Tajikistan: 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 June 2016 to gain insights into the experience of borrowing by individuals in Tajikistan. 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.

A similar survey was undertaken in Tajikistan in 2014. Since that time, there have been significant global and national economic and market events which have impacted directly upon the borrowing clients in Tajikistan. The structure of the surveys enables comparative assessments of the 2014 and 2016 situations in relation to the quantitative and qualitative dimensions of the financial and social impact of debt upon the lifestyle of borrowers.

Similar studies have been undertaken in a range of other countries, most recently in Azerbaijan (currently in course), Kyrgyzstan and Bosnia and Herzegovina. This range of countries enables some comparative assessment to provide an additional perspective and validation to the findings.

This paper provides four sections:

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

Borrowers are under much increased difficulties from debt obligations, reflecting both repayment problems and social pressures. The quality of the loan portfolio (at institution and industry levels) is highly vulnerable to adverse trends in economic activity, price inflation, and wage levels. Borrowers face an increasingly adverse impact of debt on their families and lifestyle and this poses a structural behavioural risk to loan performance. The strategy and governance of the lending institutions must assess the stability and sensitivity of lending performance in relation to the developing structural risk exposures since 2014.

Income and Expenditure

- Structural redistribution of loan portfolios towards higher income borrowers;
- Increased levels of job loss amongst borrowers and spouses;
- Improvement in net disposable income due primarily to constrained food expenditure and lower loan repayments … but …;
- Strong increase in households with greater pressures on domestic budget.

Borrowing

- Structural redistribution of loan portfolios towards more loans at lower outstanding amounts;
- Slow-down in new / renewal loans in 6 months of January – June 2016;
- Significant reduction in number of foreign currency loans, but high value loans remain with high arrears;
- Collateralised loans have higher balances and higher repayment arrears.

Affordability

- 80% of borrowers have committed expenditures (domestic essentials and loan) more than 75% of income;
- Net disposable income (after loan costs) inadequate to meet price inflation, primarily in non-foodstuffs;
- Increased reliance upon informal loans by borrowers to maintain loan payments and living costs;
- Significant sensitivity of affordability to any significant increase in cost of food or household essentials.

Risk Exposure

- Sharp increase in loan arrears to 15% of borrowers - and 60% of borrowers with loan repayment problems;
- Increase in levels of ‘own business’ failures and loss of employment;
- ‘Own business’ and ‘foreign currency’ loan portfolios show greatest credit risk and loan arrears;
- High sensitivity and vulnerability to continuing inflation and low economic growth.

Microfinance Institutions and Banks

- Stronger operational risk management, but under pressure from portfolio and structural risk exposures;
- Similar changes in lending structure and credit performance by MFIs and banks;
- Similar demographic profiles of borrowers in both microfinance institutions and banks;
- Higher loan balances and leverage amongst bank borrowers than MFIs.

Impact of Borrowing

- Substantial increase in the recognition by borrowers of problems arising from debt commitments;
- Increasing social impact of debt on family and wider financial and health strains in the community;
- Increased perception of debt dependency to maintain lifestyle of self and family;
- Increased recognition of need for assistance to deal with financial problems.

Key Issues Arising

- Significant vulnerability in loan profiles requires operational, portfolio and strategic risk management;
- 'Own business' segment requires focused strategy to address particular financial and social challenges;
- Loan product and service propositions need to be aligned to the usage of the funds and client needs;
- 'Responsible finance' by both lenders and borrowers requires a more focused use of financial services.

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

SUMMARY OBSERVATIONS

Financial Inclusion

Both MFIs and banks reduced their exposure to the lowest income segment during 2014-2016.The scope of financial inclusion remains broadly consistent across both types of institution.

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 income profiles of borrowers with MFIs and banks are broadly similar. There has been an upward redistribution of the loan portfolios towards higher incomes, greater than can be attributed to the national increase in wages. However, the 2014 survey showed that the lowest income segments had particular budget pressures – and the reduction in loan exposure may be considered to reflect a prudent lending strategy (albeit resulting in the exclusion of some clients;
- Income levels for female borrowers were consistently lower than those for males across city, urban and rural locations. Average loan amounts reflected this income difference, although female borrowers showed comparable access to higher value loans. Female borrowers showed no indication of feeling to be excluded from the target client-base of the lending institutions;
- Lending institutions were strongly recognised (96%) to treat clients with respect. However, the 2016 survey showed some reductions in the borrowers' perceptions of integrity, trustworthiness and responsiveness by lending institutions.

However, the financial pressures upon borrowers have increased substantially since 2014. Reduction in food expenditure and informal borrowings from friends / family appear to be primary mechanisms for many to enable some measure of domestic budget management and sustain loan repayments.

The adverse impact of high leverage upon the highly financially-marginal low income borrowers was highlighted in the 2014 survey review, but the 2016 review shows that this has been substantially reduced.

Over-indebtedness

Increased pressures on the domestic budget are reflected in a significant increase in loan arrears, higher recognition of difficulty in making loan repayments and greater reliance upon informal loans from friends and family. Financial pressures are resulting in greater social and family problems.

Whilst there is a wide debate upon the definition of 'over-indebtedness', this review assesses over-indebtedness as:

- "The extent to which a borrower is adversely affected by the interaction of the quantitative dimensions of loan repayment(s) upon his/her financial position and the qualitative dimensions of the impact of debt upon the financial confidence, risk vulnerability and the lifestyle of the borrower and dependents".

On the basis of this definition, the 2016 Survey shows a significant deterioration in the levels of over-indebtedness amongst individual borrowers in Tajikistan. The down-turns in both the quantitative credit performance measures and the qualitative dimensions of the impact of, and attitudes towards, debt reflect a increasing range of borrowers for whom current debt commitments are excessive in relation to available income.

In the 2014 Survey, 3% of borrowers had loan arrears and 29% considered that their loan repayments were more than could be afforded – by 2016, these levels had increased to 15% with loan arrears and 50% who acknowledged their repayment difficulties. The impact of such financial pressures impacts upon the lifestyle and society of the borrower. Increased levels of family problems, informal loans and guarantees from friends, wider financial pressure in the community and a reduction in the perceived impact of loan on the quality of life are strong and adverse trends demonstrated by borrowers in their 2016 responses in relation to the impact of loans on their lives.

This presents a sombre background. A majority of borrowers face the future in which [i] 55% had existing committed expenditures (food, household essential, utilities and loan payments) which were more than 75% of income (unchanged from 2014, despite the upward shift in income distribution; [ii] 50% (2014 – 29%) recognised that loan repayments are more than can be afforded; [iii] 80% (2014 - 48%) consider that they need to borrow to maintain their lifestyle; and [iv] despite the on-going need for debt finance, 52% (2014 – 29%) want help to resolve debt problems with their lender.

Unless there is a significant improvement in the real levels of disposable income, the current levels of debt obligations present a fundamental strategic challenge to the lending institutions, in which the established structures of loan products, operational credit criteria and strategic risk exposure need to be re-assessed.

Lender / Borrower Relationship

The reputation of lending institutions by borrowers remains strong, although the strength of this has declined since 2014. Borrowers continue to demonstrate a strong commitment to their debt obligations, despite increasing financial pressures, which may reflect an expectation of a continuing availability of loans.

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.

The additional financial and social pressures on borrowers appear to be reflected in reductions in the perceived levels of the integrity, trustworthiness and responsiveness of lending institutions. The 2014 survey showed these dimensions to be extremely strong (95+% of borrowers) and, whilst reduced in 2016, the responses of both current and former borrowers remain strong (at about 80-90%). This is, therefore, a positive endorsement of the lending institutions. Borrowers feel strongly that continuing debt is necessary to maintain their lifestyles; however, lending levels are lower in January-June 2016; if the anticipation of future borrowing is reduced by a change in lending strategy and practice, this may impact adversely upon the reputation of the lending institutions. This may be considered to be a strategic risk.

The responses indicate that the lending institutions have continued to support the borrowers by refinance (albeit still at low levels), infrequent forced sale of assets and responsiveness to the particular problems of foreign currency debt. However, if the short and medium term economic and employment outlook remains constrained, it seems probable that the scale of lending problems will increase and the options for many borrowers to cope with the increasing financial pressures will reduce. In such a scenario, the lending institutions will need to have developed short and medium term strategies to address the operational credit management of borrowers.

The survey responses do not show any clear attribution of ‘blame’ for the increased current pressures which many borrowers face. However, borrowers (90%) indicate that the lending institution had a good understanding of the financial position at the time of the loan, which implies an ability to assess affordability – but an increasing proportion of borrowers now recognise that they ‘borrowed too much’ (35%), have ‘difficulty to make loan repayments’ (50%), and have ‘difficulty to resolve problems with their lender’ (39%).

Key decisions will need to be made in relation to the scale and purpose of new/renewal lending, the practicality and realisable value of collateral assets, and the practicality of the enforcement of guarantee liabilities. The strategy for dealing with such issues is likely to impact directly upon the ‘reputation’ of the lending institutions and the ‘sense of hope and fairness’ amongst many borrowers that a ‘way forward’ can be established.

Impact of Lending on Borrowers

Fewer borrowers perceive that loans contribute to the quality of life, but more borrowers perceive a dependency on debt to maintain the lifestyle of their family. A significant reduction in the level of loan availability may be anticipated to impact immediately, and adversely, upon the ‘hope’ of the borrower for the lifestyle of the family.

Borrowers show a contrasting trend between the impact of loans upon the quality of their life (down from 93% to 67% in 2016) and the greater recognition of debt dependency to maintain the lifestyle of the family (up from 48% to 80% in 2016). The impact of borrowing brings social implications with an increase in family problems as a result of debt increasing from 22% of borrowers in 2014 to 47%.

Despite the increased financial pressures and social impact of debt, borrowers have continued to display a high level of commitment and responsibility to their debt obligations. The increase in loan arrears is sharp (from 3% to 15%), but this needs to be considered in wider context of actions taken by borrowers to maintain their loan payments – these have included [i] continued reductions to food expenditures by 40% of borrowers (over 50% by those recognising their repayment difficulties); [ii] increased informal loans by 30% of borrowers, primarily from friends and retailers (for domestic consumption); and [iv] increased guarantee support to/from friends to support loan obligations.

Borrowers show that debt and financial pressures have become an increased feature of society, with 77% of borrowers (2014 – 60%) recognising that “most of their friends have difficulties meeting their domestic budget needs”. Such wider recognition can ‘normalise’ these financial pressures and thereby affect the potential behaviour of borrowers

The impact of lending appears highly sensitive to the stability of the borrowers’ situation, the continuing availability of loan funds and the maintenance of ‘hope’, or optimism, for the future – and most of the key influences are outside the control of the individual borrower. Any significant erosion of such ‘hope’ may be regarded as a potentially significant ‘event risk’.

Social Impact of Borrowing

The growth in informal loans provides a short-term benefit to borrowers and the level of loan repayments. However, if such funds cannot be repaid or the ‘lender-friend’ feels dis-advantaged by providing such support, it could lead to social tensions within a community.

The impact of borrowing and over-indebtedness is not limited to the borrower and the immediate family and dependents. The 2016 survey shows:

- an increasing reliance upon informal loans from friends and family (particularly by those borrowers under greatest pressure);
- a sharp increase in the provision of guarantees to support the borrowings of friends and family;

- an increased level of budgetary pressure amongst the community and friends of the borrower;
- an increased level of informal credit from retailers, particularly by those borrowers under greatest pressure;
- an increased level of arrears with utility payments;
- increase in the incidence of family health problems (particularly amongst low income households).

These trends are being identified across the income ranges, although remain strong with the lower income segments.

There is, therefore, both a greater mutual inter-dependency for financial support within society and also a greater awareness (and thereby social normalisation) of debt pressures. This presents an impression of community support and solidarity. The borrower responses lead to the conclusion that such actions have enabled the loan performance to be sustained and, without which, the lending institutions would be facing higher levels of problem lending.

It does, however, pose some issues which may present social challenges and tensions. (The writer is not a sociologist, nor has experience of the Tajikistan culture, but raises these issues as a potential impact of 'over-indebtedness' outside the direct impact on the financial service industry).

- Debt and finance are often the cause of personal tensions. The extension of 'temporary' support into longer-term outstandings, and the potential inability to repay, could be a source of future tensions amongst the participants of informal lending;
- In the event of continued economic pressures, some of those who provided loans may require such monies for their own needs. If repayment is not available, then the informal lender will be disadvantaged and feel 'let down' by the borrower;
- The 'own business' retailer is dis-advantaging the cash-flow of the business by the provision of retail credit (with borrowers taking a cost overhead of the interest charged on loans). If the retail customer cannot repay such retail credit, this will impact on the viability of the 'own business' trading activity. Such retail credit is taken by both borrowers and non-borrowers and the scale is potentially significant for the 'own business' segment.

Client Segmentation

Certain borrower segments have been particularly 'hard-hit' by the economic and market pressures in 2014 – 2016. These involve the major segments of 'own business', foreign currency borrowers and public sector employees. Financial pressures are now being experienced across the income segments.

The individual borrower clients are not homogenous. The 2014 and 2016 surveys show the differences between the principal segments and the varying trends over the last two years.

A major concern in the 2014 survey related to the vulnerability and sensitivity of the lowest income segment. The particular issue related to loan repayments being based on a similar percentage of household income as was applied to higher incomes. This did not reflect the real costs of food and other essential costs (representing a greater proportion of income) and consequently resulted in disproportionate relationship between loan payments and net income. The lending institutions appear, by the 2016 survey, to have addressed this issue by a combination of reduced exposure to this segment of clients and lower loan amounts / repayments. This is a constructive and prudent approach towards responsible lending – and many of those former borrowers (now with no loan) have a much higher level of net disposable income than previously.

Foreign currency borrowers have faced substantial pressures during the last two as a result of the devaluation of the TJS Somoni against the US Dollar. The scale of such borrowers reduced to 7% (from 27%). This was achieved primarily by a reduction in the number of lower-value loans. The residual foreign currency loan portfolio show high risk characteristics – higher average loan amounts, high loan arrears (40%), high collateral (60+%), and strong recognition of repayment difficulties (65%). This remains a significant operational credit risk for both MFIs and banks, with exposures concentrated on a relatively few, high-loan-value borrowers – but highly sensitive to the external risks of the economy and exchange rates.

The 'own business' segment accounts for a substantial proportion[1] of loan value and has shown a significant deterioration in credit quality between 2014 and 2016. The level of business failures in this segment in the last 6 months has been about 40%, over 20% of borrowers are in arrears, 70% are in the retail sector. The particular characteristics and challenges of this client segment are reviewed in 'Issues for Consideration' (see below). This segment faces particular macro-/ micro-economic and local market challenges for its trading performance. It should be considered to be a high risk segment in relation to its impact on both the credit performance of the lending institution and also social performance of a community.

Public Sector employees represent about 50% of personal, non-business borrowers. This is a significant segment of borrowers. The income of this segment has been almost unchanged over the last 2 years. Whilst average loan levels and loan arrears are relatively low, the aggregate exposure of such a high number of borrowers (28% of clients and 15% of loan value) makes this a significant segment to the performance of the lending institutions.

Clients who move between MFIs and banks demonstrate a significantly higher risk profile, with higher levels of outstanding loan balance and loan arrears.

Operational Credit Management

Operational credit management has been tightened by the lending institutions during 2014 – 2016. Despite the higher level of loan arrears, many borrowers have taken actions to maintain loan repayments and thereby mask the scale of the financial problems.

A comparison of the profiles of the 2014 and 2016 surveys suggests that the lending institutions have undertaken a range of operational credit management initiatives. The responses of borrowers indicate that these actions (by both MFIs and banks) have included:

- Redistribution of the loan portfolio towards higher income clients;
- Alignment of the loan repayment ratio for the lowest income segments to reflect the impact of the costs of basic food and essentials upon the domestic budgets of this segments;
- Slowdown in the rate of new and/or renewal loans in the 6 month period of January – June 2016;
- Extension of loan repayment periods (for some borrowers) thereby creating increased net disposable income;

[1]Based on the 2016 Survey sample, 'own business' clients accounted for about 65% of outstanding loan value. The sample basis did **not** seek to establish a weighted profile of MFI and bank total loan portfolios. As such, the sample provides solely an indication of the potential scale and impact of the 'own business' segment upon total lending. The scale of loan exposure to the 'own business' segment will vary for each lending institution.

- Higher levels of loan refinance / rescheduling of loans, particularly in relation to those with loan arrears (although refinance levels remain low);
- Closer credit review of loan applications resulting in a higher level of 'loan refusals' by lenders – (but some of those borrowers have subsequently obtained loans from other lenders);
- Collateralised assets have remained at a broadly unchanged level (35% of borrowers) which suggests that the availability of this credit support may be saturated. However, there has been a significant increase in the number of guarantees being provided by borrowers (increasing from 35% to 90% of borrowers providing at least one guarantee).

These actions indicate that the lending institutions have undertaken a deliberate lending strategy to strengthen the operational credit structure of the loan portfolio and mitigate any destabilisation of the market.

Whilst loan arrears have increased to 15%, the level of repayments has been sustained by a range of actions by borrowers (in addition to normal income flows) which have included:

- Increased informal loans from friends and family;
- Continued reduction in food expenditures;
- Reduced discretionary spending on 'family treats'.

The fundamental uncertainty now rests with the balance between [i] the budget economies which have been made by borrowers, [ii] the scope for further cash liquidity support by informal loans, [iii] the comparative growth of wages and cost inflation and thereby, [iv] the capacity and willingness of the lending institutions to address, or tolerate, the potential portfolio and strategic risk exposures of global and national economic pressures.

Loans Collateralised by Pledged Assets

The level of collateralised loans remained broadly unchanged during 2014 – 2016, with property as the major asset. The lending institutions have increased substantially the level of personal guarantees to support borrowers, although many of such guarantees are from borrowers who are, themselves, experiencing financial pressures.

The proportion of borrowers providing collateralised assets to support lending has remained broadly unchanged between 2014 and 2016. This suggests that the availability of such asset support has been saturated.

The stability between 2014 and 2016 relates to both the number of borrowers (about 35%) and the value of outstanding loans (about 60%). The value of outstanding debt has been consistently and substantially higher amongst collateralised borrowers, than non-collateralised. This suggests that 'collateralisation' was a 'lead marketing' mechanism for higher value lending, rather than a defensive 'lag credit management' mechanism to support loan exposure.

The principal types of collateral assets were property (business 15% and residential 30%), domestic assets (16%) and gold / jewellery (13%). The types of collateral were similar for both MFIs and banks.

Collateralisation of assets to support a loan presents a fundamental dilemma to the lending institution. In the short term, it demonstrates an underlying value of the borrower – it provides a motivation as a result of the borrower not wishing to lose the assets or be forced to sell it – but, in the event of an incapacity to repay (due to lack of cash flow), the fundamental issue relates to the 'forced sale realisable value' of the asset.

The overwhelming majority of borrowers have lived in the same neighbourhood for many years. Any attempt to re-possess, or realise, assets would, therefore be a high profile action and may be anticipated to have an impact upon the reputation of the lending institution (not least when most members of the community "have difficulties meeting the domestic budget"). Furthermore, the 'forced sale' value of such assets would probably result in one member of the well-established community befitting from the failure of another. This is a challenging social situation. The strategy of the lending institutions towards the future actions in relation to collateralised assets may have significant implications not only for the amount-at-risk, but also as a public demonstration to borrowers of their resolve to take action.

Whilst the level of collateralised assets has remained unchanged, there has been a significant increase in the number of guarantees being provided by borrowers (presumably to support other borrowers). The profile of such guarantors is, therefore, the same as that of the borrowers – it appears to be simply borrowers guaranteeing each-other, in addition to obtaining informal loans from friends. It does not, therefore, appear to have any material favourable impact upon the quality of the loan credit. Whilst it provides the lender with an additional point(s) of recourse in the event of the inability of the prime borrower to make repayments, it appears that most of such guarantors are, themselves, facing significant financial constraints.

The financial value of a majority of such guarantees appears, therefore, to be questionable. The challenge for the lending institution relates to their operational processes in relation to any attempt to enforce such guarantees. The established communities would ensure that such actions would be highly visible, as with the realisation of collateralised assets. Again, as with collateralised assets, the strategy of the lending institutions may have significant reputational implications and also for the credibility of the guarantee commitment.

Loans in Foreign Currency

The risks of the mismatch of foreign currency debt and local currency income (shown in 2014) have been dramatically exposed by the devaluation of the TJS Somoni against the US Dollar. The number of currency loans has been substantially reduced since 2014 but the residual portfolio shows a severely high risk profile.

The 2014 survey identified the risks of the mismatch of foreign currency debt exposure with domestic currency income streams. The exchange rate turmoil which followed demonstrated the severe impact of such structural (rather than operational credit) risks.

Whilst the proportion of clients has reduced from 27% to 7%, of total borrowers (in the survey sample[2]) and the amount of outstanding loan value from 43% to 27% (again in the survey sample), the credit quality of the residual portfolio is severely pressured.

Asset collateral is high, being provided by 64% of clients (65% in property); 40% of loans are in arrears; 20% have informal loans from friends. As such, the risk characteristics are high and 55% of currency borrowers are in the 'own business' segment.

This appears to be a segment in which the work-out of the debt situation should be part of the medium-long-term strategy and structure of the lending institutions – and remains highly sensitive to external events, particularly in relation to the economy, local market liquidity and consumer demand levels.

[2] CARE: this relates **only** to the survey samples. It does not reflect a weighted national position. It may provide some indication of the scale of the change which has occurred but it does not imply that this is a robust representation of the whole portfolio.

Location

Significant differences between regions and city, urban and rural locations.

As was observed in 2014, there are considerable differences in the client income, expenditure and borrowing profiles across the regions. The lending institutions also appear to apply different strategies in the various regions.

This highlights the need for lending institutions to identify the different profiles and budgetary situations and establish appropriate lending guidelines and standards.

Outlook for Lending to Current Borrowers

The outlook appears sombre with a reduced 'feel good' mood amongst borrowers. Debt dependency has increased but the capacity of loan affordability has reduced. The demand for borrowing is closely aligned to domestic needs with 42% of usage for short-term needs. Unless there is a significant increase in real net disposable incomes, the loan product and service propositions need to be reviewed.

The current situation appears to be sombre. The borrowers have faced continuing and increasing austerity during the last two years, being impacted by the lower levels of economic growth, the inflationary pressures (particularly on non-food imported goods) resulting from the dramatic exchange rate devaluation, and the reduction in income from inward remittances. The pressures on the financial domestic budgets have increased and there has been an erosion of the 'feel good' factors which had been much stronger in 2014.

The lending institutions have responded by strengthening the conventional mechanisms of operational credit management and credit support, which were briefly outlined above. Borrowers have responded by further 'tightening of the domestic belt' by reductions in domestic expenditure.

The demand for continuing access to loans by borrowers has strengthened, reflecting a perception that debt is the only mechanism by which they can maintain their lifestyle. However, with 25% of loan funds being directly used for domestic consumption purposes (on fixed loan terms of about 18 months) and a significant proportion of each loan payment being taken by interest charges, this is unlikely to be a situation which can be sustained for any undue length of time. Furthermore, the 'own business' segment (primarily in the retail and service sectors) faces trading pressures unless there is a marked upturn in economic activity.

The outlook for future lending requires, therefore, the lending institutions to undertake a close strategic review and interaction of a product and service proposition which is focused towards client needs and capacity, together with a risk strategy which reflects the operational, portfolio and systemic exposures. This is reviewed further in the 'Issues for Consideration' section below.

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.

'Own Business'

The significance of the 'own business' segment has been indicated in the previous section. Such clients are the entrepreneurs who seek to generate economic value from the loans and contribute to the development of local economies. This segment accounts for a substantial proportion of outstanding loan value and is, therefore, an important dimension of the stability of the loan exposure of lending institutions.

During the period 2014 – 2016, there has been a significant deterioration in the credit quality of this segment – strong increase in loan arrears, high incidence of business failures, increased recognition of the difficulty in making loan repayments. The 'own business' segment is strongly concentrated in the retail and service sectors, which have generally low-entry, low-exit barriers.

These trading activities are also directly sensitive to the level of consumer demand and the cash liquidity in the local communities / economies. This has been adversely affected, in real terms, by the strong increase in price inflation (non-foodstuffs), the lower levels of inward remittances and, to a lesser extent, the slow-down in lending to individuals.

