US$700-1000)	51%	59%	32%	17%	25%	24%
20,001 - 30,000 (US$400-600)	1,501 - 2,000 (US$1000-1400)	45%	46%	26%	14%	27%	24%
30,001 - 40,000 (US$600-800)	2,001 - 2,500 (US$1400-1750)	44%	41%	26%	12%	9%	14%
> 40,000 (>US$800)	> 2,500 (>US$1750)	33%	34%	28%	11%	11%	12%

- o The distribution of clients in relation to the respective income bands is similar
- o The levels of domestic expenditure are similar at the higher levels of income;
- o However, the impact of loan costs upon the available net disposable income is significantly different.

- Whilst it is inappropriate to draw strong conclusions from two different countries, it is interesting, nonetheless, to note the similarity in household expenditures, as a percentage of available income. (In each country, the distribution of these income bands spans the average income – Kyrgyzstan: about KGS 21,000 per household; and Bosnia and Herzegovina: about BAM 1,650 per household.

  - o This suggests that borrowers in Kyrgyzstan do not create any systemic over-indebtedness as a result of their levels of domestic expenditure. This is based upon this broad comparison with Bosnia and Herzegovina. A separate analysis is shown below to identify the scale of those clients who appear to have disproportionate levels of domestic expenditure;
  - o This comparative analysis identifies quite different structures in the comparative loan product and lending propositions in the two countries. This will be considered (below) in relation to the potential opportunities for loan refinance for problem lending situations.

4.3 Why are loan arrears so low?

Strong financial support from informal lending and family / friends – self-help initiatives by the borrower and family by additional work and reductions of food expenditure

- Loan arrears relate to about 2% of clients (see also Q & A 4.5);

- The highest levels of loan arrears occur amongst clients in the following borrower sub-segments:

Segment	Sub-Segment	arrears % of sub-segment
• Loan Purpose	Property	5%
• Loan Type	Agricultural loan by MFI	5%
• Multiple lenders in last 2 years	MFI borrowers	5%
• Multiple lenders in last 2 years	Bank borrowers	5%
• Trade Sector	Unallocated	5%

- Borrowers undertake actions to enable loan repayments to be made:

	Loan from family or friends	Friends or family provided money to repay loan	Sale of a major asset	Reduced food expenditure to make loan repayments	Additional work to make loan repayments
Arrears	23%	29%	16%	47%	37%
Lender Refusal	21%	16%	6%	32%	32%
Repayment Difficulty	15%	19%	6%	32%	35%
Expenditure >75% Income	10%	7%	3%	19%	18%
Remainder	5%	6%	3%	20%	15%

  - Borrowers with problem repayments clearly make some significant actions in order to maintain their debt obligations and avoid loan arrears;
  - The strong support from family is evident but it may be suggested that the scale of this support will be limited because of the family's own commitments;
  - The level of actions which are being undertaken by family are less than the broad levels of 30-40% of borrowers who acknowledge that they have debt repayment problems.

- The levels of support of loans by family is greater in rural locations;

- Many borrowers may wish to borrow again and therefore need to maintain an acceptable history of credit performance:

	Loans improve the quality of life : Agree	More than two loans in the last two years	I need to continue to borrow to maintain how my family and I live : Agree	Compared with 12 months ago, current loans are the same or higher	My household expenses have risen faster than income in the last 6 months : Agree
City : MFI	67%	39%	30%	63%	50%
City : Bank	66%	40%	26%	60%	47%
Rural : MFI	76%	51%	38%	66%	62%
Rural : Bank	82%	46%	37%	73%	69%
Urban : All	78%	45%	25%	47%	39%

  - The above table shows a substantive underlying demand for a continuation of access to borrowing.

4.4 Do borrowers who move between lenders have a different risk profile?

Almost 25% of borrowers have used two or more lenders in the last two years – this client segment shows a higher risk profile (both MFIs and banks) than those clients who remain with a single lender.

- During the last two years, the movement between lenders by current borrowers is:
  - MFI 78% with single lender; 22% with two or more lenders
  - Bank 77% with single lender; 23% with two or more lenders

- The income, expenditure and borrowing profiles of these different borrower segments are shown in the following table:

  - This segmentation indicates that mobility between lenders (during the last two years) appears to be linked directly with a need for higher borrowings:

KGS	Income	Household and Utility Costs	Loan Repayments	Net Disposable Income	Outstanding Loan
MFI : One Lender	23,100	10,600	5,600	6,900	44,600
MFI : Two or more	25,800	10,800	7,700	7,300	75,900
Bank : One Lender	29,200	12,500	10,000	6,700	110,400
Bank : Two or more	31,800	13,300	11,200	7,300	161,600

- The basic risk characteristics of these segments shows the varying recognition of higher financial pressures being experienced by the 'multiple' segment:

Multiple lenders in the last two years	I borrowed too much	My loan repayments are more than I can afford	Debt repayments cause problems within my family	Reduced food expenditure to make loan repayments	Additional work to make loan repayments
MFI : One Lender	36%	31%	39%	21%	21%
MFI : Two or more	43%	38%	44%	34%	34%
Bank : One Lender	40%	36%	40%	24%	23%
Bank : Two or more	44%	32%	43%	36%	30%

  - The perception of repayment affordability by 'multiple' bank clients appears inconsistent with their other responses. This may suggest either a higher risk acceptance / tolerance by this segment, or a greater optimism.

- However, the profile based upon the risk categorisation profile suggests that there is little overall difference between the risk structure of 'single' and 'multiple' borrower segments – although, of course, the individual risk exposures (outstanding loan amount) of the 'multiple' clients is higher.

Distribution of Borrowers (see Attachment 2.)		Affordable	Concerned	Vulnerable	Exposed
MFI	Single lender	10%	5%	34%	51%
	Multiple lender	8%	8%	34%	51%
Bank	Single lender	10%	4%	27%	59%
	Multiple lender	6%	6%	30%	58%

  - *Risk categorisation is based upon an expenditure : income ratio including loan repayments*

4.5 Do borrowers with arrears show any particular characteristics?

Loan arrears is only 2% of borrowers – five client sub-segments show higher loan arrears of 5% - loan arrears clients have received relatively strong support from family and show higher use of informal lending sources.

- The overall level of loan arrears is low at 2% of borrowers (see also Q & A 4.3);

- Within this level of loan arrears the sub-segments of borrowers which show the highest level of loan arrears – all at 5% of borrowers:

% relates to proportion of clients within the sub-segment (italics)	Arrears with Utility Payments	Refinance, or consolidation of debts during the last 12 months	Refusal by lender for loan in last 12 months	My loan repayments are / were more than I can afford	Food expenditure has been reduced to make loan repayments	I (or my spouse) have taken additional work to make loan repayments
Loan Type *Agricultural Loan*	11%	16%	13%	26%	30%	25%
Loan Purpose : *Property*	4%	6%	9%	33%	31%	29%
Trade Sector : *Other*	0%	7%	13%	21%	20%	25%
Multiple Lender : *MFI Two or more*	7%	6%	10%	38%	34%	34%
Multiple Lender : *Bank Two or more*	7%	7%	13%	32%	36%	30%

- o Each of the multiple lender segments and the property segment represent about 11% of borrowers; the other two segments account each for only about 2% of borrowers;
- o At loan arrears of 4%, the major borrower sub-segments are : age (16-25); loan purpose (other business needs); and region (Bishkek).

- Those borrowers with 'recognised' loan problems show that they have already undertaken independent actions to generate funds to enable them (by implication) to either support their lifestyles or make loan repayments (or both):

% relates to proportion of clients within each segment	Loan from Friends or Family	Loan from Retailer	Friends or family provided money to repay my loan	Refinance, or consolidation of debts during the last 12 months	Food expenditure has been reduced to make loan repayments	I (or my spouse) have taken additional work to make loan repayments
Arrears	23%	10%	29%	27%	47%	37%
Lender Refusal	21%	16%	16%	7%	32%	32%
Repayment Difficulty	15%	7%	19%	4%	32%	35%
Expenditure >75% Income	10%	5%	7%	2%	19%	18%
Remainder	5%	4%	6%	2%	20%	15%

- o The level of arrears in Kyrgyzstan (2%) was much lower than in BiH (9%) but many of the debtor actions reflect very similar levels:

% relates to proportion of clients within each segment	Loan from Friends or Family	Loan from Retailer	Friends or family provided money to repay my loan	Refinance, or consolidation of debts during the last 12 months	Food expenditure has been reduced to make loan repayments	I (or my spouse) have taken additional work to make loan repayments
Kyrgyzstan	23%	10%	29%	27%	47%	37%
BiH	27%	17%	25% [12]	25%	49%	39%

- o The level of support from families seems to be reasonably strong and is, of course, dependent upon their own financial capacity (nonetheless this is probably a finite, and probably short-term, resource);

- o The budget improvement actions (food expenditure and additional work) for arrears clients are very similar to those undertaken in BiH.

