CHALLENGES AND RISK OF MICROFINANCE SUSTAINABILITY AMID COVID-19 PANDEMIC CRISIS

Ali Saleh Alshebami*, King Faisal University
Varadarajan Rengarajan, Microfinance Consultant
Reza Widhar Pahlevi*, Universitas Amikom Yogyakarta
Jamaliah Said, Universiti Teknologi Mara
Wahyuni Rusliyana Sari *, Universitas Trisakti

ABSTRACT

At this moment, the Coronavirus disease (COVID-19) is omnipresence causing unabated morbidity and mortality globally. The current scenario portrays that the microfinance sector has been paralyzed in terms of the financial stress of the Microfinance Institutions (MFIs) and their clients, especially poor borrowers and micro-entrepreneurs. Contextually the twin problem in the battle against COVID-19 in this sector includes economic revival of the microfinance sector from liquidity crunch and survival of the actors from the economic and medical consequences of COVID-19. This phenomenon calls for policy measures for coping with the critical situation and revival of the microfinance sector.

Keywords: COVID 19 Pandemic, Economic Deprivation, Liquidity Crunch, Microenterprise-s, Microfinance Institutions (MFIs), Poverty
JEL Classifications: I1, I12, J28, K32

INTRODUCTION

Disasters in general, negatively affect the poor people's standard of living and lead them to more financial vulnerability and over-indebtedness. According to the records of the (World Bank, 2016), there are about 65 million people who have been forcibly displaced by factional conflicts, war, or natural disasters, and more than 90% of them are hosted by developing countries as cited in (Elzoghbi et al., 2017).

Presently, the whole world is suffering from the corona Virus that has heavily impacted the entire world and affected the poor segment of the world population. They have been affected because its effect becomes more than their instant health needs and it has stopped them from covering their most essential needs and led them to situations with a more acute form of economic and social vulnerability (Beinker, 2020).This reminds us of the Ebola West African crises that took place in the year 2014 resulting in an economic impact of more than $ 2.8 billion (Abed et al., 2017).

Ironically, COVID-19 affects human beings directly and the viral keeps spreading from one to one irrespective of demography and topography. It has multidimensional impacts on economy and human life (Di Mauro, 2020; Alam et al., 2020; Erken et al., 2020).Nevertheles-s, this cohort in the pyramid of poverty pyramid is identified more in the sector of microfinance. This section of individuals suffers most of both economic deficiency and health services. The current socio-economic scenario affected by the coronavirus and subsequent implementation of numerous lockdown measures related to prevention of the Covid19 spread among individuals shows that the sector of microfinance has been massively paralyzed in terms of financial stress due to liquidity crunch both from institutional and clients' perspective.

Currently, the global microfinance sector has a combined portfolio of about $124 billion in outstanding loans and about $80 billion in saving (Greta Bull, 2020). There are about 139.9 million borrowers where 80% are women and 65% are rural borrowers. They are being largely benefited from the services of Microfinance Institutions (MFIs). Due to the onslaught of COVID-19, the global community is facing a very difficult challenge of both saving the lives of millions of poor people and at the same time saving their livelihood.

The present study aims to investigate the challenges that MFIs are facing during the pandemic from institutional perspectives and to diagnose the energetic of social relations of the poor individuals in the battle against COVID-19 from MFI's clients' view, especially poor borrowers and micro-entrepreneurs. It will also attempt to provide a slew of recommendations for microfinance stakeholders in general, and toward ushering in a resilient ecosystem in the microfinance.

Impacts of COVID-19 on MFIs

Due to COVID-19, across the world, the MFIs are apprehended to be more vulnerable and be profoundly negatively impacted on multidimensional perspectives that are described below:

Operational Cost Increase

Due to lockdown measures, MFIs are likely to suffer in various ways. Since MFIs serve the poor segment in society, it would be more expensive for them to maintain social distance and all other health precautions and collect the instalments from all over the country. Moreover, their employees would expose themselves to a higher degree of infection risks (Toth, 2020).