The constraints upon the liquidity of household budgets, and thereby purchasing capacity, is reflected in an increase in the level of informal credit being provided by retailers, particularly for domestic consumption expenditures. Whilst such 'retailer credit' supports the community and households and sustains nominal 'sales turnover', it does not provide sales cash flow. Such informal credit is, therefore, effectively funded by the 'own business' loan funds at a nominal interest cost of about 35-40% (about 75% APR). This is a substantial cost overhead and the extent to which this is incorporated in the sales price structure is not known. Lending to such 'own business' clients is, therefore, effectively lending (in part) to the end-consumer, rather than the trading activity itself. About 40-50% of lending to 'own business' is provided by standard 'individual loans', rather than 'business loans', which suggests that the lending institutions have not focused upon the particular needs / characteristics of such borrowers.

This is a complex situation. The dynamics of the 'own business' client performance reflect an interaction of the individual's business ability (operational credit), the quality of the business cash-flow from both trading and retailer credit (operational credit), the local market conditions with the in/outflow of competitors and trading terms of wholesalers and distributors (portfolio risk), and the external pressures of economic and inflationary changes (structural risk).The 'own business' segment of borrowers do not show any significant level of available cash savings by which to fund any adjustment in trading conditions.

The 'own business' segment appears to be, therefore, strategically important to the stability of the lending institutions but, in the current environment, extremely vulnerable and sensitive to a wide range of both controllable and external risk factors.

Issue: The 'own business' segment is both strategically and operationally important to the performance of the lending institution and the systemic risk performance of the industry. Whilst it is outside the scope of the 2016 Indebtedness Survey to determine the governance structure of lending portfolios, the management of this client segment represents an important dimension of the stability of the industry. The factors affecting the performance of the 'own business' segment are complex.

It is suggested that consideration be given to:

i. *focused management of the 'own business' segment, together with a detailed assessment of their needs and trading activities;*

ii. *appropriate skills within the loan officers to understand, identify, and respond to the trading and cash flow dynamics of 'own business' clients;*

iii. *development of an appropriate product and delivery structure which is aligned to the business needs and cash flow of 'own business' clients. (This may, for example, differentiate between the funding characteristics of informal retailer credit, realities of long-term repayment structures of foreign currency debt, and the funding of short-term seasonal fluctuations).*

Risk Structure

The earlier summary comments identify that, despite the actions to strengthen operational credit by both lending institutions and borrowers, the credit quality of the loan portfolio has deteriorated significantly between 2014 and 2016. The market faces continuing economic pressures and external reports (which are outside the experience of the writer) suggest that there is no immediate prospect of any return to the 'pre-devaluation', 'pre-economic crisis' situation.

The lending institutions face, therefore, three fundamental dimensions of risk management:

- Operational risk: relating to the credit quality and management of individual lending situations;
- Portfolio risk: relating to the structural risks which impact more greatly upon certain segments;
- Structural risk: relating to the systemic risks of external events which have widespread impact.

In a 'normal' trading environment, there would be a particular focus upon the demands of operational credit. The 2016 survey (and its comparison with 2014) indicates that these are, however, not 'normal' times and that the financial capacity and responsiveness of individuals is affected by a range of external factors which are outside their control (irrespective of their level of responsibility to meet their loan commitments – the usual dynamic of operational credit).

Such exogenous risks impact upon the 'portfolio risk' and 'structural risk' profiles of both the individual lending institutions and the lending industry. (It is outside the scope of this review to consider the balance sheet, capital and loan loss reserve implications of this exposure).

The 2016 survey demonstrates a deteriorating situation amongst borrowers with the colliding influences of domestic budgetary pressures, continuing austerity in lifestyles and outlook, increasing social pressures on the borrower and family and a reduced perception of the benefits of borrowing, but with borrowers unable to see a way forward without debt. Such factors erode the 'hope' of borrowers.

The structural exposure of 'systemic risk' relates to the assessment of the 'breaking-point' of these factors which would trigger a widespread change in borrower behaviour.

Issue: The 2016 Survey indicates that such wider risks present a significant challenge to the stability of lending performance of both an individual lending institution and the industry. These require risk management and governance structures which extend beyond that which controls operational risk management.

It is suggested that the lending institutions, the collective industry and other appropriate stakeholders consider:

i. the basis upon which such portfolio and structural risks are currently identified and managed, and the governance which surrounds such exposures in relation to institution and industry performance;

ii. the identification of scale and performance of the major lending portfolios and the sensitivity of these to a range of scenarios of 'external events and influences'.

Product and Service Focus

The delivery of lending to individuals is primarily undertaken by means of a fixed-term, fixed-repayment loan structure over a loan period of 12-18 months (but averaging about 18 months). The purpose of such lending (to non-own business clients) is primarily for domestic consumption expenditures and other domestic expenditures in relation to health and education. The usage of the funds is, therefore, mostly for a much shorter period than that for which the loan is outstanding.

The demand for borrowing is currently high, with over 75% of borrowers indicating that they need to continue to borrow to maintain the lifestyle of the family. However, over 50% of borrowers also recognise that current loan repayments are more than can be afforded.

This presents a fundamental dilemma which does not appear to be sustainable over the medium-term. This challenge was highlighted in the 2014 survey review of the affordability pressures – and the trends over the last 2 years in the financial performance and attitudes of borrowers have demonstrated their vulnerability to adverse events and their limited capacity to respond (other than by increased deprivation of their lifestyles and food consumption).

The borrowing of individuals (other than 'own business') appears to involve primarily the use of funds for [i] short-term domestic consumption, [ii] 'family support' in relation to health and/or education, and [iii] property (either acquisition or improvement). The roles of lending and/or other financial mechanisms for these three generic needs are very different. However, the same loan product (individual fixed-term loan) is principally used for all these needs. The cash-flows, usage periods and budgetary impacts are different and seldom aligned to the product structure (unless by some coincidence). However, the fixed-term, fixed-repayment loan structure provides possibly the most cost-effective and operationally-efficient delivery proposition for the lending institutions.

Issue: The development of the lending markets has led to a relatively high saturation of potential clients. Whilst lending growth within an expanding market against a relatively stable economic background has been achieved by the use of a principal fixed-term loan product, the limitations and inefficiencies of such a loan product are highlighted by the current market conditions.

It is suggested that the lending institutions should assess if the dominant 'driver' of the product and delivery proposition should be the operational and cost efficiencies – or if the strategic development of the institution and industry is best served by the alignment of financial products and services to the driver of client need and capacity.

Financial Inclusion and Responsible Finance

The continuing economic and market conditions, both global and national, which have affected Tajikistan since 2014, are reflected in the increased financial and social pressures identified by the 2016 survey of 'Borrowing by Individuals'.

The impact of 'Responsible Finance' may be considered in relation to [i] Responsible Finance', [ii] Responsible Lending', and [iii] Responsible Borrowing'.(In the following sections, a suggested definition is set out in italics in view of the range of interpretations, the writer has set out the basis of comments in relation to the 2014 and 2016 surveys).

Responsible Finance: *«From the financial institution: The provision of financial services (both product and service) which are appropriate to provide a balance between the commercial performance of the institution and the needs of the recipient client and which provide a positive contribution to the client's financial well-being.*

From the client: The realistic understanding of the likely income and expenditure cash flows in the near and medium term and to seek financial services which are commensurate with such anticipated cash flows and the usage of loan funds."

The previous 'issues for consideration' identified that the greater maturity of the market and needs of the client require a progressive development of the product and services. If the provision of loan finance is perceived as simply a mechanism of providing a commodity, cash, then it may be difficult to determine the benefits of the loan as being attributable to the services of the lending institution.

The greater financial inclusion of clients will inevitably result in many clients having inadequate experience of financial products to understand the risks, opportunities or appropriateness of the products. The 2016 survey highlighted that borrowers were using products which they perceived as appropriate, but the usage of the loan funds was inconsistent. The financial institutions will need to consider the scope of their responsibility in the provision of appropriate services, which may not include lending for some client segments or expenditure purposes.

Issue: Lending institutions need to consider the alignment of their mission and strategy in relation to their client service and product propositions. This will enable clarification of the driver of the business strategy, together with the balance between a 'product / transaction'-led market approach and a client relationship.

Responsible Lending: *"The provision of loan finance, by appropriate product structures and on clearly understandable terms, for the betterment of the client for which repayment can be undertaken from identified and adequate cash flow sources, and which will not cause inappropriate financial pressure or budgetary strictures upon the borrower or his/her dependents"*

The balance of 'responsible lending' and 'prudent and commercial management' presents a challenging dichotomy for the governance and management of the lending institution. The survey responses demonstrate a range of situations in which a 'client-driven' definition of 'responsible lending' is challenged by 'commercial drivers' for the credit strength of the loan portfolio and the financial performance and stability of the institution.

The competition between such driving factors is exampled below, based upon the survey responses of borrowers.

- For those institutions with US Dollar-based funding, foreign currency lending improved the balance sheet currency match … but the exchange rate risk exposure was transferred to the borrower with largely un-matched TJS income streams;

- Collateralised assets supported the credit approval of higher-value loan exposure at higher leverage ratios … but the debt exposure resulted in a more vulnerable financial position for the borrower;
- Fixed-term, fixed repayment loans provide a cost efficient mechanism for loan delivery and operational control … but such loan structure is often inconsistent with the usage of the loan funds and, for 'own business borrowers, the cash flow of the trading activity;
- Increased requirement for personal guarantees to support lending may improve the apparent credit quality of the loan … but the value of such guarantees is highly uncertain as many are from financially-pressured borrowers and add to the level of debt liability;
- Lending levels have reduced in the 6 months to June 2016 (presumably in reflection of credit standards) … but 'former borrowers' (80%) have a strong perceived need to borrow to maintain their lifestyle and reduced access to loan funds removes that 'hope' or optimism;
- Loan interest charges are high (at 35-40% pa nominal) and this may be required to cover the operating and capital costs of the lending institution … but at such levels, these rates have a very high 'real' cost – in which for the lowest income borrowers, the interest portion of the monthly repayment is broadly equivalent to the cost of food and household essentials for one person for a month;
- The level of loan arrears (albeit increased to 15% in the 2016 survey) may present a favourable position of credit performance in comparison to the underlying (and 'unseen') level of 'over-indebtedness … but many borrowers experienced significant reductions to their lifestyle to enable repayments and maintain a 'credit record' to support loan renewal;
- The structural credit strength of loan portfolios may have been improved by an upward redistribution towards higher income borrowers … but this causes the exclusion of those low-income clients who had in recent years been part of the 'financial inclusion' process and for whom, no alternative financial service appears to be available.

This is a delicately-poised situation – the stability and performance of the institution needs to be maintained, together with the expectations of external stakeholders –but a majority of borrowers have a strong 'trust' in the product and service propositions of the lending institutions. There are significant strategic and operational implications for the governance and management of individual institutions and the industry.

Issue: The balance of 'responsible lending' between a commercial-driven approach by the institution to maintain its obligations to external stakeholders and a client-driven approach to protect the client from inappropriate actions by either the institution or him/herself is a significant governance and management issue for the institution, the industry and external stakeholders. Any erosion of that trust could represent a significant 'structural / event risk' to the industry.

Responsible Borrowing: *"The acceptance of debt and repayment obligations which are consistent with the reasonably-anticipated income flows and expenditure commitments of the borrower, with the reasonable anticipation of the financial capacity to make timely loan repayments without an unduly adverse impact upon the lifestyle of the borrower or his/her dependents, and responding with accuracy and probity to information requested by the lending institution"*

The trends in the 2014 – 2016 surveys indicate that many borrowers perceive the loan primarily as a source of funds, rather than future stream of cash repayments. This is particularly illustrated by the increased recognition of difficulty in making loan payments whilst, at the same time, recognizing a dependency on continued borrowings. The above example of the impact and equivalence of interest payments indicates that the borrower may not have [fully] understood the 'real' cost of the loan in more tangible terms. Similarly, the acceptance of loan terms which do not appear to be coincident with the uses (such as property) further indicates that the borrower is not aligning the loan structure with the usage.

The development of financial services and financial inclusion is not necessarily dominated by lending. Savings with financial institutions are little used by borrowers in Tajikistan, whilst other types of savings are much more prevalent. Similarly, the use of insurance is minimal.

Issue: The financial education and awareness of the range and usage of different financial services appears to be an important dimension in the development of an integrated use of financial services by consumers. Again, the responsibility for developing such understanding may not lie exclusively with the financial institutions.

It is suggested that the current governance and management structures in lending institutions are identified to enable the implications of 'responsible finance' to be assessed from the different perspectives of the commercial and client viewpoints. Attachment 5 provides a framework by which to determine the governance structure and responsibilities of lending institutions by which the 'balance of responsible lending' is addressed.

Strategic Implications

The 2016 Survey on 'Borrowing by Individuals', together with the trends from 2014, identifies a range of issues which may have significant implications for individual lending institutions and the wider lending industry in Tajikistan. Whilst it is not within the scope of this survey to quantify the potential implications resulting from the changes in the structure of the loan portfolios, the increased financial pressures being acknowledged by borrowers, and the deterioration in the overall 'mood' of borrowers, have a range of risk management implications which are broader than operational credit risk. Such dimensions may be anticipated to impact upon the financial structure, trading performances and strategic risk outlook of institutions.

The following factors have implications for the balance sheet, capital and trading positions of lending institutions:

- The increased portfolio and structural risks within the lending portfolios will require assessment of the adequacy of the general loan loss reserve, in addition to the specific loan loss provisions for individual debt situations;
- Trading revenues will be pressured by the reduction in the level of new/renewal loan approvals, the underlying reduction of average loan values, and the potential lower demand for lending;
- The increase in loan arrears, together with the 'overhang' of certain higher risk portfolios, will impact upon the cash flow of the institution.

Additionally, the reputation of both an individual institution and the industry may be affected by actions which may attract high 'public profile'. The continuing availability of loan funds is clearly shown to be a significant attitude of borrowers in relation to their hopes and expectations of the lifestyle of their family – this response is extremely strong (80% of current and former borrowers). If the borrowers feel that the sacrifices and austerity to make loan repayments are not adequately 'recognised or 'rewarded' by loan renewal, this may have a fundamental impact upon popular attitudes towards lending institutions.

This may be further influenced by actions in relation to the determination / realisation of collateral on defaulting loans, or the crystallisation and collection of guarantee liabilities in the event of default. If the repossession / realisation of the collateral support is pursued, it may impact the reputation of the financial industry (and thereby future development of financial inclusion), but if such action is not pursued, then the 'motivational value' of such collateral may be eroded.

The demands of an integrated risk management strategy (operational, portfolio and structural – discussed above) are increased for the individual institution because of the strong apparent similarity of current actions across institutions in the industry (although the risk profiles of institutions vary somewhat). This is seen not only across the generic microfinance and bank segments, but also across those institutions which were identified/named by survey respondents. This suggests that the risk(s) applicable to one institution may be applicable, to a significant level, across the industry. In this regard, the performance and reputation of an institution may be affected by the independent actions of other institution(s).

In the absence of a significant improvement in the financial position and outlook of individual borrowers, the strategic outlook of an institution must consider not only the dimensions of its own business / lending activities, but also the systemic implications for the behaviour and actions of the industry in relation to both the financial pressures upon borrowers and the financial stability / adequacy of individual lending institutions.

Issue: The strategic review of the financial and social implications of the profile of the lending portfolio requires an assessment of the strategic risk management dimensions at both the institution and industry levels. This impacts upon the overall strategic assessment of the capital and trading performance of both an institution and the industry.

The structural risk pressures on the loan portfolio appear significant and the stability of credit performance are highly sensitive and vulnerable to both economic and social pressures. This presents potential systemic exposures to lending (institution and industry) beyond the operational credit management of individual borrowers. The "management of hope" and the maintenance of optimism amongst borrowers may be an important dimension of the structural risk profile of the industry.

It is suggested that the governance and management structures of both the lending institution(s) and the lending industry should be reviewed to ensure that appropriate assessment, and future actions (if necessary) can be undertaken of the risk framework, and that this is integrated into the wider strategic development.

Some Questions and Answers

Some Questions

A range of substantive issues have been raised by the responses of borrowers in the surveys conducted in June 2016, and the additional dimension of a comparison with the survey of 2014.

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 2014 and 2016 surveys. 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.

Some 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.

SYNOPSIS OF OBSERVATIONS

1 Survey Respondent Demographics

1.1 What is the domestic profile of borrowers?

Strong consistency of client profiles across MFIs and banks – slight increase in number of dependents compared with 2014 – slight reduction in number of wage-earners – high stability of population in communities.

1.2 What are the income profiles of borrowers?

Minimal difference in income profiles between MFIs and banks – upward redistribution of incomes between 2014 and 2016 – redistribution is more than can be attributed to wage inflation which indicates deliberate market and credit actions by lending institutions.

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

Lower level of multiple household incomes in 2016 – no direct impact upon level of loan arrears.

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

Little change in nominal expenditure on foodstuff and household essentials between 2014 and 2016 – lower income clients show slightly lower expenditure per household person – food price inflation was low in 2014-2016 – reduction of food expenditure to enable loan repayments increased in 2016.

1.5 What impact does the loan have upon basic household expenditures (including food)?

Food expenditure takes a greater share of the budgets of lower income households – expenditure levels broadly similar in 2014 and 2016 within different income ranges – overall domestic net disposable income adversely impacted by high non-food inflation price rises – borrowers experiencing increased budget pressure from stronger rise in non-food prices.

1.6 What are the principal differences between city, urban and rural borrower profiles?

Higher incomes in city – similar net disposable levels in urban and rural locations – greater loan repayment difficulties in city – lower loan balances in rural locations.

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

Widespread usage of fixed-term, fixed-repayment loans across a range of usage of loan funds – loan periods very consistent across usage (except foreign currency loans) – 25% of clients used loans to support domestic consumption – usage of loan funds identifies opportunities for greater product focus.

2 Financial Profile of Borrowers

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

Fundamental change in loan repayment structure to improve net disposable income of lower income clients – major change in credit structure by lending institutions - structural shift in redistribution of loan portfolio towards higher income borrowers – some increase in net disposable incomes (after loan payment) is primarily due to *constrained domestic expenditures – residual net disposable income of lower incomes remains highly vulnerable.*

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

Substantial reduction in income from 'irregular work' and 'remittances'.

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

Major increase in arrears from 3% to 15% - substantial deterioration in borrower attitudes to debt pressures – adverse trends across all income ranges – continuing strong reliance on informal loan sources – continuing reduction in food expenditures to enable loan repayments – only 9% of borrowers (21% of loan value) demonstrate adequate quantitative and qualitative characteristics.

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

Movement of clients between MFIs and banks slightly higher in 2016 than 2014.

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

Significant increase certain adverse events: loss of job: 'own business' failure: major illness in family: remittance – adverse events most frequent amongst borrowers who recognise debt problems – strategic lending and social implications.

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

All borrower segments show a substantial deterioration in credit quality - 'own business' borrowers show a more severe adverse trend in credit performance – 21% of 'own business' borrowers are in loan arrears – 'own business' activities are primarily in the retail sector – 'own business' have highest exposure to foreign currency loan debt.

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

34% of loan funds used for domestic consumption and 20% used for health and education by borrowers in 'regular work' – 65% of 'own business' loans were used primarily for business purposes, but 20% was used primarily for domestic expenditure needs.

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

64% of former borrowers did not have a current loan – former borrowers who obtained loans by moving from MFI to bank, or vice versa, had a high level of arrears (23%) and a higher level of outstanding loan balances – former borrowers, now non-borrowers, gad a much higher level of net disposable income.

3 Lending Institutions and Lending Portfolios

3.1 What are the principal financial characteristics of borrowers?

Significant variation of income growth in different trade sectors – public sector wages most constrained – major variations in risk exposure across the regions – shift in the number of loans towards lower balances – reduction in new / renewal loans in January-June 2016 (compared with 2014 survey).

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

Similar strategies between 2014 and 2016 to reduce proportion of lower income borrowers – both MFIs and banks have increased the proportion of clients with lower outstanding loan balances – both MFIs and banks have reduced the level of loan approvals in last 6 months – levels of problem lending are similar – banks continue to higher value loans and higher leverage – similar usage of loan product types.

3.3 Do the survey responses indicate credit standards or criteria?

Overall, banks provide higher loans and higher leverage ratios than those taken by MFI borrowers – the leverage ratios are highest amongst the lowest income groups – major improvement of loan repayment leverage since 2014 by both MFIs and banks in relation to lower income segments–such improvements in the operational credit measures have been overtaken by the wider portfolio and systemic risks of economic and market pressures, resulting in a deterioration of the loan portfolio quality – nevertheless, without the operational credit actions which been taken, the portfolio performance may be anticipated to have been much worse.

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

Similar severe adverse deterioration of 'own business' segment for both MFIs and banks – strong concentration in retail sector – banks have larger exposure to higher value loans – pressures on 'own business' segment present a major structural risk exposure to lending institutions.

3.5 Collateral Security – does it affect lending?

Outstanding loans with collateral are much higher than those which are non-collateralised – higher leverage costs erode any higher income differential – loan arrears almost double amongst collateral borrowers – no increase in the incidence of collateralisation since 2014 which suggests that collateral opportunities are now saturated – number of guarantees given by borrowers almost doubled between 2014 and 2016, but no differentiation in the underlying credit quality of the guarantor.

3.6 What is the scope of lending in foreign currency?

Significant adverse impact of TJS Somoni devaluation against US$ - 42% of currency loans in arrears (similar for both MFIs and banks) – substantial reduction in the number of foreign currency loans since 2014 – remaining foreign currency loans have higher US$ outstanding balances than in 2014 (the lower-value US$ balances have been much reduced) – 55% of foreign currency borrowers were 'own business' clients – little indication of 'matched currency' incomes, and currency borrowers have experienced greater reduction / loss in remittance income.

4. Risk Profile and Performance

4.1 What proportion of borrowers is over-indebted?

Significant deterioration in credit quality of loan portfolio – 15% of borrowers in arrears with loan payments – significant increase in the proportion of borrowers who recognise that they have financial problems – deterioration of financial position impacts across all income ranges – major pressures on domestic budgets arise from increasing price inflation of non-foodstuffs – continuing domestic budget economies by reduction of expenditures on food.

4.2 What are the trends in arrears?

Severe deterioration in arrears from 3% in 2014 to 15% in 2016 – increases also in utility arrears, loan refinance and recognition of difficulty to make loan repayments – 'own business' segment shows highest increase in arrears – certain individual lending institutions indicate higher arrears levels.

4.3 Where do loan arrears principally occur?

Highest arrears 40+% in foreign currency lending – arrears borrowers also show higher levels of additional informal debt – arrears concentrations in certain segments, principally amongst 'own business' clients.

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

Borrowers who move between lending institutions demonstrate much higher credit risk characteristics.

4.5 Do borrowers with problem lending show different characteristics?

Significant increase in the level of borrowers who acknowledge their difficulties with debt – only 21% of clients / 9% of outstanding loan show a reasonable level of credit strength – major deterioration in the attitude of borrowers towards debt.

4.6 Do borrowers who undertake loan refinance have particular characteristics?

Refinance increased to 11% compared with 6% in 2014 – significant regional differences, highest incidence being in GBAO – further refinance situations may be anticipated.

4.7 What is the extent of informal lending?

Informal loans from friends and family are higher in 2016 than in 2014 – informal loans are higher amongst those borrowers who recognise debt repayment difficulties – the level of informal retail credit to support domestic consumption remains high.

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

'Non-savers' have higher loan arrears than 'savers' – 'non-savers' demonstrate higher general levels of financial pressure.

5 Outlook for Borrowing

5.1 What is the outlook for borrowing demand?

Based upon current borrowers and without a significant upturn in the economy, outlook for lending appears sombre with increasing pressure on repayment capacity and reduction in outstanding loan value – only 21% of clients / 9% of outstanding loan show a reasonable level of credit strength – demand appears to be driven, to a large extent, by necessity – in addition to continuing operational credit management, particular strategic consideration needs to be given to portfolio and systemic risk pressures – 'own business' segment presents significant structural portfolio risks – such generic pressures require effective industry coordination to maintain market stability.

5.2 What is the sensitivity of affordability?

The loan portfolios show significant sensitivity to relatively modest increases in the costs of basic foodstuffs and household essentials – this presents a significant structural and strategic risk to the lending institutions – there should be close and continuing review of the dynamics of this sensitivity.

6 Impact of Borrowing

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

Substantial downturn in attitude towards benefits of loans – stronger recognition of debt repayment difficulties and impact upon lifestyle.

6.2 Do microfinance institutions stimulate greater 'financial inclusion'?

No substantial difference in profiles of MFIs and bank borrowers – both MFIs and banks have reduced exposure to lowest income clients.

7 Lender / Borrower Relationship

7.1 What is the reputation of the lending institutions?

Continuing overall strength but at reduced levels from 2014.

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 – recognition by 58% that the risks in foreign currency lending were explained.