4.6 Do borrowers who undertake loan refinance have particular characteristics?

Refinance of debt relates to only about 4% of borrowers – refinance occurs most frequently (not surprisingly) amongst those borrowers who recognise that they have debt

[12] BiH : Friends and Family provided funds to make loan repayment" : relates to payments under a guarantee

problems – an extension of repayment periods would have significant and favourable impact upon the budget position of many households which have repayment pressures.

- The level of refinance amongst all borrowers is low at 4%;

- The sub-segments of borrowers which report the highest level of loan refinance are shown in the following table. (The proportion of sub-segment refinance is shown after the segment description).

% (below) relates to proportion of refinance clients within the sub-segment (italics)	Loan Arrears	Utility Arrears	Refusal by lender for loan in last 12 months	My loan payments are more than I can afford	Food spending has been reduced to make loan repayment	I (or my spouse) have taken additional work to make loan repayment
Problem lending: *Arrears : **27%***	na	9%	43%	46%	47%	37%
Loan type : *Agricultural : **16%***	5%	11%	13%	26%	30%	25%
Trade Sector : ***10%*** *Building & Property*	4%	3%	15%	45%	24%	24%
Income Frequency: *Bank Other : **9%***	4%	2%	17%	42%	37%	38%
Loan Type : *Bank Group : **9%***	1%	9%	13%	39%	23%	25%

  - These 'refinance' borrowers show higher risk profile characteristics;

  - The overall level of refinance is the same in both MFIs and banks, and is minimal for the lowest income borrowers.

- Despite the low level of refinance arrangements amongst borrowers, certain borrower segments show characteristics which may suggest an opportunity to extend the use of refinance and improve debt affordability by the client. This may be initially related to those borrowers who recognise their financial difficulties and that "loan repayments are more than can be afforded".

  - Their net income (prior to loan repayments) is KGS 16,100, representing 60% of household income - compared with an overall average of KGS19,600 and 65% of income by borrowers with no immediate payment pressures;
  - Their average loan repayments as a percentage of income are 33%, compared with 20% for those clients who are confident about their financial situation
  - The average outstanding loan of 'problem' segment is KGS 102,500 over an average loan period of 22 months;

- If, for example, such 'problem' loans were restructured on a basis of repayments being 25% of household income – based on an acknowledgment that the borrower has recognised the problem situation and 80% of such situations have been with a single lender over the last two years:
  - Monthly loan repayments would reduce, on average, from KGS 9,100 to KGS 6,800;
  - The remaining period for repayment of outstanding indebtedness would increase from 11 months to 15 months;
  - The average net income (after loan costs) would increase by 32% from KGS 7,000 to KGS 9,300.

4.7 Which borrower segments show a higher risk profile?

Major risk segment differentiation occurs in [i] income range, [ii] income source, [iii] recognition / non-recognition of debt problems, and [iv] mobility between lenders – within these broad segments, borrower sub-segments with the highest risk characteristics involve uncertain income frequency, borrowers who have been refused a loan by a lender, agricultural loan products (not generic lending to agriculture), and borrowers who change lenders.

- The principal client segments can be dis-aggregated into sub-segments of borrowers;
- The broader borrower segments include regional, income, loan amount, problem loan repayment, age, trade sector, location, loan purpose, loan type, savings, multiple lenders, and income frequency. Each of these segments has between four and nine sub-segments;
- A range of financial, debt management, event and problem recognition characteristics may be identified to enable the highest and lowest risk profiles to be determined, based upon the survey responses in relation to:
  - Financial:
    - Loan arrears;
    - Utility arrears;
    - Loan repayment as a percentage of income;
    - Total committed expenditures (household, utility and loan) greater than 75% of income;
    - Net disposable income as a percentage of income.
  - Debt management:
    - Loan from family or friends;
    - Loans from retailers;
    - Loan refinance in last 12 months;
    - Level of loan applications in last 12 months;
    - Refusal by lender to approve loan application;
  - Event in last six months:
    - Loss of job;
    - Loss of job by spouse or partner;
    - Business activity was unsuccessful.
  - Problem debt recognition by the borrower:
    - Borrowed too much;
    - Loan repayments more than can be afforded;
    - Reduction in food expenditure to meet loan repayments;
    - Additional work undertaken to enable loan repayments.

- The segments with the highest composite risk exposures involved:
  - Income Frequency : Irregular and not 'own business' income ;
  - Loan type : Agricultural loans from both MFI and bank lenders;
  - Problem Repayment : Refusal by lenders for a loan;
  - Multiple lenders: bank borrowers using two or more lenders in the last two years.
- The segments with the lowest composite risk involved:
  - Income : Borrowers with incomes over KGS 30,000;
  - Income Frequency : MFI borrowers with regular monthly income – which overlaps with;
  - Trade Activity: Public Sector employees.

4.8 Are there differences in the credit profiles of those borrowers who have savings balances and those who do not?

About 70% of borrowers have no savings with a financial or informal savings organisation – savings with an informal savings institutions are used more extensively than with a formal financial institution – the risk profile is higher amongst those with no savings and those with savings with a financial institution.

- The levels of 'savers' amongst borrowers was:

	Savings with a Financial Institution	Other savings	Non-Savers
MFI	8%	28%	72%
Bank	8%	31%	66%

  - A comparison with Bosnia and Herzegovina identified that, in BiH, 27% of MFI clients and 38% of bank clients had savings with a savings institution;
  - There is, therefore, a substantial similarity between the financial behaviour across these two markets.

- The financial profile of 'savers' is shown in the following table:

Average for each segment KGS	Income	Household and Utility Costs	Loan Repayment	Net Disposable Income	Outstanding Loan
Savings : FI : Borrowers	32,200	13,000	10,000	9,200	95,100
Other Savings : MFI	25,500	11,400	6,300	7,800	53,500
No Savings : MFI	23,000	10,300	6,100	6,600	50,900
Other Savings : Bank	31,700	13,300	10,700	7,700	135,800
No Savings : Bank	28,800	12,300	9,700	6,800	113,100

  - The 'other savers' show, on average, higher incomes (+10%), higher net disposable incomes (MFI +17%; bank +13%) and higher borrowings (MFI + 5%; bank +20%) in comparison with the 'non-savers'.

- Whilst savings are undertaken by a greater proportion of higher income households, the use of savings by lower income groups is not at substantially lower levels.

	Savings with a Financial Institution		Other Savings	
	MFI clients	Bank clients	MFI clients	Bank clients
< 15,000	7%	5%	25%	21%
15,001 - 20,000	9%	8%	27%	31%
20,001 - 30,000	8%	6%	29%	33%
30,001 - 40,000	9%	7%	33%	36%
> 40,000	15%	14%	33%	38%

  - The respective savings levels of MFI and bank clients are broadly consistent.

- The stronger financial / budgetary management which may be intuitively implied amongst the 'saver' segment is reflected in their attitudes towards indebtedness:

	I borrowed too much	My loan repayments are more than I can afford	Debt repayments cause problems within my family	Reduced food expenditure to make loan repayments	Additional work to make loan repayments
Savings : FI : Borrowers	42%	35%	38%	33%	29%
Other Savings : MFI	34%	25%	28%	24%	19%
No Savings : MFI	38%	35%	45%	24%	25%
Other Savings : Bank	36%	28%	29%	23%	14%
No Savings : Bank	44%	39%	46%	28%	30%

  - These responses demonstrate a marked difference in the attitudes of 'savers' and 'non-savers' to a greater level than may be inferred from the differences in the quantitative financial situation of each segment;
  - However, the responses of the smaller segment of those who have savings with a formal financial institution reveal higher risk attitudes which are more similar to those of 'non-savers'.

- These higher risk attitudes ('non-savers' and 'FI savers') are reflected in other indicators of financial pressure:

	Informal Loans		Friends or family provided money to repay my loan	I lost my job	My spouse / partner lost his/her job
	Friends or family	Retail shop			
Savings : FI : Borrowers	12%	3%	14%	10%	12%
Other Savings : MFI	6%	3%	12%	9%	10%
No Savings : MFI	11%	8%	10%	7%	9%
Other Savings : Bank	9%	4%	7%	4%	6%
No Savings : Bank	16%	9%	13%	7%	10%

- These responses again suggest that 'other saver' segments are generally more self-reliant in their budgetary situation than the non-savers;
- Again, the 'FI savers' appear to show a higher risk profile than the 'other savers'.