Micro-Insurance Coverage Cost Increase

Micro-insurance is one of the most important services of MFIs. Micro-insurance plays a key role in the mitigation of the uncertainties and shocks faced by the borrowers. Therefore, due to COVID-19, massive infections and death might be inflicted upon their customers and clients. This would increase their normal insurance cost (Micro-insurance Network, 2020).

Liquidity Crisis Increase

Due to lockdown and related economic crisis, MFIs would not be able to collect regular instalments and in some countries, the government would restrict by postponing such collection by legislating laws and//or promulgating executive orders. Moreover, in many cases, clients would also be unable to pay their regular instalments. In the case of clients' death, the account would remain uncollected forever. As a result, MFIs would be forced to operate entirely from cash reserves which may not be adequate to continue the operation of the business for a long time leading to a severe liquidity crunch (Toth, 2020; Rozas, 2020).

Capital Crisis Increase

Due to the COVID-19, there would be a high international donor fund to shrink significantly. Moreover, due to the consequences of the COVID-19 pandemic, it is highly likely that fewer savings would generate and more savings withdrawal on the part of the clients would take place. Therefore, MFIs would face a higher risk of potential capital shortage. This would, in turn, cause a significant decline in the future outreach activities of MFIs. For example, Microfinance Institutions in India have lately slowed down the disbursements of new loans due to the coronavirus outbreak (Ray & Agarwal, 2020).

Impacts of COVID-19 on MFIs' Clients

From the perspective of MFIs' clients, the twin scourges, inflicted by COVID-19 include health vulnerability and economic deprivation. Both of these issues needs to be addressed simultaneously to ensure the survival of both people's lives and livelihood.

Health Burden Leading Financial Burden Increase

It is widely reported that a widespread COVID-19 outbreak is associated with many deaths or physical and mental health problems which would ultimately give rise to the huge financial burden of the MFIs' clients, especially those of the poor borrowers and micro-entrepreneurs (Panchal et al., 2020). Many borrowers with consumer credit contracts would face financial stress due to illness, or loss of employment or other incomes or all (Grierson, 2020).

Financial Distress Induce Credit Repayment Decrease

COVID-19 causes financial distress on the part of MFI's clients, especially poor borrowers and micro-entrepreneurs, who depend on day to day income which will lead them to be in trouble with their instalments. Once microfinance borrowers are unable to repay their regular payments, there is a possibility of their becoming loan defaulters. For example, 70% of the microfinance borrowers in Pakistan are now unable to repay their regular instalments to the MFIs due to the COVID-19 pandemic resulting in a precipitous fall in the repayment rates to as high as 34% (Malik et al., 2020).

Business Capital Losses

Microfinance borrowers have been financially and physically hurt by COVID-19. For example, the study reveals that 84% of households suffer a loss of income since the lockdown due to COVID-19 in India (Rao et al., 2020). Therefore, they may use their business capital for the regular basic livelihood, health, and household purposes. Thus, even after the pandemic is over, these micro-entrepreneurs will face a lack of capital as well as a high loan burden that may push them again under the vicious cycle of poverty.

DISCUSSIONS

At the time of the financial crisis of the 2010-11 periods, the microfinance sector was adversely affected due to various reasons, most importantly due to the high-interest rate charged by the MFIs and the scarce borrowing opportunities (Bella, 2011). Subsequently, the crisis was somehow managed the microfinance industry and thus survived through some regulatory measures taken by some governments. But in the case of the current COVID-19 induced crisis, the ultimate result remains largely uncertain.

As the target customers of the Microfinance sector in general, with more emphasis on the bottom tier of people who eke out a living through running micro-entrepreneurial activities, the impact of COVID-19 has not only devastated their livelihood but also pushed them into deeper financial stress that may lead to increase the suicide rate among them (Panchal et al., 2020; Grierson, 2020). As many of them are positioned around the marginal poverty level, a slight change in their way of living may affect the poverty level significantly. Now due to loss of businesses at the time of continuous lockdown resulting in deepening their poverty level and consuming their past accumulated savings. Due to poverty, poor living conditions, poor hygiene, and lack of awareness, it is very difficult to make them maintain social distancing, hand-washing, maintaining good nutrition, self-quarantines, and repay credit on time (Malik et al., 2020).