7.3 Do lenders understand the borrower's financial position?

Continuing favourable perception of lending institutions – minimal change in the ease with which loans can be obtained – some deterioration in the resolution of debt problems with lending institution.

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

Some deterioration in ability to resolve debt problems – substantive regional differences – increased recognition by borrowers of need for assistance in dealings with lending institution.

Questions and Answers

1 Survey Respondent Demographics

1.1 What is the domestic profile of borrowers?

Strong consistency of client profiles across MFIs and banks – slight increase in number of dependents compared with 2014 – slight reduction in number of wage-earners – high stability of population in communities.

- The principal demographic characteristics of the regional profiles of households were:

	Average Age	Number in Household	Number of Dependents	Number of Wage Earners	Married
Dushanbe	37.8	5.6	3.5	2.2	76%
Khatlon	38.4	6.5	4.2	2.2	81%
Sogd	37.9	5.6	3.3	2.3	88%
RRP	37.5	5.9	3.7	2.2	81%
GBAO	38.9	5.0	2.7	2.2	80%

Compared to 2014, there were increases in the household size in Dushanbe and Khatlon and reductions in RRP and GBAO. There was a slight reduction (by an overall average of 0.2) in the average number of wage-earners (greater in Khatlon) and a corresponding increase in the level of dependents.

- This profile varied in relation to the location of the borrower, and the following factors may be noted:
    - The larger household size and number of dependents in urban and rural locations;
    - The similar profiles of both MFI and bank clients in each type of location. (There appears to be no market differentiation at this basic level of segmentation).

	Average Age	Number in Household	Number of Dependents	Number of Wage Earners	Neighborhood more than 5 years
City - MFI	37.2	5.5	3.3	3.3	90%
City - Bank	38.2	5.6	3.4	3.4	88%
Urban - MFI	38.1	5.7	3.5	3.5	94%
Urban - Bank	39.6	5.9	3.7	3.7	96%
Rural - MFI	37.4	5.9	3.7	3.7	97%
Rural - Bank	40.0	5.9	3.6	3.6	97%

The average number of wage-earners was broadly unchanged from 2014 in city locations, but reduced by about an average 0.2 elsewhere. There was a high level of stability of the population in their community. About 75% of respondents had lived in their current neighbourhood for more than 15 years.

- The similarity of the comparative market positions of MFIs and banks may be further reviewed in relation to the trade sector sources of the borrowers' income.
    - There is no substantive difference in the range of income sources between MFIs and banks;

- There is a strong concentration of activity in the retail, service and public sectors in all locations.

	Agriculture	Retail	Service	Public Sector	Other
City - MFI	3%	29%	25%	35%	18%
City - Bank	4%	34%	23%	34%	13%
Urban - MFI	13%	34%	19%	29%	18%
Urban - Bank	12%	33%	24%	25%	18%
Rural - MFI	24%	21%	23%	32%	14%
Rural - Bank	23%	23%	22%	26%	13%

1.2 What are the income profiles of borrowers?

Minimal difference in income profiles between MFIs and banks – upward redistribution of incomes between 2014 and 2016 – redistribution is more than can be attributed to wage inflation which indicates deliberate market and credit actions by lending institutions.

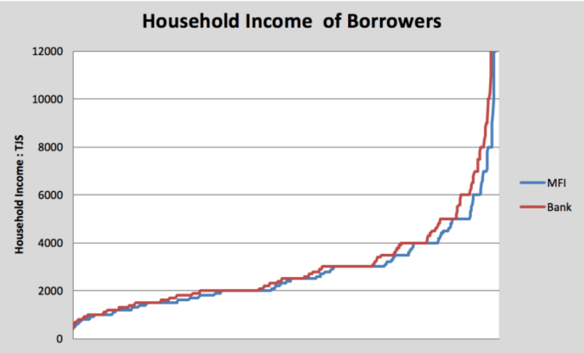
- The overall average household of all respondent borrowers was TJS 2,951. This represents an 8% increase on 2014: TJS 2,739. With an average of 2.2 (2014: 2.4) income earners per household, this represents an average individual income of TJS 1,329 – a 16% increase above the average in 2014: TJS 1,141. This is greater than the overall national trend in wage levels and, therefore, suggests that there had been some slight redistribution by lending institutions by a reduction in the lower earning client segments.
  - Average income of MFI clients (TJS2,817) was 11% lower than that of bank clients (TJS 3,168) – average individual incomes (per wage-earner) were TJS 1,266 (MFI) and TJS 1,421 (bank). This indicates a high level of overlap across the MFI and bank client profiles;
  - Income differentials were wider in comparisons of locations.

Income TJS	City		Rural		Urban	
	MFI	Bank	MFI	Bank	MFI	Bank
Household	3,093	3,554	2,512	2,600	2,756	3,127
Individual	1,371	1,597	1,126	1,145	1,263	1,419

- The distribution of borrowers across the income ranges showed that the MFIs and banks had a broadly similar distribution of borrowers across the range of household incomes.

Income Range: TJS: 2016	< 1,200	1,201-1,800	1,801-2,600	2,601-3,400	>3,400
MFI	14%	19%	25%	17%	24%
Bank	11%	17%	27%	17%	28%
2014					
MFI	19%	19%	27%	14%	21%
Bank	13%	18%	28%	15%	26%
Change: 2014 – 2016 – reductions in red					
MFI	-5%	-	-2%	+3%	+3%
Bank	-2%	-1%	-1%	+2%	+2%

- There is, therefore, a significant level of overlap across the client portfolios. The survey shows a high similarity in many client segments across MFI and bank portfolios – and it may be considered that their target client markets are very similar.
  - This strong similarity in the income profiles of the MFIs and banks is shown in the following graph:



- The average household incomes varied across the regions, particularly in comparison with Dushanbe. However, the variations were less than in 2014, which suggests that the lending institutions may have reduced their exposure to lower income segments.

Income TJS	Income Segment: Distribution					Average Income
	< 1,200	1,201-1,800	1,801-2,600	2,601-3,400	>3,400	
Dushanbe	6%	11%	20%	19%	45%	4,457
Khatlon	15%	19%	30%	18%	19%	2,516
Sogd	14%	18%	28%	17%	23%	2,653
RRP	12%	24%	31%	14%	20%	2,570
GBAO	17%	21%	23%	18%	21%	2,525

- A comparison of household incomes in relation to loan products is shown below.

Average Income TJS	Group Loan	Business Loan	Individual Loan	Agricultural Loan
MFI	2,714	3,247	2,352	2,452
Bank	3,481	3,263	2,657	2,690
Difference %	28 %	1 %	13 %	10 %

  - This comparison of income levels shows an interesting differentiation between business and individual loans;
  - The following table shows that the loan products have a similar distribution within MFIs and banks in relation to TJS Somoni loans, although Foreign Currency loans show a particular emphasis towards business lending by banks.

TJS Currency	Group Loan	Business Loan	Individual Loan	Property / Mortgage	Agricultural Loan
MFI	8 %	18 %	59 %	4 %	4 %
Bank	2 %	23 %	56 %	8 %	5%

Foreign Currency	Group Loan	Business Loan	Individual Loan	Property / Mortgage	Agricultural Loan
MFI	5 %	47 %	30 %	9 %	5 %
Bank	1 %	64 %	27 %	3 %	2 %

The appropriateness of the use of foreign currency loans for certain purposes is reviewed in a later section.

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

Lower level of multiple household incomes in 2016 – no direct impact upon level of loan arrears

- Multiple incomes have two principal dimensions:
    - The number of incomes which contribute to the household budget;
    - The number of income sources for each income provider.

- The level of multiple incomes into the household budget reduced in 2016 in comparison with 2014.

Number of Income Earners	Distribution: Clients		Distribution: Loan Balance		Arrears	
	2014	2016	2014	2016	2014	2016
One Income	19 %	25 %	19 %	25 %	4 %	15 %
Two Incomes	45 %	45 %	44 %	36 %	3 %	15 %
Three or more	37 %	30 %	36 %	38 %	3 %	15 %

This table highlights the adverse structural change in the income structure of the loan portfolios. Whilst the levels of arrears are constant across these three client segments, the risk profile of the lending institutions is disadvantaged by this reduction in income diversification. This may have adverse implications if the current economic pressures continue.

- The level of household income relates directly to the level of multiple income sources.

TJS: 2016	Household Income	Household Expenditure	Utility Expenditure	Loan Repayment	Net Disposable Income	Persons in Household
One Income	2,374	899	134	861	480	4.6
Two Incomes	2,699	1,083	161	786	668	5.4
Three or more	3,795	1,480	200	954	1,161	7.2

- There is little differentiation in the levels of multiple incomes in city, urban and rural areas;
- Multiple incomes are lowest (about an average of 2.0) amongst the age group 26-45 years, in comparison to about an average of 2.5 for the other age groups.

- Since the previous 2014 survey, the financial budgetary pressures have increased across all borrowers. Despite the higher net disposable income being shown in the above table, the following table highlights that financial challenges have spread across all borrowers and the higher income multiple borrowers are now experiencing problems.

% of clients in the income multiple	Household Income <TJS 1,200	Household Income TJS 1,201 - 2,600	Household Income >TJS 2,600	My loan repayments are more than I can afford		I need to continue to borrow to maintain how my family and I live	
	Distribution			2014	2016	2014	2016
One Income	30%	45 %	25 %	37%	53%	51%	84%
Two Incomes	10%	55 %	35 %	31%	50%	53%	79%
Three or more	2%	30 %	68 %	23%	46%	40%	78%

- The other dimension of multiple income relates to the number of income sources of an individual person. This reduced from an overall average of 1.8 per earner in 2014 to 1.2 per earner in 2016. The following table shows strongly that income from irregular work and remittance reduced sharply in 2016.

Source of Income	Regular Work	Irregular Work	Own Business	Remittance	Other
2014	47%	42%	47%	29%	15%
2016	46%	15%	37%	15%	7%

The implications of this redistribution of income to borrowers are further demonstrated in the following table which shows that the average household incomes for borrowers in these different segments results in a reduction to the overall income which is supporting loan repayment.

Household Income: TJS	Regular Work	Irregular Work	Own Business	Remittance
MFI	2,484	2,499	3,560	2,827
Bank	2,516	2,345	4,160	2,953

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

Little change in nominal expenditure on foodstuff and household essentials between 2014 and 2016 –lower income clients show slightly lower expenditure per household person – food price inflation was low in 2014-2016 – reduction of food expenditure to enable loan repayments increased in 2016.

- The overall monthly expenditure by borrowing households on basic domestic needs (food, family and domestic essentials, but excluding utilities) was TJS 1,158 (compared with 2014: TJS 1,145), equivalent to an average of TJS 202 per household person (unchanged from 2014). Average utility costs amounted to TJS 166, an increase of 32% from TJS 126 in 2014:

- This coincides with formal national statistics which indicate that CPI food costs were broadly unchanged during this period (see additional notes in Attachment 4 at the end of this review.
- Borrower responses also identify that 41% had reduced food expenditures in order to afford loan repayments.

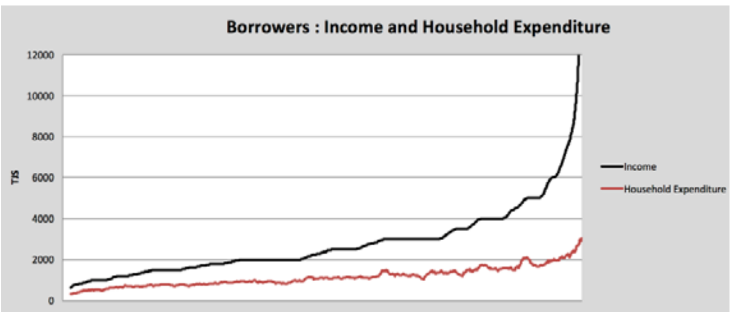
- The cost-of-living varied only slightly between city (44% of income), rural locations (48% of income) and urban (43% of income:
  - It is somewhat surprising that urban and rural expenditures should absorb such higher shares of available incomes. However, it may be noted that household sizes are larger in these locations;
  - The level of 'own food produce' in rural locations is not known, but it may be noted that only about 45-50% of respondents in these locations reported that their income is based upon agriculture.
- Outside Dushanbe, the regions showed similar levels of expenditure on food and household essential.

Ave. Household Expenditure TJS	Dushanbe	Khatlon	Sogd	RRP	GBAO
Household	1,497	1,046	1,090	1,065	1,081
Utility	195	151	146	138	205

- 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 TJS	Income Segments: TJS				
	< 1,200	1,201 – 1,800	1,801 – 2,600	2,601 – 3,400	> 3,400
Household	527	769	1,000	1,276	1,824
Per capita	116	148	177	205	282
Household as % of income	54%	49%	46%	43%	32%

The changing impact of food and household costs in relation to income levels is shown in the following graph.



This shows that:

- the impact of food and essential household costs are proportionately much greater upon lower income households than for those at higher incomes;
- the level of essential, basic household expenditure is relatively stable across the income range and is not substantially impacted by increasing incomes.

- The levels of household expenditure were similar for both MFI and bank clients, although the particular financial pressures upon the lowest income segment of bank borrowers (12% of total borrowers) appear to be reflected in lower expenditure levels.

Tajikistan: Income Segments	Average Monthly Household Expenditure: Total: TJS		Average Monthly Household Expenditure: Per Capita: TJS		Average Monthly Household Expenditure as % of Income	
	MFI	Bank	MFI	Bank	MFI	Bank
< 1,200	528	528	120	109	54%	53%
1,201-1,800	769	765	152	141	49%	49%
1,801-2,600	1,020	973	180	173	47%	45%
2,601-3,400	1,305	1,233	212	194	44%	41%
>3,400	1,797	1,858	273	296	33%	30%

- Reductions in food expenditure (in order to make loan repayments)continue to be a significant dimensions of domestic budget management, involving by 40% MFI clients and 43% bank clients. These are similar levels to those seen in 2014. This continuing pressure may be a factor in other social indicators in the survey which show increasing health problems and a significant deterioration the number of borrowers experiencing problems within their family because of debt repayments.

  The following table shows the impact of reduced food expenditure through the income segments – the 2014 levels are in parentheses.

Reduction in food expenditure to meet loan repayments	Income Segments: TJS				
	< 1,200	1,201 – 1,800	1,801 – 2,600	2,601 – 3,400	> 3,400
MFI	52 % (36)	40 %(49)	42 % (49)	38 % (41)	34 % (28)
Bank	50 % (43)	48 % (45)	37 % (50)	43 % (35)	41 % (28)

- The lowest income segment is clearly experiencing significant pressures;
- Such expenditure reductions represent a significant social cost in relation to the real overall impact of loan repayments upon the family.

Whilst food costs have been relatively stable against inflation (see Attachment 4), this on-going reduction in food levels may be considered to have potentially significant social implications (in relation to health and family relationships) – and also in relation to the reputation of the value of financial services (the survey shows a reduction in the perception of the benefits of the loan product).

1.5 What impact does the loan have upon basic household expenditures (including food)?

Food expenditure takes a greater share of the budgets of lower income households – expenditure levels broadly similar in 2014 and 2016 within different income ranges – overall domestic net disposable income adversely impacted by high non-food inflation price rises – borrowers experiencing increased budget pressure from stronger rise in non-food prices.

- The fundamental expenditures on basic domestic essentials have been broadly unchanged between 2014 and 2016;
- The average level of essential household expenditures[3] is broadly unchanged from 2014 and shown in the following table:

TJS	Income	Household expenditures	Utility costs	Net Disposable Income (pre loan)	Household Expenses as % of Income	Average Household Expense per person
MFI	2,817	1,145	161	1,510	41%	201
Bank	3,168	1,182	175	1,811	37%	204
2014						
MFI	2,678	1,120	128	1,430	42%	201
Bank	2,892	1,190	126	1,576	41%	208

  - This reflects the external economic data which indicates that there has been little change in the cost of foodstuffs since 2014.

- The impact of essential household expenditure impacts more strongly upon the lower income segments.

TJS: 2016	Income	Household expenditures	Utility costs	Net Disposable Income (pre loan)	Household Expenses as % of Income	Average Household Expense per person
< 1,200	975	527	89	359	54%	116
1,201-1,800	1,565	769	130	666	49%	148
1,801-2,600	2,175	1,000	158	1,018	46%	177
2,601-3,400	2,994	1,276	192	1,526	43%	205
>3,400	5,695	1,824	220	3,652	32%	282

2014	Income	Household expenditures	Utility costs	Net Disposable Income (pre loan)	Household Expenses as % of Income	Average Household Expense per person
< 1,200	959	523	92	345	54%	107
1,201-1,800	1,570	787	106	678	50%	145
1,801-2,600	2,206	1,134	117	955	51%	199
2,601-3,400	2,981	1,336	133	1,512	45%	231
>3,400	5,526	1,805	175	3,546	33%	291

[3] Household expenditure: relates to essential household items bought each month and include food (borrower and family), tobacco and alcohol, household items (cleaning etc), telephone, and essential transport

- There is minimal change in the expenditures on basic domestic needs between 2014 and 2016 in each of the income ranges;
- The lowest income segments account for 31% of borrowers (12%: <TJS 1,200 and 19%: 1,201-1,800).

- However, there are indications that, despite the apparent stability of basic domestic expenditures, households have been experiencing increasing pressures on domestic expenditures and that these have impacted on lifestyles.

All Borrowers	Indicators of Expenditure Trends			Impact of Expenditure Pressures		
	My financial situation has improved in the last 6 months	My household expenses have risen faster than income in the last 6 months	Food expenditure has been reduced to make loan repayments	Debt repayments cause problems within my family	I can afford to buy 'treats' for myself or my family	Major illness of self or family in last 6 months
2016	67%	68%	41%	47%	69%	18%
2014	85%	69%	41%	22%	86%	14%
Change: adverse in Red	-18%	-1%	-	25%	-17%	4%

- These overall indicators are shown below in relation to different income ranges.

	Indicators of Expenditure Trends			Impact of Expenditure Pressures		
	My financial situation has improved in the last 6 months	My household expenses have risen faster than income in the last 6 months	Food expenditure has been reduced to make loan repayments	Debt repayments cause problems within my family	I can afford to buy 'treats' for myself or my family	Major illness of self or family in last 6 months
< 1,200	61%	69%	51%	51%	59%	24%
1,201-1,800	64%	68%	42%	50%	62%	18%
1,801-2,600	68%	68%	39%	45%	69%	17%
2,601-3,400	69%	70%	39%	43%	73%	18%
>3,400	68%	68%	36%	45%	76%	16%
2014						
< 1,200	87%	57%	38%	26%	79%	10%
1,201-1,800	86%	61%	48%	23%	82%	11%
1,801-2,600	85%	75%	50%	21%	87%	13%
2,601-3,400	82%	73%	39%	21%	87%	21%
>3,400	86%	75%	28%	21%	90%	17%

- These tables indicate the following:
    - Borrowers recognise that the primary pressures on the domestic budget have not been on the expenditures on foodstuffs;
    - However, expenditure on foodstuff have been a relatively direct mechanism by which to achieve economies within the budget;
    - This has continued to impact strongly upon the lower income segments, but there has been a significant change in the budgetary behaviour of higher income segments – the financial pressures are now much more widespread;
    - The lower income segments show a significant increase in the incidence of illness. The purpose of this review is to observe such a change and not to suggest any 'cause-and-effect' in relation to the impact of medium-term budget stringencies. Nevertheless, such trends should be considered in relation to an assessment of the dimensions of 'responsible lending' and 'responsible borrowing'.

1.6 What are the principal differences between city, urban and rural borrower profiles?

Higher incomes in city – similar net disposable levels in urban and rural locations – greater loan repayment difficulties in city – lower loan balances in rural locations.

- The average household sizes showed rural households to be slightly larger (average 5.9 persons) than urban (5.8) and city (5.5);
- Income levels were higher in city locations, although the differences in food expenditure were not as wide.

TJS	Income	Household Expenditure	Utilities	Loan Repayment	Net Disposable Income (pre loan)
City - MFI	3,093	1,234	192	800	868
City - Bank	3,554	1,261	200	1,234	859
Urban - MFI	2,756	1,113	149	782	712
Urban - Bank	3,127	1,161	160	1,104	702
Rural - MFI	2,512	1,062	135	587	728
Rural - Bank	2,600	1,083	155	712	651

- The range of 'source of income' varied across the locations, with the greatest impact of remittance being shown in rural areas. The 2016 survey shows substantial reductions in the levels of 'irregular work' and 'remittances' – whilst these are widespread across all locations, the impact may be particularly acute in the urban and rural communities.

	Regular Work	Irregular Work	Own Business	Remittance	Other
City - MFI	51%	14%	37%	10%	3%
City - Bank	49%	12%	39%	9%	3%
Urban - MFI	44%	14%	40%	16%	8%
Urban - Bank	39%	12%	47%	17%	8%
Rural - MFI	46%	19%	28%	22%	14%
Rural - Bank	42%	19%	34%	21%	10%

- A comparison of lending between city and rural provides some substantial different dimensions of MFI and bank loan exposures – however, the impact of arrears appears to be widespread across communities.

	City		Urban		Rural	
	MFI	Bank	MFI	Bank	MFI	Bank
Ave Loan TJS	8,779	13,822	7,632	11,047	5,458	7,453
% Fgn Ccy	8%	12%	7%	9%	4%	6%
% Arrears	15%	16%	13%	19%	14%	16%

- The profile of the loan amounts showed some differences but within an overall underlying trend towards lower outstanding loan balances than applied in 2014.

Distribution of Borrowers	Outstanding Loan Balance (Average): TJS				
	< 1,500	1,501-3,000	3,001-5,000	5,001-10,000	> 10,000
City - MFI	30%	26%	17%	15%	12%
City - Bank	24%	23%	15%	15%	23%
Urban - MFI	27%	27%	17%	14%	15%
Urban - Bank	29%	18%	18%	12%	23%
Rural - MFI	30%	28%	19%	12%	11%
Rural - Bank	24%	23%	18%	17%	19%

- The average levels of net disposable income' (as a % of income) were reasonably consistent across the locations. This appears to indicate that there is some inherent consensus across society of the scale of such payments.

Expenditures as % of Income	Household expenditure as % of Income	Utility expenditure as % of Income	Loan repayment as % of Income	Net Monthly Disposable Income as % Income
City - MFI	40%	6%	26%	28%
City - Bank	35%	6%	35%	24%
Urban - MFI	40%	5%	28%	26%
Urban - Bank	37%	5%	35%	22%
Rural - MFI	42%	5%	23%	29%
Rural - Bank	42%	6%	27%	25%

- Attitudes towards lending deteriorated significantly between 2014 and 2016.

% of respondents who agree with the statement – adverse shown in red		MFI			Bank		
		City	Urban	Rural	City	Urban	Rural
I borrowed too much	2014	24 %	29 %	27 %	23 %	31 %	22 %
	2016	36 %	32 %	27 %	47 %	36 %	33 %
It is / was difficult to resolve debt problems with my lender	2014	24 %	25 %	21 %	26 %	24 %	26 %
	2016	44 %	34 %	30 %	52 %	36 %	36 %
Debt repayments cause problems within my family	2014	25 %	22 %	19 %	24 %	21 %	19 %
	2016	53 %	41 %	38 %	57 %	44 %	48 %
My loan repayments are / were more than I can afford	2014	30 %	34 %	23 %	26 %	36 %	24 %
	2016	52 %	49 %	44 %	56 %	48 %	53 %
I would like help to resolve debt problems with my lending institution	2014	22 %	39 %	31 %	22 %	41 %	32 %
	2016	54 %	52 %	43 %	57 %	54 %	53 %

- The deterioration is at a stark level across all locations;
- These responses present a direct challenge to the lending industry to determine how to respond to what appears to be a national problem.

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

Widespread usage of fixed-term, fixed-repayment loans across a range of usage of loan funds – loan periods very consistent across usage (except foreign currency loans) –25% of clients used loans to support domestic consumption – usage of loan funds identifies opportunities for greater product focus.

- The distribution of the principal loan products is shown in the following tables in relation to TJS and Foreign Currency lending.

TJS Somoni	Group Loan	Business Loan	Individual Loan	Agriculture / Education / Property Loans
MFI	8%	18%	59%	12%
Bank	2%	23%	56%	16%

Foreign Currency	Group Loan	Business Loan	Individual Loan	Agriculture / Education / Property Loans
MFI	5%	47%	30%	14%
Bank	1%	64%	27%	5%

- The proportion of loans in foreign currency (98% in US$) has fallen sharply since 2014 (27%) to 7% of borrowers in 2016;
- The 2014 and 2016 surveys do not suggest that there was any significant level of foreign currency-based income amongst foreign currency borrowers. Higher-value loans to the 'own business' segment related primarily to the retail sector with a TJS Somoni revenue stream. This structural risk exposure was identified by the 2014 survey and is a fundamental mis-match of loan product structure and income cash-flow.