- This apparent anomaly with the 'FI saver' segment is also reflected in their attitudes towards the reputation of the lending institutions (a divergence which is greater than has been identified by other segmentation analyses).

  - The following table includes, additionally, the perceptions of non-borrowers. These may be consider to reflect popular opinion which may be influenced by media comment or the observations of friends in general conversation.

	Lending institutions act with integrity	Lending institutions are trustworthy	Lending institutions seek to improve the lives of their clients	Lending institutions understand customers' needs	The institutions respond well to people with lending problems
Savings : FI : Borrowers	76%	78%	72%	75%	63%
Other Savings : MFI	79%	85%	76%	83%	74%
No Savings : MFI	83%	89%	80%	82%	74%
Other Savings : Bank	86%	86%	77%	85%	74%
No Savings : Bank	82%	85%	77%	77%	72%
Non-Borrowers	77%	77%	68%	77%	69%

- This table provides some interesting shades of contrasting opinion.
  - Those 'FI savers' have a lower opinion of the lending institutions which is broadly similar to that of 'non-borrowers':
    - The terms of such savings are not identified by the survey but the adverse risk profile of this segment suggests that these savings may be a part of wider client / lender negotiation;
    - The incidence of 'FI Savers' is much higher in city locations (about 10% of borrowers) and this may reflect a greater ease of access to branches, in comparison to urban and rural (about 4%).
  - The attitudes of 'MFI Other Saver' are generally lower than those of the non-savers. Does this suggest that this segment reflects its greater financial confidence by having higher expectations of the lending institutions;
  - However, the balance of such attitudes amongst MFI clients is reversed by the opinions of bank borrowers.

- The use of 'other savings' varies slightly across locations in which rural (both MFI and bank) show about 33%, whilst in the city locations only 26% of MFI clients are 'savers' compared with 30% of bank clients.

- Those ‘former borrowers’ who continue to borrow have a higher level of savings than those who do not (see also Q & A 2.8):

	Former MFI Borrowers		Former Bank Borrowers	
	Bank Borrower	Non-Borrower	MFI Borrower	Non-Borrower
Savings with a financial institution	9%	10%	27%	12%
Other savings	46%	28%	45%	38%
Insurance product(s) from financial institution	5%	3%	14%	1%

  - This is a further indication of the apparently stronger financial position of those clients (particularly former MFI) who continue to borrow.

5 OUTLOOK FOR BORROWING

5.1 What is the outlook for borrowing demand?

60-70% of borrowers have positive attitudes towards borrowing and their loan experience – only 15-20% have higher outstanding debt than a year ago – decisions upon future borrowing are taken at, or about, the maturity of the current loan – certain borrowers segments ([i] repayment difficulty, [ii] expenditure over 75% of income, [iii] financially confident) are likely to have different needs and attitudes as loans mature – product and service propositions will need to recognise, and respond, to such differentiated positions.

- The pattern of loan purpose suggests that about 50% of loans are used for on-going, recurring needs, with the remainder being primarily for some particular (asset finance) purpose.

	Asset acquisition : Business	Asset acquisition : Domestic	Other Business needs	Other Domestic	Property
MFI	26%	25%	13%	31%	9%
Commercial Bank	25%	21%	16%	30%	13%

  - This suggests that the ‘asset’ segment of borrowers will need to make a deliberate decision of their future needs at, or near to, the time of the maturity of the loan.

- About 60-70% of borrowers appear to have positive attitudes towards their loan, whilst 30-40% of borrowers feel some reservation / uncertainty of their experience of borrowing. The following table is based upon the level of positive responses.

  - Comparison is shown with responses to the same questions from the recent survey of borrowers in Bosnia and Herzegovina.

	Loans improve the quality of life : *Agree*	Debt repayments cause problems within my family : *Disagree*	My loan repayments are more than I can afford : *Disagree*	Compared with 12 months ago your present total loans are : *Same or Higher*	After the next 12 months, do you expect your debt level to be : *Lower*
MFI	71%	60%	68%	63%	77%
Commercial Bank	72%	59%	65%	63%	79%
For comparison : Response from Bosnia and Herzegovina					
MFI	62%	82%	83%	51%	89%
Commercial Bank	70%	83%	85%	53%	84%

- The uncertainty of most borrowers of the amount of their debt over the next 12 months indicates the low level of even medium-term financial planning, other than the reduction of current debt by the existing repayments schedules.
  - The outlook by borrowers for their future loan needs is similar for both 'savers' and 'non-savers';
  - Similarly, other than those with arrears, the perception of repayment problems by borrowers does not create a different outlook from other segments;
  - 'Own business' clients do not reflect a greater recognition of future borrowing requirements than the employed consumer sector – this may suggest a low level of business or financial planning.

- The adverse attitudes of about 30-40% of borrowers towards their loan experience, although it may be considered that financial necessity will result in a continuation of such borrowings;
- The low levels of arrears suggests that borrowers are striving to maintain their formal credit performance records despite the scale of underlying financial pressures which are shown by other Q & A reviews.

- The high level of debt leverage in relation to the impact of loan payments upon net disposable income, and a significant majority being 'non-savers', result in the large majority of borrowers having low (or minimal) levels of available funds to move out of a debt-based budget, without significant revisions to their lifestyles. Similarly, there appears to be limited scope for a majority for borrowers to increase the level of debt repayment without a corresponding increase in income. (The capacity for budget reductions has been discussed in Q&As 1.4 and 2.1).

  - Both MFIs and banks show similar high levels of committed expenditure amongst their borrowers.

Total expenditures as % of Income	<25%	26-50%	51-75%	76-100%	>100%
MFI	2%	14%	35%	34%	15%
Bank	2%	12%	29%	38%	20%

- The constraint upon the affordability / capacity for additional expenditures is particularly severe amongst the lowest income groups. The borrowers from the MFIs will, therefore, be most constrained in their capacity to increase debt levels.

Total expenditures as % of Income	<25%	26-50%	51-75%	76-100%	>100%	Distribution of Loans : Client
< 15,000	0%	3%	21%	43%	33%	28%
15,001 - 20,000	0%	7%	36%	41%	16%	25%
20,001 - 30,000	0%	21%	39%	30%	9%	27%
30,001 - 40,000	1%	18%	43%	29%	9%	9%
> 40,000	7%	27%	27%	29%	10%	11%

- In response to a direct question on the expected level of borrowing after the next 12 months, the large majority (over 75%) anticipate their borrowings to be less, and just under half of these anticipate their borrowings to be 'much less'
  - Such 'optimism' has been seen in other countries and it probably reflects a perception of current repayments, rather than a longer-term financial planning strategy. It does suggest, however, that the majority of loan decisions are made at, or approaching, the maturity of the current loan.

- The following table seeks to relate these different dynamics to the distribution of borrowers, based upon their perceived risk profile (see also Q & A 2.3). It provides a framework to dis-aggregate the potential borrowing needs and capacities of client segments with different risk characteristics. This is not, of course, a forecast of lending volumes, and relates only to the current financial position of existing clients. There is no reflection of any events which may impact upon their future actions for borrowing, nor of any changes in their economic situation.

	Distribution		Net Disposable Income (post Loan Payment) KGS	% of clients with more than one loan in last 2 years	Loan Purpose				
					Business		Domestic		
	Loan Value	Clients			Asset Acq'n	Other	Asset Acq'n	Other	Property
Arrears	2%	2%	6,300	67%	18%	27%	18%	23%	22%
Lender Refusal	8%	8%	5,600	40%	23%	15%	21%	37%	8%
Repayment Difficulty	34%	27%	7,000	41%	29%	15%	25%	30%	11%
Expenditure >75% Income	34%	32%	750	43%	24%	14%	21%	32%	12%
Remainder	22%	31%	13,600	39%	26%	15%	24%	28%	10%

  - *'Arrears'* this segment clearly has severe repayment problems, together with relatively high levels of informal debt. The repayment period of current outstanding debt, based upon current contractual repayment levels, is about 10 months. However, in view of the arrears and the other informal debts of this segment, it may be anticipated that this borrowing will remaining outstanding, at reducing levels, for longer than the next 12 months. The adverse credit ratings arising from the arrears status may preclude further borrowings in the near future;

- *'Lender Refusal'* the incidence of 'lender refusal' suggests that this segment is likely to be of marginal credit quality. In addition to current direct borrowing, this segment also has an above average use of informal lending sources. This suggests there will be a continuing need for renewal at the maturity of current loans, which have an average residual repayment period of 11 months;