At the same time, once poor individuals are not able to carry out their income-generating activities, this would lead to their delinquency in payment. This will affect MFIs directly as

MFIs depend on the timely collection of tiny amounts to recycle their capital and lends them to new borrowers. If MFIs are not able to meet with poor clients and collect regular payments, this would create a new problem for them as they will not be able to meet their daily operational expenses as well as cannot increase outreach engagements. The delinquency phenomenon limits the MFIs operations, stops their lending process, increases their operating cost, enhances liquidity crises, pushes borrowers to withdraw their savings, and increases the MFIs debt levels (Toth, 2020; Rozas, 2020).

At the same time, it is highly likely that the flow of donor funds would shrink significantly as well as government and regulatory bodies will force them to postpone the collection of instalments for a certain period. That will further decrease the outreach activities increasing the overall poverty level of developing countries (Beinker, 2020; Greta Bull, 2020). Therefore, the COVID-19 pandemic is likely to lead to an increase in indebtedness at the microfinance client level and liquidity and capital fund crisis at the MFIs level.

RECOMMENDATIONS

To deal with the problems discussed above, first, it is needed to take care of disease and related health issues. The most effective way to address this challenge would be to put together a national task force comprising of technical medical and health care experts, administrative staff, social, political, and local community leaders. Moreover, an indigenous value-based knowledge management system is to be conceived for developing an effective information package as suggested by the World Health Organization (WHO), CDC, and the Johns Hopkins University of USA. MFIs and Non-Government Organizations (NGOs) in consultation with the local leaders and respectable persons may take steps for effectively disseminating the information related to health care necessary for coronavirus spread prevention.

It should be ensured that the MFIs' clients adopt all mandatory preventive norms for respiratory etiquette strictly in the battle against COVID-19. At the same time, the public health authorities also need to coordinate with MFI, NGO, SHG to encourage people's participation in the movement for adoption of preventive mandatory norms and repayment norms for both health and financial governance respectively at client households and institutional levels.

In the context of a severe liquidity crunch, the Apex financial institutions acting as the regulatory authority in the financial sector need to take into consideration Microfinance institutions refinancing with the help of institutional modes like Commercial banks and Non-Banking Financial Institutions (NBFC). The donor agencies should link the health issue and poverty issue together while addressing the Corona crisis. Governments should provide generous funding to MFIs to develop and design a social welfare-oriented bundle comprising of both non-financial and financial products that assist in mitigating the problems emanating the COVID-19 menace.

CONCLUSIONS

Due to the high vulnerability attached to micro finance borrowers, the Corona effect may likely inflict some additional limitations on the effective functioning of the whole MFIs and the entire microfinance sector. It is believed that the entire microfinance industry has been badly hit by this virus resulting in various negative financial and psychological effects on both MFIs and their poor borrowers. The long lockdown implementations have resulted in huge losses for the MFIs and made them suffer from a shortage of liquidity and escalated operating costs. It also hit the borrowers and forced them to remain at homes and close down their small business activities resulting in high delinquency and of being more loan defaulters. Donors, on the other hand, would reduce and/or discontinue their financial support to the MFIs and NGOs due to the situation following the Corona pandemic. Thus, we may also conclude that dealing with this crisis requires a joint effort by all microfinance industry stakeholders represented by MFIs, donors, governments, international bodies, insurance companies, borrowers, and all others involved.

Since the COVID-19 crisis is still an on-going phenomenon, it is difficult to anticipate the future consequences and estimate the actual damage or impact of this very difficult problem. Therefore, finally, we recommend further comprehensive studies of the problem in multiple countries and regions.

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