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

	Business	Domestic	Property: Acquisition	Property: Improvement	Health / Education
Business: TJS	87%	6%	1%	1%	3%
Business: Fgn Ccy	93%	3%	2%	2%	0%
Individual Fixed: TJS	21%	40%	11%	11%	16%
House / Property: TJS	12%	38%	20%	16%	12%
Group: TJS	18%	40%	7%	10%	20%
Agriculture: TJS	28%	42%	7%	14%	6%
Education: TJS	1%	6%	1%	2%	88%

- The use of business and education loans appears to be closely related to the usage;
- However, fixed-term loans appear to be widely used (c.85%) for business trading (with its shorter-term and more fluctuating cash flow) and also for 'domestic' (which is predominately used for consumption rather than asset acquisition purposes);
- The use of 'individual loans' for property purposes identifies two disparate timescales – which result in higher levels of loan repayment.
- This suggests that the description of a loan product related to its use may be a method for establishing a greater alignment of product structure with product usage.

2 FINANCIAL PROFILE OF BORROWERS

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

Fundamental change in loan repayment structure to improve net disposable income of lower income clients – major change in credit structure by lending institutions - structural shift in redistribution of loan portfolio towards higher income borrowers –some increase in net disposable incomes (after loan payment) is primarily due to constrained domestic expenditures – residual net disposable income of lower incomes remains highly vulnerable.

- The overall average household income of all borrowers was TJS 2,951 (2014 - TJS 2,739). With an average of 2.2 (2014 - 2.4) income earners per household, this represents an average individual income of TJS 1.329 (2014 - TJS 1,141):
  - This increase of 16% is somewhat higher than an underlying wage growth of about 12% (source: National Statistics). This suggests that the lending institutions may have been moving the loan portfolios away from the lowest income sectors and/or that lower income borrowers have maintained a lower level of loan demand (in the face of the affordability pressures);
  - Average incomes of bank clients (TJS 3,168) were 12% higher than that of MFI clients (TJS 2,817) – average individual wage-earner incomes were TJS1,421(bank) and TJS 1,266 (MFI). This differential is 4% greater than the difference of 8% in 2014. This may suggest that the bank lending institutions have imposed greater income target selectivity;
  - Such income differentials were stretched further in comparisons of locations.

Income TJS	City		Urban		Rural	
	MFI	Bank	MFI	Bank	MFI	Bank
2016						
Household	3,093	3,554	2,756	3,127	2,512	2,600
Individual	1,371	1,597	1,263	1,419	1,126	1,145
2014						
Household	3,101	3,304	2,265	2,708	2,211	2,456
Individual	1,350	1,401	936	1,080	904	962

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

Net Disposable Income TJS	Income	Household costs	Utility costs	Net Disposable Income (pre-Loan)	Loan Repayments	Net Disposable Income (after Loan)
MFI	2,817	1,145	161	1,510	733	777
Bank	3,168	1,182	175	1,811	1,056	754
Former Borrowers MFI	2,836	1,138	182	1,516	1,364	152
Former Borrowers Bank	2,694	1,179	162	1,353	891	462
Non-Borrowers	2,297	1,134	165	998		998

- This table also suggests the following:
  - The former borrowers of banks had a lower average income than those who continue to borrow from the banks. This suggests that the banks have reduced their exposure to lower income clients;
  - Conversely, average income of both current and former MFI clients are at a similar level;
  - Nevertheless, some of those 'former clients' have obtained loans from other lenders (MFI now with banks, and vice versa) and their average loan repayments are relatively high, particularly those former MFI clients now borrowing from banks (with an average outstanding loan balance of TJS 16,958);
  - The improvement in the residual net disposable income in 2016, against 2014, results primarily from the lower levels of expenditures on domestic household essentials.

	Net Disposable Income (pre-Loan)		Loan Repayments		Net Disposable Income (after Loan)	
	2014	2016	2014	2016	2014	2016
MFI	1,430	1,510	771	733	659	777
Bank	1,576	1,811	966	1,056	610	755

- 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.

Household Income Segments	Household and Utility costs	Loan Repayments	Net Disposable Income NDI (after Loan) 2016	Net Disposable Income NDI (after Loan) 2014	Distribution of Borrowers
< 1,200	616	261	98	-147	12%
1,201-1,800	899	384	282	85	19%
1,801-2,600	1,158	511	507	267	26%
2,601-3,400	1,468	691	835	756	17%
>3,400	2,044	1,816	1,835	2,025	26%

- This table highlights the particular vulnerability of about 30% of borrowers to only modest increases in the real cost-of-living. 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 TJS 1,200, 78% of borrowers reported committed expenditures in excess of 75% of income;
    - Within the income segment up to TJS 1,201-1,800, 65% of borrowers reported committed expenditures in excess of 75% of income.

- However, the comparison of 'net disposable income' between 2014 and 2016 identifies that the net financial position had strengthened, albeit that it remains at a very low level. This may reflect:
    - Deliberate actions by lending institutions to restrict the loan exposure of the lowest income segments; and/or
    - A reflection of the negligible inflation on foodstuffs and the much stronger CPI/inflation pressures upon other goods and requirements – and thereby the need for consumers to re-adjust still further the balance of their domestic budget to accommodate such inflationary pressures;
    - NDI is highly sensitive to rises in costs. An increase of 10% only in relation to food and household essentials would double the number of borrowers with a negative NDI (after loan costs) from 13% to 23% of borrowers.

- 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)
< 1,200	26%	72%	29%	76%
1,201-1,800	24%	55%	27%	64%
1,801-2,600	23%	51%	24%	50%
2,601-3,400	22%	44%	25%	49%
>3,400	28%	45%	36%	55%

    - There has, however, been a major change in the level of loan repayment in relation to income.

	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)	
	2014	2016	2014	2016	201 4	2016	2014	2016
< 1,200	49%	26%	145%	72%	59%	29%	150%	76%
1,201-1,800	38%	24%	88%	55%	39%	27%	89%	64%
1,801-2,600	29%	23%	67%	51%	35%	24%	82%	50%
2,601-3,400	23%	22%	46%	44%	28%	25%	55%	49%
>3,400	25%	28%	39%	45%	31%	36%	49%	55%

- This table (comparing 2016 and 2014) is **a major finding of the survey**. It identifies that:
  - The lending institutions have undertaken a fundamental reposition of the loan leverage levels to lower income borrowers;
  - This change reduces dramatically the impact of loan costs on the domestic budgets of lower income borrowers;
  - There is now a consistency of the cost of loan repayments in relation to net disposable income across the income ranges;
  - Such actions have been undertaken by both MFIs and banks;
  - This appears to be a significant action towards a greater demonstration of 'responsible lending'.
- Nevertheless, the previous two tables highlight 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	Friends	Retailer Credit: Assets	Retailer Credit: Domestic
< 1,200	12%	20%	4%	29%
1,201-1,800	7%	15%	6%	22%
1,801-2,600	5%	11%	4%	15%
2,601-3,400	8%	12%	4%	18%
>3,400	6%	11%	5%	10%

- These responses highlight additional and significant dimensions:
  - The substantive level of additional 'informal' support being obtained across all borrowers, and particularly the lowest income segment;

    - The significant inter-dependency within local communities of informal credit;
    - Informal credit from retailers, whilst remaining high for consumption spending, is lower than was seen in 2014. This may be related to the relatively high levels of arrears amongst ‘retail own business’ borrowers – and may suggest that it has been necessary for retailers to reduce the extent to which they provide informal credit;
    - Conversely, informal lending by family and friends has increased. There must be some caution in relation to the extent to which such can be continued;
    - The social implications of informal financial support to family and friends should also be considered. There is a higher usage of such informal loans by those in arrears or with foreign currency loans – who will the borrower prefer for repayment?
  - This situation appears to present a substantive strategic and structural risk to both MFIs and banks – and also has significant social implications.

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

Substantial reduction in income from ‘irregular work’ and ‘remittances’.

- The distribution of borrowers is broadly similar in MFIs and banks across the different income characteristics: ‘employer: bank transfer’ 24%; ‘employer: cash/cheque’ 28%; ‘social subsidies’ 4%; ‘occasional or irregular payments’ 17%; and ‘own business’ 41%[4];

- 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 the broad similarity across the comparable client segments for MFIs and banks;
  - However, between 2014 and 2016, there were substantial reductions in the proportion of clients whose income is based upon ‘irregular work’ (down from 42% to 15%) and ‘remittances’ (down 29% to 15%). It is possible that the greater vulnerability of the ‘irregular work’ segment caused lending institutions to be more cautious in lending to such clients.

Source of Income	Income	Household costs	Utility costs	Loan Repayments	Net Disposable Income (after Loan)
Microfinance Institutions					
Regular Work	2,484	1,076	150	495	762
Irregular Work	2,499	1,047	173	492	787
Own Business	3,560	1,343	174	1,174	869
Remittances	2,827	1,205	149	739	733
Bank					
Regular Work	2,516	1,061	159	571	726
Irregular Work	2,345	1,015	155	638	536
Own Business	4,160	1,407	208	1,643	902
Remittances	2,953	1,125	137	916	775

[4] Some borrowers report more than one source of income

- The above table, based upon the source of income, can be related to the credit quality performance of these segments. The following table provides some characteristics of credit performance of the various client segments. Such variations indicate the need for lending institutions to maintain a differentiated approach towards the identification, work-out / resolution of problem lending with different client segments – and to recognise, and respond to, the different characteristics.

Source of Income	Arrears	Reduction in food to meet loan repayments	Informal loan(s): family and friends	Loan refinance / reschedule	Loan refusal by a lending institution)
Microfinance Institutions					
Regular Work	10%	38%	20%	11%	22%
Irregular Work	15%	53%	36%	13%	30%
Own Business	20%	39%	18%	14%	19%
Remittances	12%	41%	26%	17%	38%
Bank					
Regular Work	12%	44%	19%	11%	21%
Irregular Work	17%	50%	37%	19%	29%
Own Business	23%	42%	25%	16%	21%
Remittances	16%	47%	29%	21%	25%

- Borrowers recognise the pressures on their financial position in qualitative terms in addition to the quantitative financial dimensions. However, the differences in attitudes do not show any great differentiation which may have been expected in relation to the stability / assurance of income flows against the obligation of fixed monthly loan repayments.

Source of Income	I borrowed too much	My loan repayments are / were more than I can afford	Debt repayments cause problems within my family	I need / needed to continue to borrow to maintain how my family and I live	I would like help to resolve debt problems with my lending institution
Microfinance Institutions					
Regular Work	31%	47%	44%	77%	50%
Irregular Work	36%	57%	52%	77%	55%
Own Business	36%	51%	47%	84%	51%
Remittances	31%	57%	48%	84%	53%
Bank					
Regular Work	41%	51%	50%	80%	53%
Irregular Work	46%	59%	59%	80%	69%
Own Business	40%	55%	51%	84%	55%
Remittances	36%	63%	59%	85%	57%

These responses show a much stronger recognition of the financial pressures than were acknowledged in the 2014 survey – and the subsequent review of the credit profile of borrowers will show that a significant proportion of borrowers still do not fully admit to the vulnerability of their financial position.

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

Major increase in arrears from 3% to 15% - substantial deterioration in borrower attitudes to debt pressures – adverse trends across all income ranges – continuing strong reliance on informal loan sources – continuing reduction in food expenditures to enable loan repayments – only 9% of borrowers (21% of loan value) demonstrate adequate quantitative and qualitative characteristics

- The level of arrears has increased dramatically to 15% from only 3% in 2014;
- However, arrears in loan repayments is a headline public measure of credit risk quality and does not fully reflect the many borrowers who strive hard to maintain payments for as long as possible – the borrowers in Tajikistan most certainly demonstrate such commitment to their debt obligations;
- 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 tables in which each segment is exclusive (no borrower is included in more than one segment);
- Separate tables are shown for 2014 and 2016 … the contrast between the two years is so stark, particularly in relation to the distribution of clients and outstanding loan value. This has such potential implications for the outlook of individual lending in Tajikistan that detailed comparison is appropriate.

Repayment Characteristic[5]: 2016	Household Income TJS	Average Outstanding Loan Balance	Net Disposable Income NDI (after Loan)	Distribution of Loans: Value	Distribution of Borrowers
Arrears	3,281	16,012	571	28%	15%
Lender Refusal	2,819	9,052	806	11%	10%
Repayment Difficulty[6]	2,738	8,052	679	31%	33%
Expenditure >75% Income	2,763	8,622	264	21%	21%
Remainder	3,314	3,648	1,561	9%	21%

Repayment Characteristic: 2014	Household Income TJS	Average Outstanding Loan Balance	Net Disposable Income NDI (after Loan)	Distribution of Loans: Value	Distribution of Borrowers
Arrears	2,546	7,662	365	3%	3%
Lender Refusal	3,007	7,318	830	4%	4%
Repayment Difficulty	2,560	7,552	515	25%	25%
Expenditure >75% Income	2,166	8,707	(85)	46%	40%
Remainder	3,717	5,778	1,784	21%	28%

[5] This reflects a progressive segmentation of clients – those in 'arrears' are excluded from subsequent segments and then 'lender refusal' are similarly excluded from the following segments, and so on.

[6] 'Repayment Difficulty': Based upon those borrowers who agreed 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.

- These tables indicate that:
    - There has been a significant adverse change in the credit quality of the loan portfolios – problem lending is recognised by 58% of borrowers (2014 – 32%) accounting for 70% of loan value (2014 – 32%);
    - There has been some (albeit small) improvement in the net disposable incomes of some segments
    - There has been a substantial increase in the self-recognition / acknowledgement of loan repayment problems by many borrowers;
    - The problem recognition by 33% of clients is not yet resulting in arrears;
    - There is very significant financial pressure upon those (21%) with committed expenditures in excess of 75% of household income – but this segment has not acknowledged their vulnerable financial situation;
    - The 'remainder' are not necessarily financially strong – but rather that they are stronger than the other segments.
- The positive dimensions of such segmentation result primarily from the recognition, rather than avoidance, of the problem by such a proportion of clients. This provides a basis upon which a 'way forward' can be developed.
- However, this segmentation does highlight the extreme vulnerability which appears from the client responses – and the seemingly acute sensitivity to economic trends, the balance of wage and inflation trends, and the buoyancy of local economies to support the 'own business' sector.

- 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	Informal Loan: Family	Informal Loan: Friends	Informal Loan: Retails	Arrears: Utility Payments
Arrears	62%	40%	12%	27%	26%	16%
Lender Refusal	48%	26%	9%	16%	34%	18%
Repayment Difficulty	52%	31%	8%	14%	26%	13%
Expenditure >75% Income	24%	16%	5%	10%	14%	9%
Remainder	19%	13%	3%	5%	14%	6%

- The above characteristics demonstrate the range of actions which have been taken not only by those borrowers who have recognised the financial pressures which they must address, but also those under particular financial constraint;
- The level of reduction of monthly food expenditure may be particularly significant. Current expenditures on food across all these segment is only about TJS 200 per person. 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. Because the deterioration of the credit quality of the loan portfolios is so severe between 2014 and 2016, the following table is shown for both 2014 and 2016 to highlight the scale of adverse change across all income ranges.

Household Income: 2016	< 1,200	1,201 – 1,800	1,801 – 2,600	2,601 – 3,400	> 3,400
Arrears	9 %	12 %	17 %	16 %	17 %
Lender Refusal	16 %	10 %	14 %	12 %	14 %
Repayment Difficulty	52 %	50 %	49 %	51 %	48 %
Expenditure >75% Income	78 %	65 %	54 %	45 %	42 %
Remainder	11 %	17 %	21 %	25 %	25 %

Household Income: 2014	< 1,200	1,201 – 1,800	1,801 – 2,600	2,601 – 3,400	> 3,400
Arrears	4%	3%	4%	4%	3%
Lender Refusal	2%	4%	5%	6%	6%
Repayment Difficulty	25%	30%	33%	32%	25%
Expenditure >75% Income	85%	76%	64%	43%	29%
Remainder	11%	16%	22%	39%	50%

  - *These figures show the total share of clients in each income segment for each 'problem' category – for example, in income segment 1,201-1,800 in 2016, 50% of borrowers had 'repayment difficulty', 65% of all borrowers in this income range had committed expenditures above 75% of income.*

- Such widespread recognition of problem lending amongst clients (although the lending institutions will not be able to directly measure it) requires the lending institutions to differentiate the types / segments of debt problem which they face.
- Such widespread financial problems amongst borrowers, most of whom are striving to maintain loan payments and meet their financial obligations, requires lending institutions, together with other stakeholders, to recognise the strategic and structural risk drivers – and not to focus primarily on the visible levels of arrears.

- Such financial pressures on the domestic budget have potentially far-reaching consequences for the lifestyle of the borrowers, social attitudes towards indebtedness, and the reputation and potential contribution of financial services to society. The following table provides some insights of the impact of current pressures upon borrowers.

Borrower Attitude: 2016	Loans improve the quality of life	Debt repayments cause problems within my family	I need / needed to continue to borrow to maintain how my family and I live	I can afford to buy 'treats' for myself or my family	Most of my friends have difficulties meeting their domestic budget needs
Arrears	49%	67%	86%	56%	75%
Lender Refusal	65%	49%	82%	58%	81%
Repayment Difficulty	61%	76%	92%	60%	81%
Expenditure >75% Income	80%	16%	71%	80%	75%
Remainder	76%	13%	64%	85%	74%

- These responses highlight some important social dimensions:
  - Family pressures because of debt which have been shown, in other countries, to place great strain on personal relationships;
  - Debt dependency can create a feeling of helplessness / hopelessness, not least if the borrower recognises that debt is not improving his/her life. It may also be recognised that, for the lowest income segments, the monthly interest cost can be almost the equivalent of the cost of food for one person for a month;
  - Widespread pressures of domestic budgets will make such situations the 'norm' – perhaps this may be contributing to a pattern of self-help between individuals with the increasing use of informal loans.

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

Movement of clients between MFIs and banks slightly higher in 2016 than 2014.

- 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 and such movement is at a slightly higher level than in 2014 (2014 levels shown in parentheses in the following comments):
  - 38% (30%) of former bank borrowers now have a loan with an MFI and an additional 11% (8%) have borrowed from an MFI in the last 2 years;
  - 37% (21%) of former MFI borrowers now have a loan with a bank, and an additional 13% (2%) 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 TJS 9,900 (2014 - TJS 11,300) with an MFI, compared to an overall average MFI debt of TJS 7,500.
            - These borrowers show a higher risk profile with 22% of borrowers in loan arrears with the MFI and21% with a loan application refusal in the last 12 months.
        - Former MFI borrowers now have an average debt of TJS 17,000 with a bank (average bank loan TJS 11,300).
            - These borrowers show a higher risk profile with 23% of borrowers in loan arrears with the MFI and 17% 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. However, these responses demonstrate that lending institutions should be keenly aware of the level and trends of client turnover and the significant adverse differences in the credit performance of borrowers who move between institutions.

- The level of borrowers with multiple concurrent loans is low and relates to only 4% of borrowers in both MFIs and banks. (This is similar to that identified in 2014).
- The level of movement between lenders during the preceding two-year period identified a low level of client movement, but somewhat higher than was shown in 2014. *[The writer is unaware of the ease with which borrowers can change lenders. The average loan periods appear to be relatively short and would thereby enable opportunities for such institutional movement].*

Number of Lenders	One		Two		Three		More than three	
	2014	2016	2014	2016	2014	2016	2014	2016
MFI	90%	84%	9%	15%	1%	2%		0
Bank	90%	81%	9%	16%	1%	3%		0

- In response to a separate, direct question, almost 90% of both MFI and bank clients agreed that “It is better to borrow from only one institution, rather than to change lenders”.
    - Anecdotal comment by respondents to the research interviewers indicated that many borrowers sought to remain with a single lender with an expectation that a lower interest rate would be available upon loan renewal (an expectation which is, reportedly, often not fulfilled).

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

Significant increase certain adverse events: loss of job: ‘own business’ failure: major illness in family: remittance – adverse events most frequent amongst borrowers who recognise debt problems – strategic lending and social implications.

- There has been a significant increase in the incidence of ‘adverse events’ in 2016, compared with 2014. The only substantive difference between MFI and bank borrowers related to the incidence of business failure.

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	Remittance income stopped, or reduced
2016						
MFI	7%	9%	18%	18%	7%	18%
Bank	10%	10%	23%	19%	10%	18%
2014						
MFI	5%	4%	15%	13%	5%	na
Bank	4%	4%	12%	16%	5%	na

- The incidence of exceptional events upon an individual during the previous six months did not occur consistently across the various client segments. The following table relates 'adverse events' to the risk segments reviewed above.

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	Remittance income stopped,or reduced
Arrears	19%	17%	41%	29%	22%	34%
Lender Refusal	9%	10%	22%	20%	6%	20%
Repayment Difficulty	8%	10%	21%	20%	8%	18%
Expenditure > 75%	3%	6%	11%	11%	3%	13%
Remainder	3%	6%	10%	11%	2%	7%

- This table shows some apparent linkages between 'adverse events' and an increased recognition of credit risk / financial problems;
- The events of 'business failure' and 'remittances' are extremely strong;
- 40% of 'arrears borrowers' have provided collateral assets but the incidence of 'having to sell an asset' is comparatively low. The role and realisable value of collateral is considered later in this review;
- The financial pressures appear to be reflected in a higher incidence of illness. This may reflect the stress of financial pressures, or the effects of financial pressures upon the domestic budget (involving reduced food expenditures), or the domestic and social consequences [embarrassment] of the sale of a major asset and thereby the public demonstration of financial failure;
- The impact of 'job loss' and 'business failure' are reflected differently across the income range.

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	Remittance income stopped, or reduced
< 1,200	9%	15%	10%	7%	24%	21%
1,201-1,800	8%	12%	14%	8%	18%	17%
1,801-2,600	8%	8%	19%	7%	17%	17%
2,601-3,400	7%	7%	25%	7%	18%	16%
>3,400	7%	7%	24%	7%	16%	16%

- The impact of the second employment income amongst lower income segments has an immediate impact, not least if alternative employment is difficult to obtain. This is also reflected in the reduction in the levels of average number of wage-earners in a household;
- Business failure corresponds with the higher average income of this borrower segment.
- The different impact of 'adverse events' is clearly shown in a comparison of borrowers with TJS Somoni and foreign currency loans. The impact of the exchange rate devaluation on the TJS equivalent liability is consistency compounded / aggravated for the 'foreign currency' borrowers in each of the types of 'adverse event'. The pressures upon this segment of clients are clearly extremely severe and reflect both financial and social impacts.

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	Remittance income stopped, or reduced
MFI: TJS	6%	8%	16%	17%	5%	17%
MFI: Fgn Ccy	16%	18%	43%	24%	29%	37%
Bank: TJS	9%	10%	20%	18%	8%	17%
Bank: Fgn Ccy	13%	12%	46%	24%	23%	25%

- Adverse events in the principal trade sectors are shown in the following table:

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	Remittance income stopped, or reduced
Agriculture	6 %	10 %	15 %	16 %	9 %	17 %
Building-Property	9 %	6 %	13 %	13 %	3 %	15 %
Retail	6 %	10 %	40 %	19 %	9 %	18 %
Services	13 %	11 %	21 %	19 %	10 %	20 %
Public Sector	4 %	7 %	5 %	16 %	4 %	15 %

- This table highlights:
  - The direct loss of a job varied substantially between trade sectors and spousal income;
  - The business failure rate occurs principally in the retail sector which has, of course, low entry / low exit barriers;
  - The previous table shows also the high level of business failures amongst foreign currency borrowers who are predominately in the retail and service sectors.

- There was low occurrence of a need to sell assets for debt repayment (except for foreign currency borrowers). This contrasts with the levels of asset collateral as loan security which are provided by 30% of MFI clients and 43% of bank clients. This suggests that the intrinsic value of such security is low, but its 'value' may rest primarily from the 'threat of loss of usage'.

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

All borrower segments show a substantial deterioration in credit quality - 'own business' borrowers show a more severe adverse trend in credit performance –21% of 'own business' borrowers are in loan arrears – 'own business' activities are primarily in the retail sector – 'own business' have highest exposure to foreign currency loan debt.

- The overall distribution of borrowers is shown in the following table in relation to the major sources[7] of employment, together with some dimensions of their loan performance.