- *'Repayment Difficulty'* this segment recognises the pressure / constraint upon its financial / budgetary position. This will reflect not only the borrowings from the lending institution, but also informal loans which are at higher levels than the remaining two segments. However, the level of disposable income is relatively strong and the frequency of loans is about average. With about 50% of loan usage for asset acquisition, this may offer an opportunity for some borrowers to not renew loans at maturity (which is again at an average residual repayment period of 11 months) – whilst the other borrowers may have a greater debt dependency and thereby need to renew their loans. Within this segment, only 63% of borrowers agree that 'loans have improved the quality of their lives'. This suggests that 40% may approach the maturity of their loan with some caution about renewal and gain the immediate benefits of increase monthly disposable income;

- *'Total expenditures greater than 75% of income'* this segment has a high commitment of current income to basic expenditures. The profile of borrowings is similar to the other segments and financial support from family is reasonably strong (10%). However, the residual net income is minimal. It may be anticipated that this segment will seek to renew its borrowings, but does not have the capacity to increase its debt level. About 75% of this segment consider that the loan improved the quality of their life. This supports an anticipation of a high level of renewal at loan maturity;

- *'Remainder'* this represents only 22% of loan value, but 31% of clients. There is, therefore, a higher volume of smaller credit decisions to be undertaken. This segment clearly has the greatest discretion for a more independent determination of future borrowing. With an average residual repayment period of 10 months, just over half of these loans will mature during the next year. This segment represents the strongest group of clients for development of the loan portfolio – but possibly such borrowers have a relatively cautious approach to their debt commitments. Nevertheless, over 80% of this segment agreed that the 'loan improved the quality of their life'. This suggests an underlying strength to the potential level of loan renewal;

- However, across the major segments about 60% of clients have had only one loan in the last 2 years, which implies that these are either first-time, or non-recurrent, borrowers, who not have established a debt-dependency in their domestic budget. For some, the loan maturity would enable the 'release' of the loan repayments into a significantly higher level of disposable income.

- This segmentation framework, as an outlook for lending, suggests :
    - Little scope for overall organic growth in the borrowings of current clients, with a greater probability of a 'bandwidth' of "level to slight reduction";
    - A critical dynamic revolves around the decisions of those 60% of first-time or non-recurrent borrowers as their loans come to maturity. This implies that the lending institutions will need to be able to identify, and focus upon, the particular needs and characteristics of the different segments of borrower;
    - An opportunity for the differentiation of client proposition from the possible wider use of 'refinance' amongst the 'repayment difficulty' segment; development of budget expenditure guidelines and/or slightly longer loan terms / lower monthly payments for the 'high expenditure' segment; and an asset financing product proposition for the 'remainder' which would resonate with borrowers who may be more cautious or risk averse.

5.2 What is the sensitivity of the borrowers' financial / budgetary position?

Overall, about 65-70% of income is committed to expenditures on household essential, utilities and loan repayments – 75% of lowest income clients (28% of all borrowers) have committed expenditures in excess of 75% of income – a 5% net increase in household expenditure would cause a significant and disproportionate erosion of the net disposable incomes of such low income households.

- During the previous six months, about 50% of borrowers considered that household expenses had risen faster than income;

- The earlier Q&A reviews have highlighted the high levels of leverage (committed expenditures in relation to income) amongst a majority of borrowers. The following tables provide an indication of the impact of a 5% increase in household expenditure (excluding utilities) upon the net disposable incomes of MFI and bank borrowers. (It assumes that all other budget factors [income, utility costs] remain unchanged.

    - MFI borrowers:

MFI Borrowers : Income Range	Net Disposable Income (after loan costs) : KGS		% of clients with committed expenditure > 75% of income		Distribution of borrowers
	Current expenditure	+5% in household expenditure	Current expenditure	+5% in household expenditure	
< 15,000	900	600	74%	77%	32%
15,001 - 20,000	4,000	3,600	52%	55%	27%
20,001 - 30,000	9,100	8,500	32%	34%	26%
30,001 - 40,000	13,000	12,300	26%	28%	8%
> 40,000	31,100	30,100	28%	29%	8%

    - The lowest income group show a 33% reduction in net disposable income. This is, of course, very substantial and must also be considered in the context that this affects 32% of MFI borrowers. The scale of budget impact upon other income segments is much less, ranging from 10% to 3%.
    - The share of outstanding loan balances attributable to the lowest income group is 21% of the total MFI lending. This represents a significant vulnerability in

relation to both the financial implications for the MFIs and also the social implications for the borrowers.

- Bank borrowers:

Bank Borrowers : Income Range	Net Disposable Income (after loan costs) : KGS		% of clients with committed expenditure > 75% of income		Distribution of borrowers
	Current expenditure	+5% in household expenditure	Current expenditure	+5% in household expenditure	
< 15,000	0	- (300)	81%	83%	22%
15,001 – 20,000	2,400	2,000	63%	66%	23%
20,001 – 30,000	6,600	6,000	47%	50%	29%
30,001 – 40,000	9,300	8,500	46%	48%	11%
> 40,000	25,900	24,800	46%	48%	15%

- Again the impact on the lowest income group is starkly shown. Whilst the relative size of this portfolio is less for the banks than the MFIs, it represents, nonetheless, 22% of the number of clients, but only 8% of outstanding loans. It is, therefore, the social implications of the vulnerability of this lending which is the greatest issue;

- It appears, therefore, to be important to maintain a continuing monitor of the expenditure levels of the respective 'average household cost' baskets which are applicable to the different income groups. These should be incorporated into the on-going credit assessment and approval process.

6 IMPACT OF BORROWING

6.1 What proportion of borrowers appear to have benefitted, or been adversely affected, by the loan experience?

About 60-70% of borrowers feel positively about the impact of borrowing on their lives (somewhat lower amongst bank group clients) – rural locations showed a stronger positive impact from borrowing (particularly amongst bank borrowers).

- About 60-70% of borrowers respond positively to the impact of borrowing on their lives:

% of borrowers --- *Care : some questions are phrased to reflect a negative position : all % show 'agree'*	Loans improve the quality of life : **Agree**	My financial situation has improved in the last 6 months : **Agree**	Debt repayments cause problems within my family : **Agree**	My loan repayments are more than I can afford : **Agree**	It is difficult to resolve debt problems with my lender : **Agree**
MFI	71%	73%	40%	32%	42%
Bank	72%	75%	41%	35%	44%

- The wider financial inclusion undertaken by the MFIs through the Group Loan product is reflected in higher levels of borrower satisfaction in comparison with bank clients – although this differential is not shown by the individual loan product.

Type of Loan Product - % of borrowers of the respective loan product *Care : some questions are phrased to reflect a negative position : all % show 'agree'*	Loans improve the quality of life : **Agree**	My financial situation has improved in the last 6 months : **Agree**	Debt repayments cause problems within my family : **Agree**	My loan repayments are more than I can afford : **Agree**	It is difficult to resolve debt problems with my lender : **Agree**
Group : MFI	72%	71%	42%	30%	43%
Group : Bank	61%	70%	41%	39%	50%
Individual : MFI	72%	76%	38%	32%	40%
Individual : Bank	74%	76%	40%	33%	43%

- The different responses of the group clients do not simply relate to lending practice :
  - Average MFI loans were KGS 48,400 compared with KGS 42,600 by the banks;
  - Loan repayments were lower for bank group clients : MFI 26% of income compared with 23% for bank clients;
  - Bank group clients had higher levels of domestic expenditure (KGS 10,300) than the MFI group clients (KGS 9,100) with the consequent direct impact on net disposable income (and thereby, probably, also on the feeling of well-being);
  - Bank group clients also had twice the levels of informal borrowing from family (19%) and retailers (12%) than was undertaken by MFI clients;
  - However, bank group clients had slightly higher household incomes (KGS 24,700) than MFI clients (KGS 22,800), which suggests that the MFI clients may have greater budgetary skills or disciplines.

- There is little difference in the impact of the loan across the range of incomes:

Income Segments - % of borrowers of the respective income segment	Loans improve the quality of life : **Agree**	My financial situation has improved in the last 6 months : **Agree**	Debt repayments cause problems within my family : **Agree**	My loan repayments are more than I can afford : **Agree**	It is difficult to resolve debt problems with my lender : **Agree**
< 15,000	69%	71%	47%	37%	50%
15,001 - 20,000	73%	76%	35%	30%	41%
20,001 - 30,000	71%	72%	36%	33%	42%
30,001 - 40,000	71%	74%	42%	30%	34%
> 40,000	67%	80%	41%	37%	40%

- However, clients in rural locations have experienced a stronger positive impact from borrowing than those in city and urban locations.