	Distribution		Average Household		Credit Performance		
	Clients	Loan	Income	Loan	Arrears	Lender Refusal	Difficulty to make loan repayments[8]
MFI							
Regular Work	48%	27%	2,484	4,266	10%	22%	47%
Irregular Work	16%	9%	2,499	4,224	15%	30%	57%
Own Business	36%	63%	3,560	13,106	20%	19%	51%
Bank							
Regular Work	46%	25%	2,516	5,450	12%	21%	51%
Irregular Work	14%	8%	2,345	5,607	17%	29%	59%
Own Business	40%	67%	4,160	16,719	23%	21%	55%

This table highlights:

- The similarity of the segmentation of the loan portfolios of MFIs and banks in relation to the source of borrower income;

[7]Sources of Employment: the table relates only those in paid employment – the receipt of remittances and/or social benefits causes overlap and are considered elsewhere in this review.
[8]Question 74: "My loan repayments are more than I can afford"

- The different concentrations of client and loan value exposure demonstrates the need for appropriate and differentiated credit propositions and client management;
- The different levels of adverse risk performance also indicate the need for the management of such 'problem situations' to be differentiated – the sensitivities, complexities and dependencies of these client segments are different and will consequently require different management skills from the lending institution;
- The income profiles of those in regular and irregular work are similar for both MFIs and banks, but the leverage of the loan balances is higher amongst bank clients.

- There was a strong adverse movement in credit performance between 2014 and 2016. The deterioration in the 'own business' segment has been particularly severe which must be considered also in conjunction with the higher levels of business failures within the last 6 months.

	Loan Arrears				Difficulty to make loan repayments			
	MFI		Bank		MFI		Bank	
	2014	2016	2014	2016	2014	2016	2014	2016
Regular work	3%	10%	4%	12%	34%	47%	30%	51%
Own Business	3%	20%	3%	23%	24%	51%	23%	55%

- The principal types of loan product which have been used by these 'income source' segments are:

Type of Loan	Business Loan	Individual: Fixed Loan	Property Loan	Agriculture Loan	Education Loan
TJS Currency					
Regular Work	7%	69%	6%	3%	5%
Irregular Work	6%	64%	10%	7%	6%
Own Business	43%	45%	3%	2%	1%
Foreign Currency					
Regular Work	20%	51%	12%	7%	0%
Irregular Work	14%	64%	5%	5%	0%
Own Business	80%	12%	5%	0%	0%

- This table suggests that the use of both loan products and currencies have often been inconsistent with the purpose of product and the underlying income / cash flow profile of the borrower:
  - Businesses have used 'individual' loan products primarily for trading purposes;
  - Both 'own business' and individuals have used foreign currency loans without corresponding currency income, with some exceptions in relation to the receipt of remittances;
  - Whilst remittance income has reduced for foreign currency borrowers, such income flows could not have under-written the exchange rate exposure because only 25% of such borrowers received remittance income in 2014, reducing to 13% in 2016.

- The major trade sector exposures of the 'income source' borrower segments are shown in the following table:

	Retail	Service	Public Sector	Engineering	Agriculture
MFI					
Regular Work	8%	18%	65%	2%	9%
Irregular Work	8%	46%	7%	21%	17%
Own Business	71%	22%	7%	3%	7%
Bank					
Regular Work	5%	21%	63%	2%	9%
Irregular Work	13%	45%	8%	18%	19%
Own Business	71%	21%	5%	2%	7%

  - Such different concentrations of trade sector exposures will necessarily cause the respective borrowers to be subject to varying economic, seasonal and social influences;
  - The lending proposition / strategy and problem loan management should, therefore, recognise, and anticipate, the particular characteristics of each of these segments.
- Informal borrowings and budget adjustment initiatives suggest the actions being undertaken by individuals to maintain up-to-date loan repayments:

	Regular Work		Irregular Work		Own Business	
	MFI	Bank	MFI	Bank	MFI	Bank
Loan: Family	8%	6%	15%	13%	6%	9%
Loan: Friends	12%	13%	21%	24%	12%	16%
Retailer Loan: Domestic	21%	22%	30%	23%	10%	10%
Arrears with Utilities	12%	15%	16%	16%	9%	8%
Food expenditure has been reduced to make loan repayments	38%	44%	53%	50%	39%	42%
I (or my spouse) have taken additional work to make loan repayments	23%	40%	21%	26%	41%	24%

  - These responses show a high level of recourse to informal loan / funding sources in addition to loans from either MFIs and banks.

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

34% of loan funds used for domestic consumption and 20% used for health and education by borrowers in 'regular work' – 65% of 'own business' loans were used primarily for business purposes, but 20% was used primarily for domestic expenditure needs.

- The profile of the use of loan funds is shown in the following table:

	Business: Asset	Business: Trading	Domestic: Asset	Domestic: Expenses	Property Acquisition	Property: Improve	Health / Edu/ Family
MFI	3%	27%	7%	27%	9%	9%	17%
Bank	3%	32%	6%	25%	9%	9%	14%

  - Within the above figures, the primary use of loan funds by ‘regular work’ / employed and ‘own business’ clients was:

	Business: Asset	Business: Trading	Domestic: Asset	Domestic: Expenses	Property Acquisiti on	Property: Improve	Health / Edu / Family
Regular work	2%	7%	9%	34%	13%	12%	20%
Own Business	4%	65%	2%	10%	3%	4%	9%

- The tables indicate:
  - ‘Own Business’: primary use of funds from last loan - 65% of borrowers for business purposes, 10% for domestic consumption, and 9% for health or education. However, it must be noted that ‘own business’ clients had higher incomes and may, therefore, be taking the loan funds on an indirect basis by means of withdrawal of business takings;
  - The use of funds for domestic consumption (c.25%) reflects short-term usage being undertaken against medium-term (12-18 months) loan periods. Interest is currently charged at about 35-40% nominal (c.75% APR) and this represents a substantial increase in the real ‘total cost’ of the domestic consumption;
  - The scale of usage of funds for specific personal needs (health, education) is greater than the usage of the respective loan product. Internet research shows that [some] institutions have a range of loan products available to clients, but the survey responses indicate that these are not being fully used.
- The usage of loan funds changes in relation to the level of household income:

	Business: Asset	Busines s: Trading	Domest ic: Asset	Domest ic: Expense s	Propert y Acq’n	Propert y: Improv e	Health / Education / Family Event
< 1,200	2%	9%	7%	46%	9%	8%	18%
1,201-1,800	2%	17%	9%	32%	10%	11%	18%
1,801-2,600	2%	25%	7%	27%	11%	9%	18%
2,601-3,400	3%	32%	6%	23%	10%	9%	16%
>3,400	5%	48%	5%	15%	6%	8%	11%

  - This table shows the strong and greater usage of loan funds for domestic consumption by lower income households;
  - The perception of debt dependency to support domestic consumption by the low income segments is particularly important. The average monthly interest component

of a TJS 3,500 loan over 12-18 months is about TJS100-120 … this is broadly equivalent to the average current expenditure per person for monthly food and essential needs. It is possible that a significant proportion of lower income households may have a stronger domestic budget / greater disposable income if loans were not used for domestic consumption purposes;

  - This suggests a need for significant financial education … and possibly suggests that lower-income borrowers are not aware of the interest component of the loan repayment but, rather, understand only the total amount which needs to be paid each month.

- The different impacts of the usage of loan funds on credit performance is shown below:

	Net Disposable Income (after loan)	Arrears: Loan	Arrears: Utility	Refinance / reschedule of loan in last 12 months	Difficulty to make loan repayments	Food expenditure reduced to make loan repayments
Business: Trading	833	22%	7%	16%	52%	41%
Domestic Expenses	669	10%	9%	9%	46%	36%
Health / Education	719	12%	14%	11%	53%	49%
Property: Acquisition	695	10%	14%	7%	45%	30%
Property: Improvement	774	11%	19%	7%	47%	39%

  - This indicates that, other than loan arrears with ‘own business’ and foreign currency loans, the impact of problem lending is well-spread through the different segments of loan usage.

- The perceptions by the borrower of the need to continue to borrow are reflected in the following table:

% of Borrowers in each Segment	Total expenditures (inc. loan repayment) greater than 75 % of Income	Loans improve the quality of life	I need / needed to continue to borrow to maintain how my family and I live	Informal Loan from Retailer: Domestic Consumption	I would like help to resolve debt problems with my lending institution
Business: Trading	60%	66%	85%	9%	53%
Domestic Expenses	55%	76%	80%	18%	60%
Health / Education	48%	68%	81%	21%	46%
Property: Acquisition	54%	68%	75%	16%	50%
Property: Improvement	55%	63%	78%	24%	55%

  - This shows the entrenched attitudes towards the need to borrow, despite the financial pressures which are being experienced.

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

64% of former borrowers did not have a current loan – former borrowers who obtained loans by moving from MFI to bank, or vice versa, had a high level of arrears (23%) and a higher level of outstanding loan balances – former borrowers, now non-borrowers, gad a much higher level of net disposable income.

- The survey obtained the responses of former borrowers of both MFIs and banks, and were selected based on those who had ceased to borrow from that type of lending institution within the last 2 years. These respondents have two principal segments: [i] those who subsequently obtain a loan from the other type of institution (that is an MFI client moving to a bank, or vice versa); and [ii] those clients who ceased to borrow at all.
- The principal characteristics of these segments are:
  - Strong similarities in the actions of the former borrowers of both types of institution, 36% of such former borrowers had obtained a loan from the other type of institution, and 64% did not have a loan at the time of the survey;
  - Average age of the non-borrowers was slightly younger;
  - Non-borrowers had slightly lower average level of dependents;
  - Non-borrowers had a higher level of single / non-married persons;
  - Borrowers showed higher-than-average levels of loan arrears:
    - former MFI now with a loan with a bank : 23%
    - former bank now with a loan with an MFI: 22%
  - The levels of savings were broadly similar across these segments. The ‘non-borrowers’ showed a higher level of savings with a financial institution, but this was at a low level of only 12%.
- The financial budget profiles are shown in the following table:

	Income	Household costs	Utility costs	Loan Repayments	Net Disposable Income (after Loan)
Former MFI: Bank Loan	3,382	1,175	163	1,346	699
Former MFI: No Current Loan	2,530	1,116	194		1,221
Former Bank: MFI Loan	2,998	1,207	133	895	763
Former Bank: No Current Loan	2,524	1,169	180		1,174

  - The significant dimensions of this table are:
    - The non-borrowers have, on average, lower income levels – and were, therefore, possibly most affected by the structural redistribution towards higher income borrowers. 80% of the ‘non-borrower’ clients indicate that they consider debt as a means of maintaining the lifestyle of their family.
    - Despite the higher income levels of those clients who continued to borrow, the ‘non-borrowers’ have a significantly higher level of net disposable income (after loan costs). The responses do not show that the respondents recognise the impact of this higher cash liquidity.

        - Non-borrowers maintained similar levels of essential household expenditures as the 'borrowers'.
    - Former MFI clients, with a current loan from a bank had a higher loan balance (TJS 16,958) than the average for all bank loans (TJS 11,282);
    - Former bank clients, with a current loan from an MFI had a higher loan balance (TJS 9,970) than the average for all MFI loans (TJS7,460);
    - This profile of higher loan balances by 'former borrowers' was also seen in the 2014 survey responses.
- The 'income sources' of these client segments show a strong differentiation in relation to 'irregular work' and 'own business'.

Source of Income: Distribution % within each segment	Regular work	Irregular work	Own business	Remittance
Former MFI: Bank Loan	44%	16%	47%	16%
Former MFI: No Current Loan	47%	21%	28%	18%
Former Bank: MFI Loan	47%	9%	45%	20%
Former Bank: No Current Loan	44%	20%	32%	17%

- The attitudes of the 'former' segments of MFI and bank clients present some what different profiles.

% of respondents who 'Agree'	My financial situation has improved in the last 6 months	The quality of my life has improved in the last 12 months	Loans improve the quality of life	Loans were easy to obtain
Former MFI: Bank Loan	53%	55%	79%	67%
Former MFI: No Current Loan	67%	70%	65%	77%
Former Bank: MFI Loan	66%	65%	75%	77%
Former Bank: No Current Loan	65%	65%	71%	69%

- These responses suggest:
    - There are different perceptions between MFI and bank clients, which may suggest that these institutions have different client and delivery propositions;
    - MFI clients have a more positive reaction to not borrowing than bank clients;
    - Nevertheless, it does seem that the majority continue to see loans as a positive contribution to their lives.

3 LENDING INSTITUTIONS AND LENDING PORTFOLIOS

3.1 What are the principal financial characteristics of borrowers?

Significant variation of income growth in different trade sectors – public sector wages most constrained – major variations in risk exposure across the regions – shift in the number of loans towards lower balances – reduction in new / renewal loans in January-June 2016 (compared with 2014 survey).

- The following comments relate to the major generic client segments across the borrowing population and thereby span both MFIs and banks. 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 level of overlap between MFI and bank client bases, with MFIs having a greater proportion (by only 5%) of the lowest income segment (<TJS 1,200) and banks having only 4% more in the highest income segment (>TJS 3,400);
        - These differences are almost unchanged from the income profiles in the 2014 survey.

- **Trade Activity**: Financial: the principal trading activities which underpin the income of borrowers are agriculture, retail, service, and public sector

	Household Income TJS	Household & Utility Costs	Net Disposable Income NDI (pre Loan)	Average Outstanding Loan Balance	Net Disposable Income NDI (after Loan)
Agriculture	2,764	1,280	1,484	5,593	809
Retail	3,862	1,539	2,323	15,774	905
Service	3,080	1,373	1,707	8,447	746
Public Sector	2,390	1,216	1,174	4 ,052	711

    - The levels of household essential expenditures are broadly similar, with retail somewhat higher reflecting the higher average incomes;
    - The impact of different levels of loan leverage are clearly reflected in the residual net disposable incomes;
    - See also Attachment 4 for national trends in trade sector income levels.

- The change in income levels in the major trade sectors varied significantly between 2014 and 2016.

	Household Income			Average income per wage-earner		
	2014	2016	Change	2014	2016	Change
Retail	3,420	3,862	13%	1,520	1,737	14%
Engineering	2,333	2,484	6%	894	1,183	32%
Building - Property	2,814	3,081	9%	1,270	1,431	13%
Service	2,564	3,080	20%	1,037	1,375	33%
Agriculture	2,427	2,764	14%	894	1,128	26%
Public Sector	2,523	2,390	-5%	1,045	1,070	2%

    - Public Sector employees accounted for 58% of those survey respondents who were in ‘regular employment’.

- Trade Activity: the scale of ‘problem repayment’ borrowers varies between these major sectors and is reflected in the following indicators.

	Loan Arrears Overall average = 15%	Utility Arrears Overall average = 12%	My loan repayments are more than I can afford	Debt repayments cause problems within my family	Food expenditure reduced for loan repay	I would like help to resolve debt problems with my lending institution
Agriculture	16%	6%	41%	32%	25%	38%
Retail	21%	7%	54%	50%	40%	53%
Service	17%	11%	51%	53%	46%	52%
Public Sector	11%	16%	48%	45%	41%	53%

- o The financial pressures are being experienced and recognised by borrowers across the major sectors.

Although the agricultural segment shows the lowest adverse impact, the above responses show a deterioration in comparison with 2014.

- **Region**: Financial

	Household Income TJS	Household & Utility Costs	Net Disposable Income NDI (pre Loan)	Average Outstanding Loan Balance	Net Disposable Income NDI (after Loan)
Dushanbe	4,457	1,692	2,766	19,152	989
Khatlon	2,516	1,197	1,319	6,484	611
Sogd	2,653	1,236	1,417	4,874	842
RRP	2,570	1,303	1,366	4,517	719
GBAO	2,525	1,286	1,239	7,394	723

- o Major differences in these regional positions will impact upon the need for differentiated credit assessment processes and budget guidelines;
- o The inflationary pressures upon non-foodstuff expenditures in recent years places substantial pressure upon the residual net disposable income shown above.

- Region: Problem Lending

	Loan Arrears Overall average = 15%	Utility Arrears Overall average = 12%	My loan repayments are more than I can afford	Debt repayments cause problems within my family	Food expenditure reduced for loan repay	I would like help to resolve debt problems with my lending institution
Dushanbe	21%	10%	56%	58%	48%	51%
Khatlon	18%	6%	66%	52%	44%	51%
Sogd	13%	6%	42%	45%	35%	39%
RRP	13%	7%	32%	32%	23%	37%
GBAO	8%	30%	54%	46%	54%	83%

- Some significant variations are evident across these regions;
- The apparent pressures in GBAO (albeit not shown in the loan arrears levels) are further reflected in substantially higher levels of informal loans from friends and retailers;
- These different regional characteristics are substantial. This suggests the need for differentiation in the credit management processes across the regions.

- **Age**: Financial

	Household Income TJS	Household & Utility Costs	Net Disposable Income NDI (pre Loan)	Average Outstanding Loan Balance	Net Disposable Income NDI (after Loan)
16-25	3,322	1,440	1,881	5,061	1,129
26-35	2,738	1,253	1,485	8,135	724
36-45	2,869	1,292	1,577	7,577	757
46-55	3,195	1,407	1,788	11,401	717
> 55	2,867	1,337	1,531	11,339	563

- Surprisingly little difference between the income and household expenditure levels across the age range;
- The higher debt levels of 46 years and older reflect underlying demand from these age segments:
  - No significant different levels of retail trade sector;
  - No significant differences in the proportion of clients with foreign currency loans;
  - No significant differences in the loan purpose / usage of funds;
  - The sample size (177 respondents) of the >55 segment was relatively small, but the sample size of the 46-55 segment was significant (721 respondents).

- 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.

	Loan Arrears Overall average = 15%	Utility Arrears Overall average = 12%	My loan repayments are more than I can afford	Debt repayments cause problems within my family	Food expenditure reduced for loan repay	I would like help to resolve debt problems with my lending institution
16-25	14%	9%	42%	42%	33%	41%
26-35	17%	12%	50%	45%	42%	51%
36-45	12%	12%	53%	47%	42%	54%
46-55	15%	12%	49%	49%	40%	56%
> 55	14%	11%	52%	51%	44%	53%

- **Loan Amount:**

- Distribution of outstanding loan balances:

  There has been an overall shift in the loan portfolios of both MFIs and banks towards lower outstanding balances. The comparative distributions of the number of outstanding loan balances are shown in the following table to contrast the situations in 2014 and 2016.

Distribution of Outstanding Loan Balances	< 1,500	1,501-3,000	3,001-5,000	5,001-10,000	> 10,000	Average
2016						
MFI	29%	27%	18%	14%	13%	7,460
Bank	26%	21%	17%	14%	22%	11,282
2014						
MFI	21%	27%	23%	15%	14%	6,936
Bank	13%	20%	23%	24%	19%	8,695

Change: 2016 - 2014	< 1,500	1,501-3,000	3,001-5,000	5,001-10,000	> 10,000	Average
MFI	+8%	-	-5%	-1%	-1%	+ 8 %
Bank	+13%	+1%	-6%	-10%	+3%	+ 30 %

The devaluation of the TJS / US$ exchange rate had, of course, a very substantial impact upon the TJS equivalent for foreign currency loans. The following table provides, therefore, distributions of domestic and foreign currency lendings in 2016. (A more detailed assessment of currency lending is undertaken elsewhere in this review).

Distribution of Outstanding Loan – based upon number of loans	Outstanding Loan Balances: 2016 TJS equivalent					
	< 1,500	1,501-3,000	3,001-5,000	5,001-10,000	> 10,000	Average
TJS Somoni	30%	26%	18%	14%	13%	6,734
Foreign Currency	10%	13%	13%	16%	47%	32,394

Nevertheless, there has been a substantial and significant shift in the portfolio distribution in relation to the number of clients with lower outstanding balances. The following table shows that this reflects, in large measure, an increased ageing of outstanding loans and an apparent slowdown in the approval and/or drawdown of new loans in recent months.

Period since last loan was taken	Within 1 month	1-3 months	4-6 months	7-12 months	Over 12 months
2016					
MFI	5%	13%	23%	38%	20%
Bank	6%	11%	19%	35%	29%
2014					
MFI	4%	16%	32%	36%	11%
Bank	4%	17%	33%	37%	9%
Change					
MFI	+1%	-3%	-9%	+2%	+9%
Bank	+2%	-6%	-14%	-2%	+20%

- Structure of Outstanding Loans

Outstanding Loan Amount	TJS Currency	Foreign Currency	Refinance / reschedule in last 12 months	Collateral pledge of assets	Last loan over 12 months ago
< 1,500	98%	2%	6%	20%	19%
1,501-3,000	96%	4%	8%	26%	17%
3,001-5,000	95%	5%	10%	36%	22%
5,001-10,000	92%	8%	15%	48%	29%
> 10,000	79%	21%	25%	62%	33%

  - The impact of foreign currency lending in the largest loan balances contrasts sharply with the other segments;
  - The higher level of loan reschedule amongst the largest loans is not reflected in higher loan arrears (see next comments);
  - Higher levels of collateral are held for the higher value loans.

- Loan Amount: Problem Lending

Loan Amount	Loan Arrears Overall average = 15%	Utility Arrears Overall average = 12%	My loan repayments are more than I can afford	Debt repayments cause problems within my family	Food expenditure reduced for loan repay	I would like help to resolve debt problems with my lending institution
< 1,500	11%	12%	43%	42%	33%	50%
1,501-3,000	10%	12%	46%	41%	39%	50%
3,001-5,000	12%	12%	51%	46%	43%	51%
5,001-10,000	22%	11%	60%	53%	45%	53%
> 10,000	26%	11%	59%	58%	50%	59%

  - Taken together, these reflect the substantive financial pressures being experienced by borrowers;
  - Whilst all loan amounts show debt repayment pressures, this is clearly most acute in the largest value loans. This represents a significant concentration of

risk. In relation to loans greater than TJS 10,000, this accounted for [i] 13% of MFI borrowers with 65% of loan value, and [ii] 22% of bank borrowers with 78% of loan value;

- Such focused credit risk exposure requires particular credit management skills which are different from those applicable to lower value loans.

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.

Similar strategies between 2014 and 2016 to reduce proportion of lower income borrowers – both MFIs and banks have increased the proportion of clients with lower outstanding loan balances – both MFIs and banks have reduced the level of loan approvals in last 6 months – levels of problem lending are similar – banks continue to higher value loans and higher leverage – similar usage of loan product types

- There is a high level of overlap in the comparative distributions of client numbers in relation to the range of household incomes and the amount of outstanding loans.

Income Range: TJS	Distribution: Clients				Loan Balance: TJS	Distribution: Clients			
	MFI		Bank			MFI		Bank	
	2014	2016	2014	2016		2014	2016	2014	2016
< 1,200	19%	14%	13%	11%	< 1,500	21%	29%	13%	26%
1,201-1,800	19%	19%	18%	17%	1,501-3,000	27%	27%	20%	21%
1,801-2,600	27%	25%	28%	27%	3,001-5,000	23%	18%	23%	17%
2,601-3,400	14%	17%	15%	17%	5,001-10,000	15%	14%	24%	14%
>3,400	21%	25%	26%	28%	> 10,000	14%	13%	19%	22%

- This table shows that both the MFIs and banks have pursued similar strategies in relation to:
  - Upward shift in the income distribution of clients;
  - Downward shift in the distribution of outstanding loan balances.

- Location: Financial

	Household Income TJS	Household & Utility Costs	Net Disposable Income NDI (pre Loan)	Average Outstanding Loan Balance	Net Disposable Income NDI (after Loan)
City - MFI	3,093	1,426	1,668	8,779	868
City - Bank	3,554	1,461	2,093	13,822	859
Urban - MFI	2,756	1,262	1,494	7,632	712
Urban - Bank	3,127	1,321	1,806	11,047	702
Rural - MFI	2,512	1,197	1,315	5,458	728
Rural - Bank	2,600	1,426	1,668	7,453	651

- Banks consistently attract clients with slightly higher household and 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

	Arrears: Loan	Loan Refinance / Reschedule in last 12 months	Informal Loan: Friends	My loan repayments are more than I can afford	Food expenditure reduced for loan repay	I would like help to resolve debt problems with my lending institution
City - MFI	15%	7%	12%	52%	44%	54%
City - Bank	16%	9%	15%	56%	46%	57%
Urban - MFI	13%	14%	9%	49%	37%	52%
Urban - Bank	19%	17%	13%	48%	40%	54%
Rural - MFI	14%	13%	19%	44%	39%	43%
Rural - Bank	16%	17%	18%	53%	41%	53%

- Problem debt is consistently higher for the bank clients in the respective locations;
- Loan refinance is significantly lower in the city areas. The proportion of currency loans is broadly similar; across the locations (except by banks in city locations). It may have been anticipated, therefore, that refinance levels would be similar in city locations. The survey responses suggest that either [i] there is a different operational credit management strategy being used, or [ii] 'refinance' actions are being undertaken under a different methodology.