Location Segments - % of borrowers of the respective location	Loans improve the quality of life : **Agree**	My financial situation has improved in the last 6 months : **Agree**	Debt repayments cause problems within my family : **Agree**	My loan repayments are more than I can afford : **Agree**	It is difficult to resolve debt problems with my lender : **Agree**
City : MFI	67%	72%	36%	28%	39%
City : Bank	66%	74%	35%	28%	40%
Rural : MFI	76%	75%	47%	43%	46%
Rural : Bank	82%	75%	52%	49%	51%
Urban : All	78%	75%	42%	32%	54%

- The rural responses show some challenging contrasts;
- The beneficial impacts of the loan are recognised;
- However, despite such benefits, the loans cause greater problems in rural locations;
- This suggests that the 'real' impact of the benefit of the loan must be even greater in such rural locations for the borrowers to remain positive and to 'see through' the difficulties and still recognise the benefits being derived from the loan;
- It may be noted that such an apparently paradoxical situation is felt most strongly by the bank clients.

- This perception of the impact of borrowing may be compared between Kyrgyzstan and BiH:

Location Segments - % of borrowers of the respective location	Loans improve the quality of life : **Agree**	My financial situation has improved in the last 6 months : **Agree**	Debt repayments cause problems within my family : **Agree**	My loan repayments are more than I can afford : **Agree**	It is difficult to resolve debt problems with my lender : **Agree**
MFI : Kyrgyzstan	71%	73%	40%	32%	42%
MFI : BiH	62%	37%	18%	17%	65%
Bank : Kyrgyzstan	72%	75%	42%	35%	44%
Bank : BiH	70%	43%	17%	15%	64%

- These responses provide an interesting, additional perspective to the Kyrgyzstan borrower comments:
  - Despite a stronger underlying improvement in their financial situation, the Kyrgyzstan borrowers appear to have greater concerns in relation to their indebtedness – or does this reflect a lower risk appetite?;
  - However, loan leverage ratios are much higher in Kyrgyzstan and, therefore, the real impact of debt upon the life of the borrower may be proportionately greater;

    - The higher level of loan arrears in BiH, despite the overall higher level of net disposable income (after loan repayments) [see Q & A 2.1], suggests that the repayment culture and relationship between lender and borrower may be more demanding in Kyrgyzstan than in BiH.

6.2 Do microfinance institutions stimulate greater 'financial inclusion'?

MFIs show a greater inclusion of lower income clients and have a higher proportion of female clients than the bank portfolios – a greater proportion of MFI clients (compared with bank clients) perceive the MFIs to be more understanding and supportive of client needs.

- The survey responses indicate that the MFIs show a higher proportion of clients in those segments which are usually targeted for improved financial inclusion:
  - 56% of MFI clients are female, compared with 46% of bank clients:
    - This was reflected particularly in city locations in which females represented 59% of the client base, compared with 45% in the bank portfolios;
    - The differentiation was less in rural areas, in which females represented 50% of clients, compared with 47% in the bank portfolios
    - In BiH, 52% of MFI clients were female whilst in banks, females accounted for 49%.
  - Amongst the lowest income segment (up to KGS 15,000), 57% of borrowers were female, compared with 51% of the comparable bank segment:
    - In BiH, females were only 51% of the lowest income segment;
  - 32% of MFI clients had households income less than KGS 15,000, compared with 22% of bank clients – again, indicating the greater focus towards financial inclusion by the MFIs;
  - Within product delivery, 43% of MFI clients had group loans, compared with 9% of bank clients. Of these product users :
    - MFIs had again a greater proportion of female clients (64%) compared with 46% in comparable bank loans;
    - MFI clients had a lower household income (KGS 9,100), compared with KGS 10,300 by bank group loan users;
    - Such lower incomes may be reflected in the different pattern of savings by group clients – 23% of MFI clients had informal savings, compared with 33% of bank group clients.

- Again using 'group loan clients' as a 'proxy' group for those borrowers with greatest characteristics of the 'financial inclusion' target segment, it can be seen that they had a strong perception of the reputational characteristics of the lending institution.

Group Loan Clients % of borrowers who Agree	Clients are treated with respect	Lending institutions are trustworthy	Lending institutions act with integrity	Lending institutions understand customers' needs	Lending institutions seek to improve the lives of their clients
MFI	96%	87%	81%	81%	78%
Bank	99%	82%	83%	74%	69%

- This table suggests that whilst the business cultural performance is strong, the operational implementation is viewed with slightly greater caution.

7 LENDER / BORROWER RELATIONSHIP

7.1 What is the reputation of the lending institutions?

The cultural 'mores' of MFIs and banks is strongly and favourably perceived by clients – the large majority of clients believe that the lending institutions understand and support client needs – the perceptions of non-borrowers towards the reputation of the lending institutions are also strong.

- The reputation of the lending institutions was considered in relation to the perceptions of respondents of both cultural values and also operational performance;

- MFIs were regarded slightly more favourably than the banks:

All Borrowers % of respondents who Agree	Clients are treated with respect	Lending institutions are trustworthy	Lending institutions act with integrity	Lending institutions understand customers' needs	Lending institutions seek to improve the lives of their clients
Current : MFI	95%	87%	82%	82%	79%
Current : Bank	95%	85%	83%	79%	76%
Former[13] : MFI	93%	84%	83%	79%	73%
Former : Bank	95%	84%	82%	82%	75%
Non-Borrowers	94%	81%	77%	77%	68%

  - The perceived reputations of MFIs and banks are very similar;
  - The attitudes of former borrowers largely correspond with those of current borrowers, although there is some apparent greater caution amongst former MFI clients. Overall, however, these responses do not suggest that former clients leave with any significant adverse opinions. This suggests that the overall treatment of clients was perceived to be 'fair';
  - The attitudes of 'non-borrowers' are probably highly influenced by media comment and general public observations. These remain strong positive attitudes towards the lending institutions.

- It is not surprising that those clients with lending difficulties show a wider range of response.

[13] Former : This relates to those respondent who used to borrow from an MFI or bank, but have ceased to borrow from that type of lending institution

All Borrowers - % of respondents who Agree	Clients are treated with respect	Lending institutions are trustworthy	Lending institutions act with integrity	Lending institutions understand customers' needs	Lending institutions seek to improve the lives of their clients
Arrears	86%	59%	60%	65%	57%
Lender Refusal	87%	79%	70%	65%	63%
Repayment Difficulty	95%	83%	73%	71%	70%
Expenditure >75% Income	96%	88%	86%	85%	81%
Remainder	97%	93%	92%	89%	86%

- The responses consistently reflect the progressive change in the clients' financial position;
- Whilst the much greater caution of the most problematic segments (arrears and lender refusal) is not surprising, it may be noted, however, that there remains a majority of clients who maintain a positive reputational perception, despite the personal difficulties which they face.

- There were minimal differences between the attitudes of [i] the city and rural clients of the MFIs and banks, and [ii] both self-employed and regular employment clients, which suggest that the corporate values are well-promulgated within the respective institutions.

- Kyrgyzstan borrowers show a more favourable perception of the lending institutions than was reflected by the borrowers in BiH.

All Borrowers : % of respondents who Agree	Clients are treated with respect	Lending institutions are trustworthy	Lending institutions act with integrity	Lending institutions understand customers' needs	Lending institutions seek to improve the lives of their clients
MFI : Kyrgyzstan	95%	87%	82%	82%	79%
MFI : BiH	92%	72%	80%	67%	64%
Bank : Kyrgyzstan	95%	85%	83%	79%	76%
Bank : BiH	92%	72%	80%	61%	57%

- The responses in Kyrgyzstan are consistently stronger than those in BiH. This appears to reflect a favourable service and relationship proposition. However, there will undoubtedly be a range of influencing factors for further consideration which may include:
  - The rapid changes in microfinance in BiH over recent years;
  - The historic performance of the microfinance and banking sectors in BiH;
  - The experience of borrowers with the lending industry and the level of expectation which exists.

7.2 Do borrowers feel that the lender is providing clear information about the loan?

Strong acknowledgment that the terms of the loan are explained.

- There is a strong recognition that the terms of the loan are being explained. This is reflected by 95% of the borrowers of both MFIs and banks.

7.3 Do borrowers understand the terms of the loan?

Despite the strong recognition of 'loan explanation' by the lending institutions, a minority of clients seem to have not fully understood the implications, or are now adversely critical of those terms (particularly interest rates) - however, the majority of borrowers do appear to understand the loan terms.

- Whilst there is a strong acknowledgment that the lending institutions have explained the terms of the loan, 10% of respondents provided additional, unrequested comments on issues related to borrowing. Of these anecdotal observations, 50% criticised adversely the level of interest rates being charged on loans. This suggests that those borrowers may not have understood the interest rate cost – or alternatively, they may have ignored such facts at the time if their need for loan funds was particularly urgent.

- A further observation derived from the survey is that the respondents were highly consistent in their answers to the various questions, even when some were phrased positively, and others negatively. This suggests that most respondents are aware of their financial situation.

- It may be noted that the research agency undertaking the survey reported that the respondents were interested, and pleased, that such research was being undertaken. This suggests, again, that the majority of respondents are aware of their financial and budgetary environment.

7.4 Do lenders understand the borrower's financial position?

(See also Q & A 3.3 re "Do the survey responses indicate credit standards or criteria").

About 90% of clients indicate that there was a transparency of the borrower's financial situation and needs – about 30-40% of client responses suggest that the loan review process did not adequately identify the appropriate loan amount or repayment capacity / affordability – consequent debt repayment problems prove difficult to resolve for about 40% of clients.

- There appear to be indications from the responses that whilst a majority of borrowers perceive that the lenders have understood their borrowing needs and capacity, there is a sizeable minority for whom the adequacy of the loan application / loan review process appears to be less certain.

% of borrowers who Agree	When I drew my last loan, the lender knew what I could afford	Lending institutions understand customers' needs	Loans were easy to obtain	I borrowed too much	My loan repayments are more than I can afford	It is difficult to resolve debt problems with my lender
MFI	89%	82%	69%	37%	32%	42%
Bank	88%	79%	63%	41%	35%	44%

- This series of questions reflect a continuum in the borrowing process:

    i. There appears to be a high transparency in the information being provided, presumably in response to requests from the lending institution;
    ii. The lending institution appears positive in its discussions with the borrower;
    iii. The loan process is generally seen to be adequate. (Often, those borrowers who want the loans even more rapidly include those who are most desperate for the funds);
    iv. Despite the perceived transparency of information and understanding of needs, the loan amount is excessive for 35-40% of borrowers. This may relate to the amount being greater than the declared purpose, or the debt is too great a liability for the borrower – in either situation, this suggests that the loan evaluation process was less than adequate in those situations;
    v. Loan repayment pressures may, of course, occur from an unexpected event or change of circumstance. However, this level of repayment difficulty is much higher than the levels of 'adverse events' which are reported elsewhere. If the financial / budget information were correctly presented, this again suggests that the credit assessment process may have been overly optimistic of the borrower's capacity for repayment;
    vi. Against these inferences of the loan assessment process, the resolution process for problem situations appears to be strained.

- This series of responses may be related to the different segments of problem lending.

% of borrowers who Agree	When I drew my last loan, the lender knew what I could afford	Lending institutions understand customers' needs	Loans were easy to obtain	I borrowed too much	My loan repayments are more than I can afford	It is difficult to resolve debt problems with my lender
Arrears	74%	65%	51%	38%	46%	57%
Lender Refusal	87%	65%	44%	43%	39%	56%
Repayment Difficulty	93%	71%	65%	65%	100%	76%
Expenditure >75% Income	85%	85%	70%	26%	0%	27%
Remainder	88%	89%	71%	26%	0%	24%

    - These responses appear broadly consistent with the observations in the preceding bullet point;
    - The greater difficulty to obtain a loan by 'arrears' and 'lender refusal' suggests that their loan applications and personal situations were subject to greater scrutiny. However, the scale of these two segments is small and it may be more appropriate to consider the responses of those clients who recognise their difficulties with loan payments.

- This assessment of lender / borrower understanding may also be considered in relation to the location.

% of borrowers who Agree	When I drew my last loan, the lender knew what I could afford	Lending institutions understand customers' needs	Loans were easy to obtain	I borrowed too much	My loan repayments are more than I can afford	It is difficult to resolve debt problems with my lender
City : MFI	91%	82%	66%	32%	28%	39%
City : Bank	92%	78%	61%	34%	28%	40%
Rural : MFI	83%	81%	75%	48%	43%	46%
Rural : Bank	79%	81%	64%	52%	49%	51%
Urban : All	88%	82%	73%	48%	32%	54%

  - o The rural locations appear to suggest that it was easier for the borrowers to obtain loans whilst the underlying information was less fulsome than that in the cities;
  - o This is then reflected in a higher level of borrowing pressures.

- It may be useful to compare the responses in Kyrgyzstan with those of borrowers in BiH.

% of borrowers who Agree	When I drew my last loan, the lender knew what I could afford	Lending institutions understand customers' needs	Loans were easy to obtain	I borrow ed too much	My loan repayments are more than I can afford	It is difficult to resolve debt problems with my lender
MFI : Kyrgyzstan	89%	82%	69%	37%	32%	42%
MFI : BiH	93%	67%	66%	19%	17%	65%
Bank : Kyrgyzstan	88%	79%	63%	41%	35%	44%
Bank : BiH	94%	61%	63%	19%	15%	64%

  - o The higher leverage ratios in Kyrgyzstan are reflected in the responses of loan amount and repayments;
  - o The resolution of debt problems may be less clear. BiH has much higher arrears levels (for both loan and utility payments) and there may, therefore, be a different social attitude towards repayment, or different 'penalties' as a result of non-payment.

7.5 Can borrowers adequately resolve their financial problems with lending institutions?

(See also Q & A 4.3 "Why are arrears so low?")

About 40-45% borrowers find it difficult to resolve debt problems – similar levels in both MFIs and banks – significant differences across the regions – little difference across the trade sectors.

- About 43% of borrowers (similar levels in MFIs and banks) considered that it is difficult to resolve debt problems with their lenders;

- This varied significantly across the regions from only 25% in Osh City experiencing difficulties to 58% in the neighbouring Osh Oblast;

- The divergence was less extended across the range of income segments, from 34% in the higher income band (KGS 30,001-40,000) to 50% in the lowest income segment;

- Across the trade sectors, there was a consistent level of recognition of difficulties (at about 45-50%) with the exception of the service sector (34%);

- Against this directional attitude by borrowers that they can address their problems, the following table provides some indication of the mechanisms which are being used to alleviate financial pressures.

	Informal Loans		Friends or family provided money to repay my loan	Have you refinanced, or consolidated your debts during the last 12 months	Food expenditure has been reduced to make loan repayments	I (or my spouse) have taken additional work to make loan repayments
	Friends or family	Retail shop				
Arrears	23%	10%	29%	27%	47%	37%
Lender Refusal	21%	16%	16%	7%	32%	32%
Repayment Difficulty	15%	7%	19%	4%	32%	35%
Expenditure >75% Income	10%	5%	7%	2%	19%	18%
Remainder	5%	4%	6%	2%	20%	15%

  - This highlights the importance of the wider family as the principal source of 'lender of last resort';

  - It suggests that the borrower will seek to resolve repayment problems on a loan with external parties, rather than address, in the first instance, the problem with the lender;

  - This may suggest that the credit reference / rating process is strong and that the borrower will seek strongly to avoid any 'public' awareness of financial difficulties.

7.6 Do borrowers want support to address problem debt repayment situations?

Only about 30% of borrowers want support for discussion with their lenders – again, substantial variations across the regions.

- Only 29% of all borrowers wanted assistance to resolve debt problems with their lending institutions, and may be contrasted with the 43% of borrowers who recognised the difficulties to resolve problem debt.
  - This is a substantially different response from that in Bosnia and Herzegovina in which 67% of all borrowers wanted assistance (and this was a low level compared with 80+% in the two preceding years.

- This contrasting, and possibly anomalous, situation may be further exampled in the following tables:

% of borrowers who Agree	It is / was difficult to resolve debt problems with my lender	I would like help to resolve debt problems with my lending institution	% of borrowers who Agree	It is / was difficult to resolve debt problems with my lender	I would like help to resolve debt problems with my lending institution
Bishkek	47%	32%	< 15,000	50%	33%
Osh	25%	26%	15,001 - 20,000	41%	28%
Chui Oblast	37%	17%	20,001 - 30,000	42%	26%
Jalal-Abad	48%	16%	30,001 - 40,000	34%	23%
Osh Oblast	58%	53%	> 40,000	40%	30%

  - Further borrower segments show similar characteristics:

% of borrowers who Agree	It is / was difficult to resolve debt problems with my lender	I would like help to resolve debt problems with my lending institution	% of borrowers who Agree	It is / was difficult to resolve debt problems with my lender	I would like help to resolve debt problems with my lending institution
Arrears	57%	45%	MFI : One Lender	42%	26%
Lender Refusal	56%	36%	MFI : Two or more	42%	35%
Repayment Difficulty	76%	60%	Bank : One Lender	44%	29%
Expenditure >75% Income	27%	13%	Bank : Two or more	44%	33%
Remainder	24%	13%			

    - The higher levels of recognition of the need for assistance appear to be concentrated upon particular segments which have higher risk characteristics.