- **Income**: Range: Financial

This segmentation is based upon clients in the various income segments.

Income Range / TJS	Net Disposable Income NDI (pre Loan)		Average Outstanding Loan Balance		Net Disposable Income NDI (after Loan)	
	MFI	Bank	MFI	Bank	MFI	Bank
< 1,200	353	375	2,452	2,742	100	92
1,201-1,800	674	656	2,825	3,703	305	238
1,801-2,600	1,003	1,037	4,132	4,231	495	516
2,601-3,400	1,506	1,559	6,954	8,671	840	798
>3,400	3,356	4,016	16,337	25,663	1,839	1,801

- The leverage of bank clients is consistently higher than that of MFI clients at all income levels – and particularly for the highest income segments;
- Against broadly similar demographic profiles, the MFIs and banks are presenting similar loan product and service propositions – with the banks differentiating by slightly higher loan amounts;

- The lowest income segments (up to TJS 1,800) show a highly marginal financial situation. This high vulnerability is exacerbated by the stronger levels of inflation in relation to non-foodstuffs;
- This represents a continuing and worsened structural risk exposure – which was also identified by the 2014 survey.
- This is, therefore, a situation for particular review by the lending institutions to determine the levels of net disposable income across the different client segments.

- Income: Range: Leverage of Loan Repayments
  - Lending by banks continues to be undertaken at significantly higher leverage ratios than those undertaken by the MFIs.

Income Range / TJS	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
< 1,200	100	92	26%	29%	72%	76%
1,201-1,800	305	238	24%	27%	55%	64%
1,801-2,600	495	516	23%	24%	51%	50%
2,601-3,400	840	798	22%	25%	44%	49%
>3,400	1,839	1,801	28%	36%	45%	55%

- This suggests:
  - A general industry standard of loan repayments across most income ranges of about 25% of household income. This appears to be applied by both banks and MFIs;
  - However, the impact of essential food and household expenditures highlights the relative higher commitment of loan repayments by the lower income segments. (It should be recognised that the ratios for the lowest income segment is much reduced from 2014);
  - This increases significantly the exposure and sensitivity to external risks.
- The scale of exposure to the lower income segments emphasises the significance of these attitudes and financial vulnerability. Again, there is a high level of similarity of the client and loan value distributions.

Income Range / TJS	Distribution: Clients		Distribution: Loan Value	
	MFI	Bank	MFI	Bank
< 1,200	14%	11%	5%	3%
1,201-1,800	19%	17%	8%	6%
1,801-2,600	25%	27%	14%	11%
2,601-3,400	17%	17%	17%	14%
>3,400	25%	28%	56%	67%

- **Loan Product / Type**: Financial

	Household Income TJS	Household & Utility Costs	Net Disposable Income NDI (pre Loan)	Average Outstanding Loan Balance	Net Disposable Income NDI (after Loan)
Business: TJS	3,734	1,536	2,198	16,239	740
Business: Fgn Ccy	6,975	2,067	4,908	50,224	1,172
Individual Fixed: TJS	2,721	1,270	1,451	6,250	808
House / Property: TJS	2,550	1,210	1,340	6,954	604
Group: TJS	2,339	1,138	1,201	4,972	791
Agriculture: TJS	2,684	1,308	1,376	5,624	708
Education: TJS	2,331	1,219	1,112	2,789	773

  - This table highlights the significant differences between loan products. However, the large majority of loan are undertaken by:
    - Individual fixed term: MFI 59% Bank 56%
    - Business loans: MFI 18% Bank 23%

- Loan Product / Type: Problem Lending

Loan Product	Loan Arrears Overall average = 15%	Have you refinanced / consolidated your debts during the last 12 months	My loan repayments are more than I can afford	Debt repayments cause problems within my family	Food expenditure reduced for loan repay	I would like help to resolve debt problems with my lending institution
Business: TJS	23%	17%	57%	57%	45%	57%
Business: Fgn Ccy	44%	23%	67%	63%	62%	52%
Individual Fixed: TJS	10%	10%	47%	42%	38%	49%
House / Property: TJS	13%	13%	60%	55%	42%	63%
Group: TJS	11%	13%	48%	44%	39%	74%
Agriculture: TJS	19%	7%	44%	36%	39%	45%
Education: TJS	12%	11%	43%	47%	48%	37%

  - The concentration of pressures in foreign currency and business lending is clearly demonstrated;
  - The difference between the visibility of ‘arrears’ and the recognition of repayment difficulty is extremely wide across all products. This emphasises further the vulnerability of these loan portfolios to any continuation of the wider economic pressures in the market.

- **Savings**: Financial

Note: The level of savings with a financial institution is relatively low (only 8% of all borrowers), although the incidence of savings through other mechanisms is higher.

- The level of savings is low with financial institutions, although a minority of borrowers do undertake savings through other mechanisms.

	2014			2016		
	Do you make savings with a financial institution	Do you make other savings	Have you bought an insurance product(s) from your financial institution	Do you make savings with a financial institution	Do you make other savings	Have you bought an insurance product(s) from your financial institution
MFI	8%	25%	5%	10%	26%	9%
Bank	9%	26%	6%	10%	26%	8%

- The budget profiles of 'savers' and 'non-savers' are shown in the following table:

	Household Income TJS	Household & Utility Costs	Net Disposable Income NDI (pre Loan)	Average Outstanding Loan Balance	Net Disposable Income NDI (after Loan)
Savings: FI: Borrowers	3,306	1,501	1,805	9,672	1,131
Other Savings: MFI	3,120	1,368	1,752	7,763	1,052
Other Savings: Bank	3,802	1,457	2,345	12,370	1,249
No Savings: MFI	2,706	1,275	1,432	7,500	673
No Savings: Bank	2,945	1,320	1,625	11,082	567

  - This shows that the financial institutions are not use as a primary savings mechanism.
  - The 'non-savers' have much lower net disposable incomes.

- Savings: Problem Lending

	Loan Arrears Overall average = 15%	Have you refinanced, or consolidated your debts during the last 12 months	My loan repayments are more than I can afford	Debt repayments cause problems within my family	Food expenditure reduced for loan repay	I would like help to resolve debt problems with my lending institution
Savings: FI: Borrowers	8%	11%	48%	46%	41%	51%
Other Savings: MFI	11%	8%	30%	32%	29%	38%
Other Savings: Bank	10%	8%	31%	35%	26%	39%
No Savings: MFI	15%	12%	56%	50%	44%	56%
No Savings: Bank	20%	15%	62%	57%	49%	61%

- The financial pressures upon the ‘other savings’ segments appear to be at lower levels;
- The ‘non-saver’ segments show highest levels of financial strain;
- The segment with savings with a financial institution present a paradox. Although the arrears are low, the other indicators display an adverse situation. These savings may be linked with the loan product, perhaps under some form of hypothecation. A similar structure was shown in the 2014 survey.

3.3 Do the survey responses indicate credit standards or criteria?

Overall, banks provide higher loans and higher leverage ratios than those taken by MFI borrowers – the leverage ratios are highest amongst the lowest income groups – major improvement of loan repayment leverage since 2014 by both MFIs and banks in relation to lower income segments–such improvements in the operational credit measures have been overtaken by the wider portfolio and systemic risks of economic and market pressures, resulting in a deterioration of the loan portfolio quality – nevertheless, without the operational credit actions which been taken, the portfolio performance may be anticipated to have been much worse.

The survey responses show the differences in the loan leverage between MFI (lower leverage) and bank clients (higher leverage). Whilst other responses show an increasing recognition by many borrowers of the difficulties to manage their debt levels and loan repayments, the following tables demonstrate some characteristics of the relationship of debt to income, which reveal the dimensions of pressures being faced.

- The level of debt repayments may be considered in relation to household income. These aggregate figures reflect a range of committed expenditures across the income ranges:

Household Income	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)	
	2014	2016	2014	2016	2014	2016
< 1,200	64%	63%	51%	27%	143%	73%
1,201-1,800	57%	57%	38%	25%	87%	58%
1,801-2,600	57%	53%	31%	23%	72%	50%
2,601-3,400	49%	49%	25%	23%	50%	45%
>3,400	36%	36%	28%	32%	43%	50%

  - This table presents some critical perspectives of the credit risk process, based on the quantitative financial positions reported by borrowers[9];
  - 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 income segments are less, the real cost of loan repayments, in relation to available net disposable income, remains significantly higher for low income groups (as shown in the final two columns of the above table);

[9]Data quality was reviewed and validated by the independent research agency which undertook the survey interviews. Additionally, the similarity of responses from different client segments (MFI and bank) and the relationship between responses at different income levels provides support for the appropriateness of these quantitative evaluations.

- o 31% of clients (MFI: 33% and Bank: 28%) are in the lowest two income segments;
- o The lending institutions have clearly undertaken some fundamental changes since 2014 to address the affordability of loan repayments by the lower income segments. This appears to represent a major re-structure of the loan portfolio – and appears to demonstrate a responsible approach to the provision of lending;
- o This is reflected in the following table which highlights the substantial changes made by the lending institutions.

Household Income	MFI				Bank			
	Loan Repayment as % of Total Household Income		Loan Repayment as % of Net Disposable Income (pre loan repayments)		Loan Repayment as % of Total Household Income		Loan Repayment as % of Net Disposable Income (pre loan repayments)	
	2014	2016	2014	2016	2014	2016	2014	2016
< 1,200	49%	26%	145%	72%	59%	29%	150%	76%
1,201-1,800	38%	24%	88%	55%	39%	27%	89%	64%
1,801-2,600	29%	23%	67%	51%	35%	24%	82%	50%
2,601-3,400	23%	22%	46%	44%	28%	25%	55%	49%
>3,400	25%	28%	39%	45%	31%	36%	49%	55%

- o This table shows that both MFIs and banks have addressed the challenge of loan affordability for the lower income segments which was shown in 2014;
- o This adjustment is likely to have been achieved by some mixture of lower loan amounts and/or refusal to lend to the most financially marginal clients;
- o This structural revision needs to be considered in the wider context of the significant deterioration of the credit quality of the overall loan portfolio:
    - ▪ Excluding the foreign currency lending (and the particular effects of the TJS Somoni devaluation against the US$), the fundamental core 'affordability' of loan repayments was structurally improved by the lending institutions;
    - ▪ **The 2016 deterioration is credit quality does not, therefore, appear to be primarily attributable to disproportionate borrower expenditures or operational risk – the lending institutions have addressed the 'affordability' issues at an individual borrower level. Without such structural actions, the credit performance of the loan portfolio, and the impact upon borrowers and society, would have been much more severe;**
        - ▪ The 2016 credit deterioration principally reflects, therefore, portfolio and systemic risks – which are reviewed in the initial broader evaluation of the 2016 survey findings.

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

Similar severe adverse deterioration of 'own business' segment for both MFIs and banks –strong concentration in retail sector – banks have larger exposure to higher value loans – pressures on 'own business' segment present a major structural risk exposure to lending institutions.

- The ‘own business’ segment of borrowers has demonstrated a high level of credit deterioration between 2014 and 2016. Such borrowers represent an important segment of business for the lending institutions – such clients being characteristically higher income and higher loan values – and are an important economic component of the community. The incomes and loans of the ‘own business’ segments in the 2014 and 2016 surveys are shown below.

	Household Income: TJS		Ave. Loan Balance: TJS		Arrears		Business Failure	
	2014	2016	2014	2016	2014	2016	2014	2016
MFI	3,175	3,560	9,852	13,106	3%	20%	20%	37%
Bank	3,345	4,160	12,059	16,719	3%	23%	15%	43%

- There is a similar distribution of ‘own business’ across the type of location
    - MFI: 40% in city locations; 38% in rural locations; 23% in urban locations;
    - Bank: 41% in city locations; 37% in rural locations; 22% in urban locations;
    - The level of ‘own business’.
- There is also a great similarity in the trade sectors which are supported.

Total Loan Portfolio	Manufacture	Food Production	Retail	Engineering	Building - Property	Service	Agriculture
MFI	2 %	4 %	71 %	3 %	1 %	22 %	7 %
Bank	2 %	3 %	71 %	2 %	2 %	21 %	7 %
2014							
MFI	2 %	4 %	31 %	5 %	6 %	15 %	20 %
Bank	3 %	3 %	29 %	4 %	7 %	16 %	24 %

- *Care*: The above table reflects the survey responses and thereby provides a comparative profile of MFIs and banks – it does not purport to reflect a nationally-weighted sample – each lending institution will have its own mix of ‘own business’ activity. However, the similarity and scale of the changes between 2014 and 2016 are similar for both MFIs and banks which suggests that the ‘directional trends’ are appropriate (even if not to a determined statistical confidence level):
    - This table shows a major change in concentration towards the retail segment. This is a ‘low entry – low exit’, low technology, [potentially] lower experience segment which offers relatively short-term opportunities for start-up situations. Such characteristics are likely to sustain short-term price competition, which will necessarily constrain the rate at which problem debt can resolved;
    - This ‘vulnerability’ of the retail sector is reflected in the highest level of business failures (40%) and arrears (21%) amongst retail borrowers – resulting in this sector being the highest credit risk segment;
    - The lower exposure of retail in the urban and rural communities may suggest the particular local economic pressures which may have occurred in those locations. Such absence / constrained impact on demand levels would constrain the capacity for any expansion of retail activities.

- 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: TJS				
	< 1,200	1,201-1,800	1,801-2,600	2,601-3,400	>3,400
MFI	5%	13%	24%	20%	37%
Bank	2%	11%	22%	21%	44%
2014					
MFI	16%	18%	27%	11%	29%
Bank	9%	18%	29%	13%	32%

  - The average incomes for these 'own business' clients [a] MFI TJS 3,560 and [b] Bank TJS 4,160 are higher than for other client segments.

- The product structure for the 'own business' segment is also similar across the MFIs and banks, as shown in the following table:

Type of Loan to 'Own Business': TJS currency only	Group	Business	Individual	Agricultural
MFI	4%	42%	47%	2%
Bank	2%	45%	42%	2%
2014				
MFI	5%	73%	26%	4%
Bank	3%	75%	24%	4%

  - The similarity of the loan product / delivery propositions of MFIs and banks is extremely strong with little differentiation;
  - These represent highly similar service and delivery propositions by the lender with minimal levels of flexibility to the borrower. 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 distribution of loan balances shows a greater similarity between MFIs and banks than in 2014, with the exception of a concentration of high value loans with banks (reflecting foreign currency exposure).

% of borrowers	Outstanding Loan Balance of 'Own Business' Borrowers: TJS				
	< 1,500	1,501-3,000	3,001-5,000	5,001-10,000	> 10,000
MFI	20%	22%	17%	18%	23%
Bank	18%	14%	16%	16%	36%
2014					
MFI	13%	23%	25%	17%	22%
Bank	7%	14%	20%	32%	27%

- This results in a difference in the average outstanding loan balances: MFI average of TJS 13,100 and Bank average of TJS 16,700.

3.5 Collateral Security – does it affect lending?

Outstanding loans with collateral are much higher than those which are non-collateralised – higher leverage costs erode any higher income differential – loan arrears almost double amongst collateral borrowers– no increase in the incidence of collateralisation since 2014 which suggests that collateral opportunities are now saturated – number of guarantees given by borrowers almost doubled between 2014 and 2016, but no differentiation in the underlying credit quality of the guarantor.

- The extent of assets pledged as security is:
  - MFI: 30% (2014 -37%) of borrowers;
  - Bank: 43% (2014 - 42%) of borrowers.
  - Within these levels, the incidence of asset collateralisation is higher amongst borrowers in the following segments:
    - MFI: Foreign Currency 60% (2014 – 58%)
    - Bank: Foreign Currency 66% (2014 – 50%)
    - 'Own Business': TJS Currency 38%
    - GBAO Region 51% (2014 – 72%)
    - Former MFI clients, now with bank loans 44% (2014 - 51%)
    - Former bank clients, now with MFI loans 31% (2014 - 46%)
    - The incidence of collateral has reduced over the last 2 years – (from 39% of borrowers to 35%); however, the amount of outstanding loan balance covered by collateral has remained unchanged for both MFIs and banks.
  - As the levels of collateral have remained broadly unchanged (slightly reduced), it may suggest that the lending institutions have not been able to obtain further assets – and that this form of lending support has been saturated. (This should be contrasted with the growth of guarantees – see later).
- The distribution of the collateral loan portfolios of the lending institutions is shown below:

	Collateralised Lending				Household Income		Outstanding Loan	
	% of Borrowers		% of Loan Balances					
	2014	2016	2014	2016	2014	2016	2014	2016
MFI	37%	30%	57%	59%	2,728	3,338	10,684	14,408
Banks	42%	43%	61%	62%	3,132	3,432	12,546	14,012

  - The proportion of clients providing collateralised assets has not increased since 2014, which suggests that the availability of such support has been saturated;
  - The comparative levels of incomes and loans for collateralised and non-collateralised borrowers is shown below.
- The financial profile of the collateral segments is shown in the following table:

TJS	Household Income	Household & Utility Costs	Loan Repayment	Net Disposable Income NDI (after Loan)	Average Outstanding Loan Balance
MFI: Collateral	3,338	1,430	1,187	721	14,408
MFI: No llateral	2,582	1,248	531	803	4,212
Bank:Collateral	3,432	1,400	1,275	757	14,012
Bank: No Collateral	2,833	1,304	783	747	6,239
2014					
MFI:Collateral	2,700	1,150	1,050	500	10,700
MFI: No Collateral	2,650	1,300	600	750	4,700
Bank:Collateral	3,150	1,200	1,350	600	12,500
Bank: No Collateral	2,700	1,400	700	600	5,900

- The income differential between borrowers with, and without, collateral has increased;
- Such higher income is eroded by the impact of higher leverage and loan repayments, with a resultant minimal difference in net disposable incomes.

	Loan repayment as % household income	Loan repayment as % net income	Loan Arears	Difficulty in making loan repayments	It is difficult to resolve debt problems with my lender	Food expenditure has been reduced to make loan repayments
MFI: Collateral	36%	62%	20%	56%	40%	48%
MFI: No Collateral	21%	40%	11%	46%	35%	37%
Bank: Collateral	37%	63%	21%	57%	42%	50%
Bank: No Collateral	28%	51%	13%	50%	43%	37%

- These tables show that the 'collateral' segment present a profile of higher vulnerability;
- The fundamental issue is whether the provision of the collateral enabled the higher loan leverage (essentially pawn-broking of the asset collateral), or if the collateral was taken to support a perceived credit vulnerability. The unchanged level of the incidence of collateral between 2014 and 2016 indicates that collateral was a 'lead' factor in the development of higher related loan balances;
- Although there appears to be a direct linkage between the availability of collateral and higher outstanding loans, the following table shows that the distribution and levels of household income are broadly similar for collateral and non-collateral borrowers – the availability of collateral thereby enabled higher lending.

Household Income TJS	< 1,200	1,201-1,800	1,801-2,600	2,601-3,400	>3,400	Average Income
MFI: Collateral	9%	15%	23%	20%	33%	3,338
MFI: No Collateral	16%	21%	26%	16%	21%	2,582
Bank: Collateral	9%	15%	24%	20%	31%	3,432
Bank: No Collateral	12%	20%	30%	15%	24%	2,833

- This distribution of incomes reflects the higher loan leverage against net disposable income shown in the earlier table;
- This suggests further that credit loan decisions may be influenced by the availability of collateral, rather than against the underlying cash flow / income of the client;
- If this suggestion is correct, and if the asset collateral does not have a readily marketable value, then this may increase significantly the risk profile of the portfolio and its sensitivity to external changes in the cost-of-living / net income.

- The higher levels of leverage amongst collateralised loans has direct implications for the potential growth / business development of this segment:

Total Expenditures as % Income: 2016	<25%	26-50%	51-75%	76-100 %	>100 %	Household expenditure as % of Income	Loan Repayment as % of Household Income
MFI: Collateral	2%	8%	27%	45%	18%	37%	36%
MFI: No Collateral	2%	15%	32%	40%	11%	42%	21%
Bank: Collateral	1%	10%	30%	41%	17%	35%	37%
Bank: No Collateral	2%	11%	36%	40%	11%	41%	28%
2014							
MFI: Collateral	2%	10%	28%	30%	29%	38%	38%
MFI: No Collateral	2%	12%	29%	35%	23%	44%	23%
Bank: Collateral	2%	12%	26%	36%	24%	35%	43%
Bank: No Collateral	1%	10%	32%	32%	25%	47%	26%

- This table shows that the more highly-leveraged 'collateralised' borrowers have lower expenditures on food and household essentials;
- The leverage of collateral loan repayments has improved since 2014; particularly in relation to bank borrowers.

- The incidence of collateral is widely spread across most borrower segments and may be evidenced below:
  - These tables show how the incidence of collateral has changed in the last 2 years;
  - The role of collateral with foreign currency lending is strongly shown;
  - There are clearly different regional policies.

% of clients in segment with collateral	Household Income		Location		
				2014	2016
	2014	2016	City - MFI	37%	29%
< 1,200	39%	25%	City - Bank	44%	39%
1,201-1,800	43%	27%	Urban - MFI	37%	31%
1,801-2,600	34%	31%	Urban - Bank	35%	42%
2,601-3,400	35%	40%	Rural - MFI	37%	30%
>3,400	43%	45%	Rural - Bank	47%	50%

	Region	
	2014	2016
Dushanbe	42%	36%
Khatlon	36%	37%
Sogd	29%	26%
RRP	11%	24%
GBAO	72%	51%

Currency of Loan		
	2014	2016
MFI - TJS	30%	28%
MFI - Fgn Ccy	58%	60%
Bank - TJS	39%	40%
Bank - Fgn Ccy	50%	66%

- The type of collateral asset is summarised in the following table, in relation to those borrowers who pledged collateral assets.

	Business Property	Residential Property	Business Equipment	Domestic Asset(s)	Vehicle	Guarantee	Gold / Jewellery
MFI	16%	27%	6%	18%	11%	8%	15%
Bank	15%	32%	6%	15%	14%	7%	12%

  - There is, again, a strong similarity across MFI and bank usage of collateral – and the types of collateral asset being taken;
  - Property is clearly the major asset being taken;
  - In relation to the other assets, it is uncertain how such assets are held and the effectiveness of the secondary markets in which the assets could be realised.

- The number of borrowers who provide guarantees for borrowings by other individuals has increased significantly since 2014.

Number of guarantees for outstanding debts	0	1	2	>2
MFI				
2016	12%	67%	19%	1%
2014	66%	23%	9%	1%
Bank				
2016	6%	66%	25%	3%
2014	63%	23%	12%	1%

  - This suggests a major change in the requirements of lending institutions – and again there is an extremely strong similarity of actions by MFIs and banks.
  - This may reflect a strategy for additional support for lending in the absence of available collateralised assets – or it may suggest that lending institutions are requesting multiple guarantees to support a loan.
  - The implications of such a substantial extension of guarantee support is to increase, still further, the levels of inter-personal commitment and dependency within a community. This is also reflected in the high levels of informal loans from friends and family.

- However, the underlying value of such guarantees does not appear to be strong.

Risk Dimensions	Number of guarantees for outstanding debts (2014 levels in parentheses)			
	0	1	2	>2
Arrears	5% .. (65%)	58% .. (18%)	32% .. (14%)	4% .. (3%)
Lender Refusal	19% .. (60%)	57% .. (28%	20% .. (12%)	4% .. (1%)
Repayment Difficulty	8% .. (66%)	72% .. (21%)	20% .. (12%)	1% .. (1%)
Expenditure > 75%	12% .. (64%)	66% .. (25%)	21% .. (9%)	1% .. (1%)
Remainder	9% .. (65%)	75% .. (23%)	15% .. (10%)	1% .. (1%)

  - Risk Dimensions[10] show the extent to which guarantees have been taken from borrowers who are, themselves, under significant financial pressures;
  - The 'Remainder' segment accounts for only 21% of borrowers (28% in 2014);
  - The underlying value of such guarantee obligations appears to be more nominal than real. The operational processes to implement and realise such guarantee commitments would be significant and the cost efficiency of the enforcement of the liability would probably be challenging;
  - The growth of guarantees appears to be 'motivational' – however, the risk of such an extensive use of guarantees (with minimal apparent likelihood of enforcement) could be to erode the reputation of the financial institutions, and to unite borrowers to resist such obligations.
- This diversity of factors suggests that the collateralisation of assets may be primarily a motivational factor to support loan repayment, rather than a source of potential realisable value for any shortfall in loan repayment:
  - The unchanged levels of collateral between 2014 and 2016 suggest that the lending institutions have been unable to obtain further levels of asset support for lending;
  - With the possible exception of property (and current market conditions may be difficult for even these assets), then the intrinsic realisable value of each item of collateral may be limited;
  - Conversely, the asset may have considerable 'lifestyle' importance to the lender, and any loss of this would represent a significant deprivation to the quality of life;
  - The existence, and occasional enforcement, of such collateral assets may also be perceived by lending institutions as a wider market motivation to maintain repayment – particularly against the financial profile of constrained net disposable income and the extensive usage of informal loan sources;

[10] Risk Dimensions are based upon: [1] Arrears: arrears with current loan; [2] Lender refusal: a lender has refused a loan application by the borrower in the last 12 months, although a loan was subsequently obtained from another lender; [3] Repayment difficulty: the borrower acknowledges to have difficulty in making the loan repayments; [4] Expenditure > 75% Income: the aggregate of essential household, utility and loan repayment expenditures exceed 75% of household income; [5] Remainder: all borrowers not included in segments 1 – 4. No borrower is included in more than one segment

- It may be noted that experience in other countries has shown the extreme difficulty of realising domestic assets held as security. It was found that people were reluctant to buy the collateralised assets of other community members / neighbours.

- The interaction of factors shown within this review suggests that the 'collateralised borrower' segment continues to present a relatively higher-risk profile within the lending portfolio.

3.6 What is the scope of lending in foreign currency?

Significant adverse impact of TJS Somoni devaluation against US$ - 42% of currency loans in arrears (similar for both MFIs and banks) – substantial reduction in the number of foreign currency loans since 2014 – remaining foreign currency loans have higher US$ outstanding balances than in 2014 (the lower-value US$ balances have been much reduced) – 55% of foreign currency borrowers were 'own business' clients – little indication of 'matched currency' incomes, and currency borrowers have experienced greater reduction / loss in remittance income

- Since the previous survey in 2014, the TJS Somoni has experienced a severe devaluation against the US$ (the dominant currency of foreign currency loans). The trends in the TJS exchange rate are reviewed in Attachment 4. These show that following a long period of stability, with the TJS Somoni on a 'peg' against the US Dollar, there have been two significant devaluations since end-2014.
This represented the crystallisation of a structural, or 'event', risk – rather than an operational credit risk.

- The extent of lending in foreign currency is shown in the following table:

	Distribution				Average Loan		Loan Arrears	
	Clients		Loan Value					
	2014	2016	2014	2016	2014	2016	2014	2016
MFI: TJS	75%	94%	56%	72%	5,144	5,536	2%	12%
MFI: Fgn Ccy	25%	6%	44%	28%	12,426	33,743	5%	42%
Bank: TJS	68%	91%	58%	74%	7,424	7,767	4%	14%
Bank: Fgn Ccy	32%	9%	42%	26%	11,364	27,934	5%	42%

  - The underlying balance in US Dollars of this currency lending is:
		2014	2016
MFI	US$ Balance	2,578	4,288
Bank	US$ Balance	2,358	3,549
    - This suggests that [i] lending in US$ continued to increase at higher loan amounts since 2014, and/or [ii] there has been an accumulation of unpaid interest / loan repayments which have been capitalised into higher loan balances, and/or [iii] the lower value loans have been repaid at a faster rate than the higher balances.
  - The distribution of outstanding foreign currency loan balances indicates that there has been a faster repayment of the higher volume of lower value loan balances.

- As the number of foreign currency loan clients is now relatively small, this review will not show a detailed sub-segment analysis of these clients (the data is separately available if required).

- The structural risk presented by foreign currency was described in the 2014 survey review. This external economic factor remains a strategic risk, but future repayment is also dependent upon other external factors, in addition to the continuing operational credit performance of individual borrowers.

2016	% Borrowers 'Own Business'	% Borrowers with lower / stopped remittances	Secondary Household Income		Trade Sector	
			Number of Income	% of secondary income in Public Sector	Retail	Service
MFI: TJS	39%	17%	2.22	33%	28%	22%
MFI: Fgn Ccy	53%	37%	2.31	22%	36%	28%
Bank: TJS	42%	17%	2.24	31%	29%	23%
Bank: Fgn Ccy	57%	25%	2.17	17%	42%	28%

- This table identifies that the operational credit quality of the 'foreign currency loan' segment is dependent upon a range of other external factors – which are outside the control of the borrower irrespective of how hard he/she works or commitment to loan obligations.
    - The higher level of 'own business' reflects the dependency upon the wider levels of national, and probably more particularly, local economic activity;
    - This trading dependency is emphasised by the concentration upon the retail and service sectors – which may be highly sensitive to local economic liquidity and also to variable levels of competitive market action (these are characteristically low-entry-barrier sectors);
    - 'Own Business' borrowers appear to have been particularly adversely affected by the lower levels of funds remittance from overseas. Any return to previous higher levels of payments is, of course, dependent upon a wider global upturn in economic activity – and any increased flow of such funds may be anticipated to 'lag' any up-turn;
    - 'Own Business' borrowers have other incomes into the household, and many of these are from employment in the public sector. Wages for such employees have been depressed in the last 2 years and are subject to greater political pressure / influence. A resurgence in such income levels may be as a 'follower' of national economic regeneration, rather than as a 'leader'.

- Nevertheless, the demands of operational credit management remain in the immediate future. The following table provides a summary of the comparative credit performance of TJS Somoni and foreign currency lending.

2016	Household Income	Loan repayment as % of net disposable income	Loan Arrears	Refinance / Reschedule in last 12 months	The institutions respond well to people with lending problems	I would like help to resolve debt problems with my lending institution
MFI: TJS	2,716	45%	12%	10%	88%	51%
MFI: Fgn Ccy	4,263	75%	42%	22%	80%	51%
Bank: TJS	2,893	52%	14%	13%	87%	55%
Bank: Fgn Ccy	5,224	79%	42%	16%	73%	55%

- This table highlights the immediate vulnerability of the credit quality of the ‘foreign currency’ segment – which is significant because it represents 25% of loan value (as identified by the 2016 survey);
- Such higher risk characteristics of the operational credit position must be considered also in conjunction with the structural risk exposures shown in the preceding paragraph.

- The ‘foreign currency’ borrower segment presents two strong observations:
  - The very substantial reduction of the risk exposure which was outstanding in 2014 – this appears to have been a major strategic achievement by the lending institutions and, of course, the borrowers;
  - The significant operational and strategic risks which apply to the remaining ‘foreign currency’ borrowers.

4. RISK PROFILE AND PERFORMANCE

4.1 What proportion of borrowers are over-indebted?

Significant deterioration in credit quality of loan portfolio – 15% of borrowers in arrears with loan payments – significant increase in the proportion of borrowers who recognise that they have financial problems – deterioration of financial position impacts across all income ranges – major pressures on domestic budgets arise from increasing price inflation of non-foodstuffs – continuing domestic budget economies by reduction of expenditures on food.

The definition of ‘over-indebted’ is widely interpreted. It may be appropriate, therefore, to describe the basis upon view the respondent borrowers are being reviewed.

> ”Over-indebtedness: “The extent to which a borrower is adversely affected by the interaction of the quantitative dimensions of loan repayment(s) upon his/her financial position and the qualitative dimensions of the impact of debt upon the financial confidence, risk vulnerability and the lifestyle of the borrower and dependents”.

- A range of factors demonstrate that the financial pressures upon borrowers have increased significantly between 2014 and 2016, despite a range of operational credit management initiatives which have been undertaken by lending institutions:
  - Loan arrears have increased from 3% to 15%;
  - Arrears with Utility payments have increased from 7% to 12%;
  - Recognition of difficulty to maintain loan repayments has increased from 29% to 50%.

- The following factors provide a quantitative assessment of trends in the financial budgets and behaviours of individuals between 2014 and 2016.

	Household Income TJS	Net Disposable Income (after loan) as % of Income	Average Loan TJS	Loan Repayment as % of Net Income (pre loan repayment)	Arrears: Loan	Arears: Utilities	Reduced food spending to make loan repayments
MFI							
2016	2,817	28%	7,460	49%	14%	11%	40%
2014	2,678	25%	6,936	54%	3%	8%	41%
Bank							
2016	3,168	24%	11,282	58%	17%	12%	43%
2014	2,892	21%	8,695	61%	4%	7%	40%

These dimensions are also shown in relation to the range of income segments.

	Household Income TJS	Net Disposable Income (after loan) as % of Income	Average Loan TJS	Loan Repayment as % of Net Income (pre loan repayment)	Arrears: Loan	Arears: Utilities	Reduced food spending to make loan repayments
2016							
< 1,200	975	10%	2,446	73%	9%	13%	51%
1,201-1,800	1,565	18%	3,076	58%	12%	15%	42%
1,801-2,600	2,175	23%	4,145	50%	17%	12%	39%
2,601-3,400	2,994	28%	7,016	45%	16%	11%	39%
>3,400	5,695	32%	19,270	50%	17%	9%	36%
2014							
< 1,200	959	-15%	4,234	143%	4%	7%	38%
1,201-1,800	1,570	5%	5,544	87%	3%	7%	48%
1,801-2,600	2,206	12%	6,225	72%	4%	6%	50%
2,601-3,400	2,981	25%	6,980	50%	4%	8%	39%
>3,400	5,526	37%	13,489	43%	3%	8%	28%

  - These quantitative responses indicate that there has been a structural improvement to the nominal basic budget of household. Particular attention should be noted for the lower income segments. The average loan and repayment leverage has been much reduced with an immediate and direct impact upon the net disposable income of these clients. If this results from the direct intervention and lending policy of the institutions, it should be regarded as a strong example of 'responsible lending';

- However, the high-level arrears measurements indicate that households have experienced additional financial pressures;
- The brief review of external economic influences (Attachment 4) highlights the impact of adverse exchange rate movements, the disproportionate inflationary impact upon non-foodstuff expenditures of households, the lower level of domestic economic activity (with particular impact upon the 'own business' sector, and the lower levels of employment.

- Despite the positive actions by both lending institutions and borrowers (as indicated above), the external factors have resulted in increased financial pressure upon borrowers. The qualitative attitudes of borrowers show the deterioration in their perception of the adequacy of their financial position. Such pressures, together with continuing outstanding loans, provide a demonstration of 'over-indebtedness' – in that the quality of lifestyle is being increasingly impaired.

	The quality of my life has improved in the last 12 months	My financial situation has improved in the last 6 months	I can afford to buy 'treats' for myself or my family	Most of my friends have difficulties meeting their domestic budget needs	Loans improve the quality of life	Debt repayments cause problems within my family	My loan repayments are more than I can afford
Total							
2016	65%	67%	69%	77%	67%	47%	50%
2014	85%	85%	86%	60%	93%	22%	29%
Adverse = Red	-20%	-18%	-17%	-17%	-26%	25%	21%
2016							
< 1,200	55%	61%	59%	85%	70%	51%	52%
1,201-1,800	60%	64%	62%	75%	65%	50%	50%
1,801-2,600	66%	68%	69%	79%	67%	45%	49%
2,601-3,400	71%	69%	73%	84%	69%	43%	51%
>3,400	68%	68%	76%	70%	65%	45%	48%
2014							
< 1,200	86%	87%	79%	73%	93%	26%	25%
1,201-1,800	86%	86%	82%	60%	96%	23%	30%
1,801-2,600	85%	85%	87%	50%	94%	21%	33%
2,601-3,400	83%	82%	87%	55%	91%	21%	32%
>3,400	84%	86%	90%	67%	92%	21%	25%

- Despite the improvement in 'net disposable income as a % of household income' for all borrowers (except the highest income segment), these responses show the significant social impact of the wider economic pressures;
- The earlier table shows that borrowers continue to undertake strong domestic budgetary reductions in order to maintain their loan repayments – but, nevertheless, other cost pressures are having a severe financial and social impact;
- These factors are widespread across the regions.

2016	The quality of my life has improved in the last 12 months	My financial situation has improved in the last 6 months	I can afford to buy 'treats' for myself or my family	Most of my friends have difficulties meeting their domestic budget needs	Loans improve the quality of life	Debt repayments cause problems within my family	My loan repayments are more than I can afford
Dushanbe	-2%	0%	-4%	-1%	-15%	27%	28%
Khatlon	-32%	-35%	-31%	7%	-33%	32%	49%
Sogd	-10%	-16%	-6%	4%	-19%	25%	14%
RRP	-28%	-30%	-16%	58%	-30%	26%	-3%
GBAO	-22%	-20%	-27%	8%	-35%	9%	13%

- The fundamental risk to the lending industry relates to the strategic exposure to the borrowers tolerance to any continuance / deterioration of such a situation.
  - The high cash-flow cost (together with the high interest component) of repayments may cause some borrowers not to renew their loans upon maturity;
  - The systemic risks of continuing cash-flow pressures on households, increasing recognition of financial pressures, reducing capacity of family / friends to provide informal cash support, and the wider economic pressures in the community should be considered in relation to the high level of borrowers (54% - 2014 59%) with essential expenditures greater than 75% of household income.
- ‘Acknowledgement / recognition by the borrower that debt repayment problems exist’.

- Borrowers show a high greater recognition of the financial pressures which they face, than was shown in 2014. This appears to demonstrate a significant social change in financial awareness and ‘facing up to the realities’ of their budgetary situation.

Household Income 2016 Adverse trends shown in red	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
< 1,200	35%	52%	51%	41%	58%
1,201-1,800	32%	50%	50%	36%	53%
1,801-2,600	33%	49%	45%	38%	53%
2,601-3,400	36%	51%	43%	40%	52%
>3,400	37%	48%	45%	39%	47%
2014					
< 1,200	22%	25%	26%	34%	26%
1,201-1,800	21%	30%	23%	29%	29%
1,801-2,600	25%	33%	21%	21%	30%
2,601-3,400	24%	32%	21%	17%	31%
>3,400	32%	25%	21%	21%	28%

- These responses show a substantial and adverse change in the attitudes of borrowers;
- The positive dimension to such a situation is that they are facing, and recognising, the reality of the financial constraints – which were apparent in the 2014 survey, but not being acknowledged to the same level;
- 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.

- **The financial capacity of borrowers to meet essential payments has improved, but wider economic and cost pressures are now the systemic 'drivers' of financial performance. Without structural improvements to the net disposable income of the domestic budget, the lending portfolios would have been more adversely pressured.**
- Actions by the lending institutions and borrowers have combined to improve the net disposable incomes of lower income borrowers (57% of clients with incomes up to TJS 2,600).

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
< 1,200	600	350	250	100	20
1,201-1,800	900	650	400	250	55
1,801-2,600	1,200	1,000	500	500	90
2,601-3,400	1,500	1,500	700	800	130
>3,400	2,000	3,650	1,800	1,850	280
2014					
< 1,200	600	350	500	(150)	(30)
1,201-1,800	900	700	600	100	15
1,801-2,600	1,250	950	690	260	50
2,601-3,400	1,500	1,500	750	750	130
>3,400	2,000	3,550	1,500	2,050	325

- The basic financial position of lower income borrowers has improved;
- If the financial profile of such borrowers had been unchanged from 2014, the level of loan arrears / losses and problem lending would have been much higher – and the adverse social implications would have been much deeper;
- The challenge to the lending industry is now reflecting the much wider economic and social pressures – and thereby the strategic implications of potential systemic risk.

- 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 7% of all borrowers (accounting for 3% of outstanding loan value) demonstrate a basis for confidence of their financial situation.

2016	Distribution		Household Income	Net Disposable Income (after loan)	Outstanding Loan
	Clients	Value			
Affordable	7%	3%	4,452	2,731	3,324
Concerned	7%	9%	4,230	2,085	11,341
Vulnerable	28%	16%	2,894	1,049	4,851
Exposed	58%	72%	2,667	267	10,629

2014	Distribution		Household Income	Net Disposable Income (after loan)	Outstanding Loan
	Clients	Value			
Affordable	9%	7%	4,777	3,065	5,621
Concerned	4%	3%	4,344	2,682	5,498
Vulnerable	28%	21%	3,142	1,154	5,738
Exposed	60%	69%	2,168	-76	8,745

  - The distribution of the risk categories is broadly unchanged between 2014 and 2016 – such categorisation is based largely upon quantitative (rather than attitudinal) responses which re-confirms that the overall portfolio vulnerability was apparent in 2014 – however, the significant change in 2016, as shown by the earlier comments, is that many more borrowers are now recognising the delicate financial situation which they face;
  - The financial resilience of the 'Concerned' risk category shows colliding impacts of lower disposable incomes and higher debts;
  - However, the greater financial improvement has occurred with the highest risk segments;
  - The overall concern with this trend is that [i] the high risk segments remain highly vulnerable, and [ii] the higher income segments (particularly the 'Concerned' segment) show a deterioration in their financial position.

- Such distribution of the risk profile of the loan portfolio, and the underlying trends, suggest that the particular concern relates to the systemic risk exposure of borrowers to external events which have wide-ranging impacts – and thereby affect the performance of the lending industry.

4.2 What are the trends in arrears?

Severe deterioration in arrears from 3% in 2014 to 15% in 2016 –increases also in utility arrears, loan refinance and recognition of difficulty to make loan repayments – 'own business' segment shows highest increase in arrears – certain individual lending institutions indicate higher arrears levels.

The levels of arrears have risen substantially since 2014 (3%) to 15% in 2016.

The earlier sections of this review have identified the structural improvements which have been achieved to the loan portfolios in relation to net disposable incomes, after household essentials and loan repayments. Despite these changes, the adverse impact of global economic trends, adverse exchange rate movements, a significant reduction of inward remittances, and strong inflation of non-food expenditures have contributed towards a

significant deterioration in the performance of loan repayments and the attitude of borrowers towards their financial position.
The impact of adverse changes to loan arrears is widespread across the loan portfolios.
The following tables demonstrate the impact of arrears across different borrower segments.

Arrears: 2016	% of Borrowers with loan arrears	Outstanding loan balances of ‘arrears’ borrowers as % of total balances	Utility Arrears	Refinance / Reschedule in last 12 months	Difficulty to make loan repayments
MFI	14%	26%	11%	11%	49%
Bank	17%	26%	12%	13%	53%

- The performance of the two types of lending institution is highly similar

;Region	% of Borrowers with loan arrears	Refinance / Reschedule in last 12 months	Household Income	% of Borrowers with loan arrears	Refinance / Reschedule in last 12 months
Dushanbe	21%	15%	< 1,200	9%	12%
Khatlon	18%	6%	1,201-1,800	12%	10%
Sogd	13%	9%	1,801-2,600	17%	8%
RRP	13%	6%	2,601-3,400	16%	11%
GBAO	8%	22%	>3,400	17%	16%

- Dushanbe shows much higher levels of arrears and loan refinance/reschedule;
- GBAO appears to have used refinance / reschedule to mitigate the level of loan arrears. Whilst it is hoped that this may be a successful action, GBAO shows extremely high levels of utility arrears (30%), informal credit from retailers (46%), and reductions in food expenditures to make loan repayments (54%) – such factors suggest that future arrears may be anticipated to increase significantly (unless there are immediate and substantial improvements to the local economic environment).

Income Sources	% of Borrowers with loan arrears	Refinance / Reschedule in last 12 months	Major Trade Sectors for Source of Income	% of Borrowers with loan arrears	Refinance / Reschedule in last 12 months
MFI: Regular Work	10%	11%	Retail	21%	14%
MFI: Irregular Work	15%	13%	Engineering	9%	7%
MFI: Own Business	20%	14%	Building - Property	12%	12%
Bank: Regular Work	12%	11%	Service	17%	13%
Bank: Irregular Work	17%	19%	Agriculture	16%	8%
Bank: Own Business	23%	16%	Public Sector	11%	12%

- The ‘own business’ segment show a higher incidence of arrears;
- Public Sector employees represent a relative high share of individual borrowers; Wage levels in this sector have been constrained more than in other sectors. Such clients present, therefore, a particular portfolio risk to lending institutions.

The following table indicates that such pressures are reflected across the major individual lending institutions – however, it must be recognised that the following statistics are merely indicators, based on limited samples – each institution would need to assess its own loan portfolios independently from their client data-bases.

Arrears: 2016	% of Borrowers with loan arrears	Refinance / Reschedule in last 12 months	Utility Arrears	Difficulty to make loan repayments	Food expenditure has been reduced to make loan repayments
MFI: A	14%	11%	6%	44%	36%
MFI: B	18%	9%	8%	48%	38%
MFI: C	20%	11%	8%	55%	40%
MFI: D	15%	7%	6%	43%	33%
Bank: A	17%	8%	8%	47%	36%
Bank: B	17%	17%	17%	54%	45%
Bank: C	15%	15%	16%	54%	44%
Bank: D	23%	20%	15%	60%	51%
Bank: E	28%	19%	7%	51%	44%

- This table is based solely upon those respondents who identified their lending institution. This data does **not** represent a detailed (or statistically robust) assessment of an institution. This should be provided by the respective lending institution. It does, however, indicate that the management and governance of those institutions need to understand the institutional performance in relation to its competitors and the market and identify the need for a close understanding of the profile, characteristics and attitudes of the respective client bases;
- Certain institutions appear to demonstrate higher risk characteristics (particularly certain of the banks);
- Lending institutions should consider the further indicators of risk exposure in relation to not only to client credit management, but also for structural risk concentrations and appropriate levels of loan loss reserve.

4.3 Where do loan arrears principally occur?

Highest arrears 40+% in foreign currency lending – arrears borrowers also show higher levels of additional informal debt – arrears concentrations in certain segments, principally amongst 'own business' clients.

- Arrears are particularly high in relation to foreign currency lending:

	Proportion of Arrears as % of Total Segment: Clients	Segment Arrears as % of Total Arrears	Refinance / Reschedule as % of Segment	Borrowers applying for loan in last 12 months as % of segment total	Lender Refusal: % of Borrowers applying for loan in last 12 months
'Own Business': Fgn Ccy	44%	12%	23%	61%	30%
MFI: Fgn Ccy	42%	10%	22%	57%	30%
Bank: Fgn Ccy	42%	10%	16%	52%	43%

- The other loan segments which have the highest levels of arrears (as a proportion of the respective segment) are shown below and provide an indication of the concentrations of highest arrears.

Loan Segment	Sub-Segment	Proportion of Arrears as % of Total Segment: Clients	Sub-Segment Arrears as % of Total Arrears	Refinance / Reschedule as % of Segment	Borrowers applying for loan in last 12 months as % of segment total	Lender Refusal: % of Borrowers applying for loan in last 12 months
A	B	C	D	E	F	G
Loan: Informal Type	Friends	30%	27%	27%	61%	39%
Loan: Bank	> 10,000	29%	18%	26%	67%	29%
Loan: MFI	> 10,000	28%	15%	27%	72%	28%
Institution: Named	Bank: E	28%	10%	19%	75%	23%
Collateral: Type	Property: Residenti al	25%	19%	16%	48%	25%
Collateral: Type	Property: Business	25%	9%	16%	63%	19%
Loan: Informal Type	Family	24%	12%	33%	60%	41%
Loan: MFI	5,001-10,000	24%	14%	12%	67%	27%
Income: Source	Bank: Own Business	23%	26%	16%	62%	21%
Institution: Named	Bank: Bank D	23%	11%	20%	65%	27%
Loan: Informal	With Informal: Total	23%	46%	19%	65%	31%
Loan: Product	Business: TJS	23%	29%	17%	72%	20%
Institution	Former Borrower s MFI	23%	7%	18%	80%	17%
Loan: Purpose Last	Business: Trading	22%	48%	16%	67%	19%
Institution	Former Borrower s Bank	22%	7%	11%	74%	21%

- The columns in the above table show:
    - A: Loan Segment: the major loan segments within the portfolio. These relate to both MFI and bank borrowers, unless shown differently;
    - B: Sub-Segment: relates to the sub-dimension with the respective loan segment;

- C: Proportion of arrears as % of total segment: relates to the number of arrears clients in the sub-segment (B) as a % of the total segment (A);
- D: Sub-segment arrears as % of total arrears: relates to sub-segment arrears (B) as % of all arrears in the total (MFI and bank) portfolio (based on the survey sample);
- E: Refinance: the proportion of the clients in the sub-segment who have refinanced / rescheduled their loan within the last 12 months
- F: Loan application in last 12 months: the proportion of the clients in the sub-segment who have applied for a loan within the last 12 months;
- G: Lender refusal: the proportion of those clients (F) who had a loan application refused, but have obtained a loan from another lender.

- This table is based upon:
  - The borrower segments which show the highest levels of arrears;
  - Some borrowers may be included in more than one segment (for example, a Loan: Bank > 10,000 may have provided 'Collateral: Residential'.
- This table identifies some segments with strong concentrations of established high risk exposures. The inclusion of two lending institutions may be particularly noted. This demonstrates the need for individual lending institutions to be keenly aware of the profiles and dynamics of their borrower client portfolios.
  - The widespread impact of informal borrowings is also shown to be aligned with high arrears segments. This is an important dimension for consideration by the lending institutions in the evaluation of problem lending situations.