- It may be suggested that against a loan performance of low arrears and low refinance (despite the indications of underlying debt pressures), the lending institutions present a resolute requirement for repayments to be achieved. This does not appear to be translated by borrowers into a situation in which alternative debt restructure mechanisms can be established.
- By comparison and contrast, about 70% of borrowers in BiH would like assistance in resolving debt problems with lending institutions, against an overall average of about 30% in Kyrgyzstan.

Survey Structure

A survey was undertaken during late-September / October 2013 in which individuals were invited to respond to questions relating to their financial position, the extent of any indebtedness and their attitudes towards indebtedness.

The survey was undertaken and co-ordinated by a local research agency and was conducted in five regions.

Location	Total Number of Respondents	Number of Borrowers from Microfinance	Number of Borrowers from Banks	Non – Borrowers
Bishkek	800	350	300	156
Osh	800	349	322	150
Osh Oblast	800	389	300	150
Chui Oblast	800	353	300	153
Jalal-Abad	800	352	300	150
Total	4,000	1,793	1,522	759

Note: Certain respondents had loans with both a microfinance institution and a bank.

The basis of the survey process was:

- Random sample selection within each region with interviews in a wide spread of socio-economic locations and avoidance of any undue concentrations of particular workplaces or markets;
- Survey interviews undertaken on a face-to-face basis;
- Borrowing experience based on:
    - About 350 persons currently with a loan with a microfinance institution;
    - About 300 persons currently with a loan with a bank;
    - About 90 persons with no current loan, but who have borrowed in the last 2 years from either a microfinance institution or a bank;
    - About 60 persons who have never had a loan from either a microfinance institution or a bank.
- Approximately equal selection of male and female respondents;
- Age profiles were spread:
    - 18 – 40 years 60% of which, 60% up to 30 years, and 40% 31 – 40 years
    - Over 40 years 40% of which, 60% 41 – 50 years, and 40% over 50 years
- Employment activity involved :
    - Trade and retail to represent at least 30% of the sample in each location;
    - In rural locations, agriculture to represent at least 30% of the sample;
    - Remaining sample was based upon a random selection across remaining trading activities.
- The city / urban / rural samples were undertaken in:

Location	Bishkek	Osh City	Osh Oblast	Chui Oblast	Jalal-Abad
City	100 %	100 %	0 %	25 %	90 %
Urban			18 %	11 %	10 %
Rural			82 %	64 %	

A summary of the principal demographic characteristics (based on the above sample process) is set out in the attached table.

The objective of the survey was to examine the characteristics and debt capacity of individuals. It was designed to enable the characteristics of different segments of borrowers to be identified and reviewed. Each independent lending institution will have its individual mix of these segments within its loan portfolio.

Attachment 1b.

Principal Demographics of Survey Respondents

Age

Borrowers

	16-25	26-35	36-45	46-55	> 55
Borrowers : MFI	14%	29%	28%	22%	7%
Borrowers : Bank	11%	32%	29%	22%	6%
Non-Borrowers	14%	35%	23%	22%	6%

Location

Borrowers only	16-25	26-35	36-45	46-55	> 55
Bishkek	12%	27%	33%	23%	5%
Osh	19%	32%	24%	18%	7%
Chui Oblast	7%	24%	32%	27%	9%
Jalal-Abad	10%	39%	27%	19%	5%
Osh Oblast	14%	31%	26%	24%	6%

Number of Persons in the Household

Borrowers

	< 2	3	4	5	> 5
Borrowers : MFI	10%	19%	25%	24%	21%
Borrowers : Bank	11%	16%	26%	24%	24%
Non-Borrowers	13%	18%	29%	21%	19%

Location

Borrowers only	< 2	3	4	5	> 5
Bishkek	14%	22%	30%	20%	13%
Osh	8%	20%	26%	25%	20%
Chui Oblast	12%	20%	28%	20%	20%
Jalal-Abad	18%	17%	26%	22%	17%
Osh Oblast	2%	8%	18%	32%	40%

Source of Income

Borrowers

	From employer 1 or 2 weekly	From employer monthly	Income payments sometimes delayed	Occasional or irregular payments	Income from own business
Borrowers : MFI	6%	40%	4%	6%	50%
Borrowers : Bank	6%	38%	2%	7%	53%
Non-Borrowers	7%	43%	3%	9%	42%

Location

Borrowers only	From employer 1 or 2 weekly	From employer monthly	Income payments sometimes delayed	Occasional or irregular payments	Income from own business
Bishkek	11%	44%	1%	6%	43%
Osh	5%	42%	4%	5%	48%
Chui Oblast	3%	30%	2%	8%	66%
Jalal-Abad	3%	53%	1%	2%	48%
Osh Oblast	7%	30%	7%	10%	54%

Risk Categorisation

An Outline of the Objective and Methodology

An assessment of the financial capacities of microfinance clients should not be seen solely in relation to quantitative measures (such as arrears, or income ratios, or material assets) but may also be considered in conjunction with other more qualitative dimensions – because the client's propensity to repay is a combination of factors, both financial and attitudinal.

A basic segmentation may be undertaken, therefore, upon the quantitative assessment of debt affordability and the qualitative assessment of clients' sense of financial concern or vulnerability. This provides also some dimensions for the impact of 'financial inclusion'.

An evaluation of the financial concern / vulnerability can be established for each borrower from the responses to the various attitudinal questions, which can be compared with the level of expenditure (as a percentage of income) for that borrower.

In this assessment, the 'Vulnerability Score' is determined by the qualitative responses to the various questions in relation to the concern of the respondent about the debt, its impact and the intensity of the response. These are reflected as:

1. Low 'concern' score	No responses which show difficulty
2. Mid 'concern' score	Limited range of responses which show difficulty
3. High 'concern' score	More frequent responses which show difficulty

The range of questions / factors comprising the qualitative 'vulnerability / concern assessment comprise:

- Loan arrears;
- Utility arrears;
- Refinance of loan or refusal of a lender to approve a loan;
- Other 'informal' loans from family, retailer, employer or moneylender;
- Reduction in food expenditure or additional work to make loan repayments;
- Recognition that loan repayments are more than can be afforded;
- Adverse events in last six months affecting household earning capacity;
- Recognition that the borrower does not feel in control of financial situation;
- Recognition by the borrower that debt causes problems in the family;
- Recognition by the borrower that the financial position has not improved in the last six months.

The expenditure: income ratio is based upon the quantitative responses provided by the respective clients.

This enables the spread / scatter of individual client responses and positions to be plotted in the following matrix.

Chart 1. Expenditures include household and utilities and excluding loan repayments

Chart 2. Expenditures include household, utilities and including loan repayments

This enables the creation of a matrix to provide some segmentation of the severity of risk amongst this group.

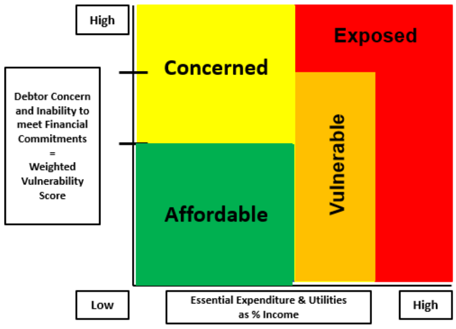

Chart 3. Client risk matrix

Such a matrix enables a broad differentiation between those clients who have possibly an unnecessarily high concerns for their repayment capacity / financial position but low expenditure commitments (these may be described as the "concerned" segments) in contrast to those with low levels of concern but whose financial position appears to be highly strained. The principle is to establish the interaction of both budget and attitude in the clients' behaviour and for this to be reflected in the management of client portfolios.

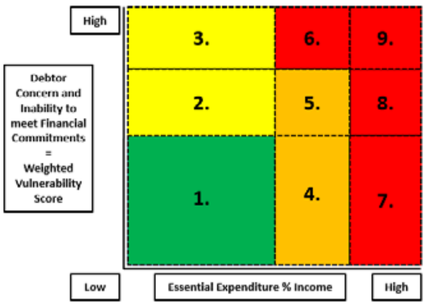

Chart 4. Segmentation of client risk and vulnerability

Such a distribution demonstrates that the management of the lending portfolios requires an understanding of the different client segments and that appropriate measures are available to address the differentiated needs and motivations of clients who are, or feel to be, experiencing financial and repayment pressures.

It is appropriate, therefore, to disaggregate the risk matrix (see charts 1 and 2 above) into different segments (charts 3 and 4 above) and identify the potential characteristics and risk management needs related to each.

The above analysis focuses upon the clients' perception of concern / vulnerability in relation to their immediate budgetary cash flow pressures. Such segmentation of the varying attitudes towards risk and budgetary capacity will enable the establishment of a differentiated approach towards risk management and client development, and thereby more effective levels of client service and support – rather than the overly blunt mechanisms of an undifferentiated approach by the lending institution towards those clients with repayment difficulties or financial concerns.

The risk matrix provides, therefore, a broad segmentation of clients into a differentiated risk framework. This combines a range of factors and enables the traditional credit risk assessment of independent criteria to be complemented by a portfolio approach combining both quantitative and qualitative dimensions of the client.

Survey Questionnaire

CLIENT SURVEY - INDIVIDUAL

We would like to better understand about how you undertake loan repayments.
All responses will remain confidential

1-2 Loan Identification *(All Respondents)*

Do you have loans with :	Yes, loan for personal needs	Yes, loan for business	Not now, but in last 2 years	Never	If Yes, how many
Q.1 Microfinance institution					Q.1.a
Q.2 Commercial bank (loan), excl. house purchase and credit card					Q.2.a

3-8 Please tell us about yourself : *(All Respondents)*

Q.3 Gender : Male ☐ Female ☐ Q.4 Age : ☐☐

Q.5 Number of people in household (inc. respondent) ☐☐ Q.6 Number of dependents ☐☐

Q.7 Marital Status Married ☐ Single ☐ With Partner ☐ Widow/Widower ☐

Q.8 Where do you live : City / Town ☐ Urban ☐ Rural ☐

9-12 Income *(All Respondents)*

What is the source of your income : *(Tick any which apply)*

Q.9 Regular work ☐ Irregular work ☐ Own Business ☐ Remittance ☐ Other ☐ None ☐

Q.10 In what type(s) of trade activity do you earn your income *(Tick any which apply)*

Manufacture ☐ Food Production ☐ Retail ☐ Engineering ☐ Building - Property ☐

Service ☐ Agriculture ☐ Public Sector ☐ Other ☐

Q.11 How would you describe the receipt of your income *(Tick any which apply)* From employer 1 or 2 weekly ☐ From employer monthly ☐ Income payments sometimes delayed ☐ Occasional or irregular payments ☐ Income from own business ☐

Q.12 How many people earn income in your household *(Please enter number)* ☐☐

13-22 Household Budget *(All Respondents)*

Q.13 How much is the average **total monthly** income into your household budge *(Please enter amount)* KGS ☐☐☐☐☐☐

Q.14 How much do you spend **each month** (on average) on food and household expenditure KGS ☐☐☐☐☐☐

Q.15 How much do you spend **each month** (on average) on gas, electricity, water, rent, garbage collection KGS ☐☐☐☐☐☐

Q.16 Do you have any payment arrears with any of electricity, gas, water, or housing costs Yes ☐ No ☐

Do you have other loans with :	Yes, loan outstanding	Not now, but in last 2 years	Never
Q.17 House purchase / property loan			
Q.18 Friends or family			
Q.19 Retail shop			
Q.20 Moneylender or Pawnshop			
Q.21 Employer			
Q.22 Credit Card			

23-35 Lifestyle ***{All Respondents}***

Did any of the the following situations happen to you in the last six months *(Please tick all which apply)*

		Yes	No			Yes	No
Q.23	I lost my job			**Q.24**	My business was not successful		
Q.25	My spouse / partner lost his/her job			**Q.26**	I had to sell a major asset to repay a loan		
Q.27	Major illness of self or family			**Q.28**	Family or friends provided money to repay my loan		

We would like to know how much you agree with the following statements

		Strongly	Agree	Disagree	Strongly Disagree	Do Not Know / No Opinion
Q.29	My financial situation has improved in the last 6 months					
Q.30	I feel in control of my financial situation					
Q.31	My children will have a better life than me.					
Q.32	My household expenses have risen faster than income in the last 6 months					
Q.33	The quality of my life has improved in the last 12 months					
Q.34	I can afford to buy 'treats' for myself or my family					
Q.35	Most of my friends have difficulties meeting their domestic budget needs					

36-41 Loan Dimensions ***{Current and Former Borrowe*** Please tell us about your loan(s)

What type(s) of loan have you used in the last 2 years *(Please tick all which apply)*

Q.36	Microfinance institution	Group		Business		Individual	Agricultural		Other
Q.37	Commercial bank (excl. mortgage and credit card)	Group		Business		Individual	Agricultural		Other

Q.38 What was the main reason(s) for your last loan *(Mark up to two reasons)*

Asset acquisition - business	Asset acquisition - domestic	Other domestic	Property	Repay / replace existing loan	Business Needs

Q.39	During the last 2 years, how many loans have you taken from microfinance institutions and commercial banks	*Enter number*
Q.40	How many lenders have you used for these loans	*Enter number*
Q.41	How many guarantees have you given for debts which are still outstanding	*Enter number*

42-52 Loan Dimensions ***{Current Borrowers}*** Please tell us about your loan(s)

Q.42 Total amount outstanding of all loans **Q.43** How much is total **monthly** repayments for all loans (include MFIs, banks, house mortgage)

(Please enter KGS amounts for Q. 42 and Q.43)

		Yes	No
Q.44	Are any of your loans in arrears		
Q.45	Have you refinanced, or consolidated your debts during the last 12 months		
Q.46	Have you applied for a loan in the last 12 months		
Q.47	If 'yes', has any lender refused to lend to you		
Q.48	Have you received any formal legal action for debt non-repayment in the last 12 months		

Q.49	How long ago did you take out your last loan	Within 1 month	1 - 3 months	4 - 6 months	7 - 12 months	Over 12 months	Cannot remember
Q.50	Compared with 12 months ago your present total loans are	Much Higher	Higher	The Same	Less	Much Less	
Q.51	After the next 12 months, do you expect your debt level to be	Much Higher	Higher	The Same	Less	Much Less	
Q.52	Who undertakes the loans in your family	Only you	Only your spouse/partn er	Jointly	Both of you independently		

53-59 Lending Institution *(All Respondents)* When you think about lending institutions, how much do you agree with the following statements

		Strongly Agree	Agree	Disagree	Strongly Disagree	Do Not Know / No Opinion
Q.53	Clients are treated with respect					
Q.54	The institutions respond well to people with repayment problems					
Q.55	Lending institutions are trustworthy					
Q.56	Lending institutions seek to improve the lives of its clients					
Q.57	Lending institutions act with integrity					
Q.58	Lending institutions understand customers' needs					
Q.59	Lending institutions explain the terms and obligations of the loan					

60-72 We would like to know your opinion, and how much you agree with the following statem *(Current and Former Borrowers)*

		Strongly Agree	Agree	Disagree	Strongly Disagree	Do Not Know / No Opinion
Q.60	Loans improve the quality of life					
Q.61	When I took my last loan, the charges (interest and fees) were explained to me and I know how much I am paying					
Q.62	Loans were easy to obtain					
Q.63	I borrowed too much					
Q.64	It is / was difficult to resolve debt problems with lending institutions					
Q.65	Debt repayments cause problems within my family					
Q.66	My loan repayments are / were more than I can afford					
Q.67	I need / needed to continue to borrow to maintain how my family and I live					
Q.68	I would like help to resolve debt problems with my lending institution					
Q.69	It is better to borrow from only one institution, rather than to change lenders					
Q.70	When I drew my last loan, the lender knew what I could afford					

Q.71	Food expenditure has been reduced to make loan repayments	Yes		No	
Q.72	I (or my spouse) have taken additional work to make loan repayments	Yes		No	

73-75 We would like to know your attitudes towards saving. *(All Respondents)*

Q.73	Do you make savings with a financial institution	Yes		No	
Q.74	Do you make other regular cash savings	Yes		No	
Q.75	Have you bought an insurance product(s) from your financial institution	Yes		No	

76-77 From which institution(s) have you borrowed in the last *(Current and Former Borrowers)*

(Please tick all which apply)

Q.76 Microfinance Institution

Bai Tushum	
Finca	
FMCC	
Kompanion	
Mol Bulak	
Elet Capital	
ABN Credit	
Other	

Other': Please name institution :

Q. 77 Commercial Bank

UniCredit	
Kyrgyz Investment and Credit Bank	
Demir Kyrgyz International Bank	
Bank Ail	
BTA Bank	
Commercial Bank	
RSK Bank	
Other	

Other': Please name institution :

Thank you for participating in this survey - All answers will remain confidential

Comments, if any, made by respondent

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