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

Borrowers who move between lending institutions demonstrate much higher credit risk characteristics.

- The financial profile and risk characteristics change significantly in relation to the mobility of borrowers:

Number of Lending Institutions in last 2 years	Household Income	Average Loan Balance	Arrears: Loan	Arrear: Utilities	Informal loan: Family	Informal loan: Friends	Difficulty to make loan payments	Food expend reduced to make loan payment
One	2,894	7,021	13%	11%	6%	12%	38%	40%
Two	3,123	14,944	24%	13%	13%	18%	43%	45%
3 or more	4,299	30,519	40%	14%	18%	33%	49%	56%

  - Additionally, the following characteristics may be noted:
    - The level of collateralised assets increased:
      - 1 lender = 33%, 2 lenders = 40%, and 3 lenders = 61%
    - The incidence of foreign currency loans increased
      - 1 lender = 6%, 2 lenders = 12%, and 3 lenders = 19%

- The level of refinance / reschedule also increased
  - 1 lender = 10%, 2 lenders = 17%, and 3 lenders = 33%
- These characteristics highlight the particular challenges in the credit assessment and management of borrowers who move between lending institutions.

- During the last two years, the number of lenders used by current borrowers has increased:

Distribution of Borrowers	MFI Borrowers			Bank Borrowers		
	1 lender	2 lenders	3+ lenders	1 lender	2 lenders	3+ lenders
Current Borrowers						
2016	84%	15%	2%	81%	16%	3%
2014	90%	9%	1%	90%	9%	1%
Former Borrowers						
2016	50%	44%	6%	51%	44%	5%
2014	72%	26%	2%	63%	34%	3%
Arrears						
2016	73%	23%	4%	70%	24%	6%
2014	70%	24%	6%	79%	19%	2%

- This shows the increased level of client mobility during the last 2 years. This may reflect a greater caution by lending institutions – but, whatever the reason; borrowers have shown a stronger willingness, or necessity, to move lenders;
- The level of mobility between lenders is, not surprisingly, higher amongst those clients with arrears or repayment difficulties than with other borrowers.

Distribution of Borrowers within each segment: 2016	MFI Borrowers			Bank Borrowers		
	1 lender	2 lenders	3+ lenders	1 lender	2 lenders	3+ lenders
Arrears	73%	23%	4%	70%	24%	6%
Lender Refusal[11]	81%	17%	1%	78%	19%	3%
Loan repayment difficulty	89%	10%	1%	85%	14%	2%

4.5 Do borrowers with problem lending show different characteristics?

Significant increase in the level of borrowers who acknowledge their difficulties with debt – only 21% of clients / 9% of outstanding loan show a reasonable level of credit strength – major deterioration in the attitude of borrowers towards debt.

The above sections of this review have identified the level of loan arrears within a range of different loan segments and portfolios. The following comments segment the loan portfolios in relation to different dimensions of recognition of problem debt by the borrower. These segments involve:

i. Arrears;
ii. Lender Refusal;
iii. Repayment Difficulty;

[11] Lender Refusal: Borrower has applied for a loan in the last 12 months and has had a loan application refused, before being accepted by the current lender

iv. Total Expenditures greater than 75% of Income;

v. Remainder.

A description of this segmentation is shown below. The characteristics are hierarchical – no borrower is included in more than one segments, starting with [i] Arrears.:

- *'Arrears'* this segment clearly has severe repayment problems, together with relatively high levels of informal debt;
- *'Lender Refusal'* the incidence of 'lender refusal' suggests that this segment is likely to be of marginal credit quality. The borrower will have realised the problem lending situation;
- *'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;
- *'Total expenditures greater than 75% of income'* this segment has a high commitment of current income to basic expenditures. This segment may have a more 'laissez-faire' approach towards their financial position;
- *'Remainder'* this segment does not demonstrate any of the financial pressure characteristics in the preceding segments.

The distribution of the loan portfolios into these characteristics is shown below:

2016	MFI				Bank			
	Distribution		Net Disposable Income (post loan)	Loan Balance	Distribution		Net Disposable Income (post loan)	Loan Balance
	Clients	Loan Value			Clients	Loan Value		
Arrears	14%	26%	589	13,512	17%	26%	530	14,786
Lender Refusal	12%	14%	824	8,831	9%	16%	846	16,830
Repayment Difficulty	32%	26%	691	5,903	35%	32%	680	8,687
Expenditure > 75%	22%	25%	258	8,222	19%	18%	259	8,659
Remainder	21%	9%	1,558	3,187	20%	9%	1,501	4,126

  - o This table identifies the contrasting levels of disposable income and outstanding indebtedness across these borrower segments.

- The change in the distribution of these segments between 2014 and 2016 is substantial.

Adverse trends shown in red	MFI				Bank			
	Distribution: Clients		Distribution: Loan Value		Distribution: Clients		Distribution: Loan Value	
	2014	2016	2014	2016	2014	2016	2014	2016
Arrears	3%	14%	4%	26%	4%	17%	4%	26%
Lender Refusal	4%	12%	3%	14%	5%	9%	5%	16%
Repayment Difficulty	26%	32%	27%	26%	23%	35%	22%	32%
Expenditure > 75%	40%	22%	44%	25%	40%	19%	49%	18%
Remainder	28%	21%	22%	9%	28%	20%	20%	9%

- The scale of such changes within the loan portfolios has significant implications for both the lending institutions and the borrowers.
    - Lending institutions: the organisation and governance structures of such changed emphases of business and client are substantial at both board and management levels;
    - Borrowers: the response to such substantial changes will impact directly upon their lifestyle and actions;
    - There are, of course, significant implications for the Regulatory Authorities and investment funding institutions.

- The scale of additional financial commitments and pressures are reflected in the following tables (which includes both MFI and bank borrowers).

Adverse trends shown in red	Arrears with Utility Providers		Have you refinanced, or consolidated your debts during the last 12 months		Informal Loans with Retailers		Food expenditure has been reduced to make loan repayments	
	2014	2016	2014	2016	2014	2016	2014	2016
Arrears	19%	16%	25%	27%	19%	26%	39%	62%
Lender Refusal	18%	18%	4%	10%	28%	34%	54%	48%
Repayment Difficulty	9%	13%	6%	10%	19%	26%	46%	52%
Expenditure > 75%	5%	9%	6%	8%	26%	14%	45%	24%
Remainder	7%	6%	5%	6%	20%	14%	28%	19%

  - There are different responses from the different segments of risk recognition;
  - Those borrowers who have recognised their financial situation have largely undertaken financial actions to respond to their situation. There does not appear to be much capacity to enable further reductions to be undertaken without severe detriment to their personal and family positions;
  - Those remaining with high levels of committed expenditure have minimal net disposable income with which to meet on-going living costs (beyond food and essential household needs).

Adverse trends shown in red	The quality of my life has improved in the last 12 months		Debt repayments cause problems within my family		I need / needed to continue to borrow to maintain how my family and I live		I would like help to resolve debt problems with my lending institution	
	2014	2016	2014	2016	2014	2016	2014	2016
Arrears	67%	42%	53%	67%	71%	86%	44%	61%
Lender Refusal	82%	64%	40%	49%	34%	82%	37%	63%
Repayment Difficulty	82%	64%	51%	76%	75%	92%	59%	72%
Expenditure > 75%	90%	70%	9%	16%	45%	71%	15%	34%
Remainder	83%	78%	9%	13%	27%	64%	18%	26%

- This chart starkly demonstrates the widespread deterioration in attitudes towards the domestic financial situation;
- A fundamental strategic issue / challenge from these trends is the period of time which can be endured by borrowers in such (or further deteriorating) financial and economic situation.

4.6 Do borrowers who undertake loan refinance have particular characteristics?

Refinance increased to 11% compared with 6% in 2014 –significant regional differences, highest incidence being in GBAO – further refinance situations may be anticipated

- The average level of refinance / reschedule of loans in 2016 was 11%, compared with 6% in 2014. This level appears to be somewhat low in relation to the increased pressures which have demonstrated. There may be some definitional issues in relation to refinance / reschedule which affect a recognition of such a restructure by the borrower.
- The preceding sections have demonstrated a higher incidence of loan refinance / reschedule in various loan segments, compared with an overall average of 11%. These have include:
    - Regional: GBAO 22%
    - Former MFI: with bank loans 18%
    - Location: Urban and Rural bank clients 17%
    - Trade Sector: Retail 14%
    - Income: Over TJS 1,800 17%
    - Income Source: Own Business 22%
    - Loan Currency: Foreign Currency 16%
    - Loan Purpose: Trading 16%
    - Loan Collateral: With collateral 18%
- Despite the increase in the incidence of refinance / reschedule in 2016, it may be anticipated (in the absence of any significant upturn) that further and more extensive loan restructures will continue for the short and medium term futures. In this regard, the following comments may be noted:
    - Many of the existing refinance situations may be anticipated to require future restructure as borrowers continue to face the financial challenges;
    - The process of refinance / rescheduling will need to be increasingly ‘productised’ to reflect the on-going use of funds and the related underlying cash-flow.

4.7 What is the extent of informal lending?

Informal loans from friends and family are higher in 2016 than in 2014 – informal loans are higher amongst those borrowers who recognise debt repayment difficulties – the level of informal retail credit to support domestic consumption remains high.

- Informal lending is based upon the use of non-financial institution sources for funding. These are primarily from family, friends, retailers, employers, money-lenders;

- The incidence of such informal loan sources amongst borrowers is shown in the following table.

Number of Informal Loan Sources	Distribution: Clients	Distribution: Loan Value	Household Income	Net Disposable Income (after loan payments)	Outstanding Loan
None	70%	67%	3,074	838	8,119
One	19%	14%	2,702	706	6,471
Two	7%	10%	2,630	518	13,035
Three or more	4%	9%	2,482	296	17,898

  - The incidence of informal borrowings is shown to be extended, involving about 30% of borrowers;
  - At this scale, it is a significant component of the credit assessment process and over-indebtedness.
- The financial performance of these ‘informal loan’ client segments may be summarised in the following table:

Number of Informal Loan Sources	Characteristic of Borrower				
	Arrears: Loan	Arrears: Utilities	Have you refinanced, or consolidated your debts during the last 12 months	If loan application in last 12 months, has any lender refused to lend to you	Food expenditure has been reduced to make loan repayments
None	11%	5%	8%	16%	31%
One	20%	23%	11%	24%	56%
Two	30%	30%	24%	39%	70%
Three or more	23%	36%	43%	54%	82%

  - *This table shows the characteristics in relation to the number of informal loans – for example, 23% of those borrowers with 3 or more informal loans have loan arrears.*
  - There is a clear relationship between (increasing) usage of informal loan sources and adverse credit performance.
- The sources of informal credit are shown below:

	Family	Friends	Retail: Assets	Retail: Domestic	Moneylender / Pawnbroker	Employer	Other
One	9%	26%	8%	47%	1%	3%	6%
Two	32%	64%	23%	68%	3%	4%	5%
Three or more	79%	96%	39%	91%	7%	23%	4%

  - These usage levels relate to the proportion of borrowers within each segment which use the respective sources;
- The strong dependencies upon family, friends and retail dominate these sources. This is in addition to the increased level of guarantee commitments being provided between borrowers;

- Compared to 2014, the incidence of informal loans from family and friends is higher; whilst the level of retailer credit has remained broadly unchanged (which may reflect the greater trading and financial pressures experienced by the retail 'own business' segment);
- The preceding table showed the higher levels of financial pressure being reflected amongst borrowers with informal loan sources. This has significant implications in relation to:
    - Capacity for repayment and the extent to which informal sources are 'preferred' in the hierarchy of cash payments;
    - The high 'visibility' of the financial pressures of the borrower. The communities are highly stable and, therefore, the financial situation of the borrower will be well-known. However, other responses indicate that such financial pressures are widespread and there may not be a social stigma to the situation of extreme financial pressure;
    - However, non-repayment of such indebtedness may be a cause of social pressure – money is often the cause of much social 'ill-ease' – this may suggest that the lending institution will be repaid after funds are disbursed informally;
    - The high level of retailer credit is a significant dimension of the assessment of the credit quality of an 'own business' borrower. The business turnover and cash-flow depends, at some level, on the liquidity of the customers of the 'own business' borrower;
    - The 'own business' trader (most of the 'own business' borrowers are in retail or service) is dependent upon the level of local demand. If loan funds decline, and/or the savings of family/ friends become used, and/or market conditions continue to be constrained by the impact of rising inflation – then the 'own business' sector will experience lower demand and lower liquidity within the community. This will, of course, vary in different locations – but if current trends continue, or are even held level, then the 'own business' borrowers will come under increasing pressure – and this is already one of the most vulnerable segments.
- The incidence of 'informal lending' varies in different segments and are exampled below.

	Family	Friends	Retail: Assets	Retail: Domestic	Moneylender / Pawnbroker	Employer	Other
Dushanbe	9%	15%	6%	11%	2%	5%	0%
Khatlon	3%	13%	1%	19%	0%	0%	7%
Sogd	4%	4%	3%	7%	1%	1%	0%
RRP	3%	10%	5%	6%	1%	0%	0%
GBAO	17%	26%	9%	46%	0%	3%	0%
Arrears	12%	27%	5%	21%	2%	3%	5%
Lender Refusal	9%	16%	9%	25%	2%	2%	0%
Repayment Difficulty	8%	14%	6%	20%	1%	2%	1%
Expenditure> 75%	5%	10%	3%	11%	1%	2%	1%
Remainder	3%	5%	2%	12%	0%	1%	1%

- o The lending institutions should incorporate informal lending as a possible strong indicator of financial pressure;
- o Financial education must reflect such lending into its programmes of communication;
- o GBAO shows again higher risk characteristics than the other regions. These factors may have contributed to the lower level of loan arrears which was reported in that region.

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

'Non-savers' have higher loan arrears than 'savers' – 'non-savers' demonstrate higher general levels of financial pressure

- The levels of 'savers' amongst borrowers was almost unchanged from 2014:

	Savings with a Financial Institution	Other savings	Non-Savers
MFI	10 %	26 %	70 %
Bank	10 %	26 %	70 %

- o The use of savings mechanisms other than with financial institutions remains strong.

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

	Income	Household and Utility Costs	Loan Repayment	Net Disposable Income	Outstanding Loan
Savings: FI: Borrowers	3,306	1,501	675	1,131	9,672
Other Savings: MFI	3,120	1,368	700	1,052	7,763
No Savings: MFI	2,706	1,275	759	673	7,500
Other Savings: Bank	3,802	1,457	1,096	1,249	12,370
No Savings: Bank	2,945	1,320	1,058	567	11,082

- The credit performance of these segments is summarised in the table below:

	Loan: Arrears	Utility: Arrears	Have you refinanced, or consolidated your debts during the last 12 months	If loan application in last 12 months, has any lender refused to lend to you	% of borrowers with essential expenditures (inc loan repayments) greater than 75% of income
Savings: FI: Borrowers	8%	8%	11%	10%	47%
Other Savings: MFI	11%	4%	8%	12%	45%
No Savings: MFI	15%	14%	12%	25%	58%
Other Savings: Bank	10%	4%	8%	11%	46%
No Savings: Bank	20%	15%	15%	25%	59%

- The greater vulnerability of those borrowers with no savings is clearly shown for both MFI and bank borrowers;
- The credit performance of these segments is almost identical for MFIs and banks;
- Those borrowers with 'no savings' also have higher levels of informal loans from friends and retails (to fund domestic consumption).

- The budgetary vulnerability indicated in the above table is reflected in the differential responses of savers and non-savers, which again highlight the pressures of those (majority) borrowers who have no savings.

	I borrowed too much	My loan repayments are more than I can afford	Debt repayments cause problems within my family	I would like help to resolve debt problems with my lending institution	Food expenditure has been reduced to make loan repayments
Savings: FI: Borrowers	45%	48%	46%	51%	41%
Other Savings: MFI	27%	30%	32%	38%	29%
No Savings: MFI	35%	56%	50%	56%	44%
Other Savings: Bank	32%	31%	35%	31%	26%
No Savings: Bank	43%	62%	57%	62%	49%

- This highlights further the greater vulnerability of the financial budgets of those borrowers with no savings;
- The similarity of responses by both MFI and bank borrowers is again strong;
- Paradoxically, the responses of those savers with financial institutions shows similar characteristics to those of the 'non-savers'. It may suggest that the banks may use such funds as hypothecated balances as part of a collateral structure for the loan.

5 OUTLOOK FOR BORROWING

5.1 What is the outlook for borrowing demand?

Based upon current borrowers and without a significant upturn in the economy, outlook for lending appears sombre with increasing pressure on repayment capacity and reduction in outstanding loan value – only 21% of clients / 9% of outstanding loan show a reasonable level of credit strength – demand appears to be driven, to a large extent, by necessity – in addition to continuing operational credit management, particular strategic consideration needs to be given to portfolio and systemic risk pressures – 'own business' segment presents significant structural portfolio risks – such generic pressures require effective industry coordination to maintain market stability.

- The short-term and strategic outlooks for lending in Tajikistan is a complex interaction of a range of factors. The individual lending institutions will have a keen understanding of the strength and sensitivity of the range of dynamics. The following comments on the outlook for lending are based, however, solely upon the interpretation (by the writer) of the responses to the 2014 and 2016 surveys, together with the public domain data of recent economic trends.

- The outlook for lending reflects the inter-action of four principal dimensions:
    - Current loan portfolio structure and actions taken in the last 2 years
    - External economic, financial and social factors which impact the market
    - Borrower demand and requirements
    - Risk framework (operational, portfolio, and structural) to be addressed by lending institutions

- The following comments briefly summarise issues which have been raised in the earlier review of the findings of the 2014 and 2016 surveys.

- Current loan portfolio structure and actions taken in the last 2 years:
    - Significant improvement in the operational credit profile of the lowest income borrowers;
    - Substantial reduction in the scale of exposure to foreign currency loans;
    - Despite such structural changes to operational credit, pressure has increased upon most borrowers resulting from a deterioration of wider economic and market conditions;
    - Apparent saturation in the availability of collateralised assets, although the implications of asset repossession and realisation are likely to present operational and strategic challenges;
    - Significant expansion in the use of guarantees to support lending, although the underlying 'value' of guarantor appears, for many, to be highly uncertain;
    - Significant deterioration in the vulnerability and sensitivity of the credit quality of the overall loan portfolios.
- External economic, financial and social factors which impact market conditions. (These factors are reviewed in Attachment 4, based upon public domain data)
    - Significant devaluation of the national currency against the US dollar;
    - Strong inflationary pressures upon imported goods, which impact most domestic requirements (other than basic foodstuffs);
    - Reduced levels of inward remittance of funds from overseas workers;
    - Constrained levels of employment and remuneration;
    - Constrained levels of domestic economic activity.
- Borrower demand and requirements:
    - Existing borrowers continue to express a strong demand for future borrowings, despite an increased recognition of the difficulty to make existing loan repayments;
    - Significant usage of loan funds for purposes which reflect consumption, rather than generation of economic value;
    - Continuing high interest rate levels on borrowings which impact directly upon the 'real' cost of the items being purchased;
    - Continuing constraints on domestic budgets, despite the structural improvements which have been achieved;

- Appropriateness of loan products to address the related usage of funds.

- Risk framework to be addressed by the lending institutions:
    - Operational credit risk – the capacity of existing (or potential) borrowers to maintain current, or increased, borrowings;
    - Portfolio credit risk – the structural risks which apply particularly to certain substantial segments of the loan portfolio and the performance of which has a significant impact on the total lending portfolio. (The 'own business' segment is such a major segment);
    - Systemic risk – the vulnerability and sensitivity of the total lending to external trends and pressures.

- The outlook and strategy for the management of current loan exposures and development of future lending needs to reflect the inter-action of these various issues. The following comments do not seek to undertake a detailed review against each of the above issues – but rather to highlight the findings of the 2014 and 2016 surveys within the context of such strategic dynamics.

  The following comments seek to provide some examples of these inter-related factors which are likely to impact on future borrowing levels and credit performance.

- The profile of the usage of loan funds by individuals shows a strong focus for domestic needs.

2016	Business	Domestic			Property	
		Assets	Expenses	Health, Education, and Family Events	Acquisition	Improvement
MFI	30%	7%	27%	17%	9%	9%
Bank	35%	6%	25%	14%	9%	9%

- This summary table highlights the different purposes of loan usage and thereby the different timescales which are involved. For example,
    - the timescale of property expenditures is far longer than that on expenditures for domestic consumables;
    - the trading needs of a business may reflect seasonal fluctuations.
- However, the over-whelming majority (85%) of loans were undertaken on a fixed-term, fixed-repayment basis with an implied overall loan period of about 18-24 months.
- The nominal interest rate on Individual loans is about 35%, which implies an APR of about 75%. This is a high cost by which to fund expenditures on short-term domestic consumption.

- The dependency of lower income segments to fund short-term domestic consumption is highlighted in the following table:

2016	Business	Domestic			Property	
		Assets	Expenses	Health, Education, and Family Events	Acquisition	Improvement
< 1,200	11%	7%	46%	18%	9%	8%
1,201-1,800	11%	9%	32%	18%	10%	11%
1,801-2,600	17%	7%	27%	18%	11%	9%
2,601-3,400	16%	6%	23%	16%	10%	9%
>3,400	38%	5%	15%	11%	6%	8%

- This table shows starkly the different roles of loan finance.
- The implications for the lower income segments are substantial.
- With interest rates at about 35% (APR equiv. 75%) and an implied initial loan of about TJS 4,000, the monthly interest cost on an 18 month loan would be about TJS 115. This monthly interest cost is, in itself, equivalent to the average monthly expenditure on food and household essentials for one person.
- In the vulnerable financial positions of a large majority of borrowers, the interest component of the on-going loan repayments represents a significant additional cost to the underlying usage. If such loan monies are used for domestic consumption of foodstuffs (on which there has been minimal inflation), then the real cost of such items is being significantly understated.

• The following table shows the perception of dependency upon continuing access to debt to support the lifestyle of the borrower.

	Loan Repayments TJS	Average monthly expenditure per person on food and domestic essentials	Net Disposable Income (after Loan) TJS	I need to continue to borrow to maintain how my family and I live	My loan repayments are / were more than I can afford	Food expenditure has been reduced to make loan repayments
< 1,200	261	116	98	81%	52%	51%
1,201-1,800	384	148	282	85%	50%	42%
1,801-2,600	511	177	507	79%	49%	39%
2,601-3,400	691	205	835	78%	51%	39%
>3,400	1,816	282	1,835	79%	48%	36%

- The interest component of loan repayments is likely to be about 40% of the total monthly payment. On this basis, the above table shows how the interest being paid by the lowest income segment is almost as much as being spent on food and essentials for one person in a month. This is a significant challenge for ‘responsible finance’ and with whom responsibility lies: the lender, or the borrower, or who else?;
- Despite the delicate financial position of the lower income segments (the NDI figure is based only on expenditures for food, household essentials, utilities and loan payments), the perceived solution by such clients is for continued borrowing;

    - Domestic consumption levels (and thereby lifestyle) could be improved if loans were not taken to fund such spending.

- The 'own business' segment has shown a high credit risk profile and, within this segment, the retail and service sectors account for the large proportion of clients and outstanding loan balances. The surveys and external data indicate that:
    - Stronger inflation and rising prices have increased at a greater rate than incomes – and this implies, therefore, that trading performance has been adversely affected;
    - Constrained wage levels and lower lending to individuals will have further constrained liquidity in local markets;
    - Informal retailer credit to customers has continued and this will impact upon the cash flow of the respective businesses;
    - Such trading pressures have resulted in:
        - higher levels of loan arrears,
        - higher levels of business failure, and
        - stronger recognition of difficulties in making loan repayments.
    - Nevertheless, whilst this 'own business' segment was only 33% of borrowers (2016 Survey), it represented about 65% of outstanding loan value. This is, therefore, a critically important dimension of the lending business of the lending institutions – in relation to both income and risk.
- The usage of loan funds by the 'own business' segment has been focused upon business needs.

'Own Business' Clients: Usage of Loan Funds	Business		Domestic	Property	Health, Education, Family Events
	Assets	Trading			
MFI	4%	64%	12%	8%	10%
Bank	4%	67%	13%	6%	8%

    - This table indicates a strong focus and commitment by the 'own business' client to support the business activity, with a relatively low leakage of loan funds into domestic expenditure;
    - Whilst the majority of loan usage was for trading / working capital purposes, the loan product was primarily on a fixed-tern, fixed-repayment basis. This is unlikely to be consistent with the underlying cash flow of the business and may, therefore, result in additional pressures upon the borrower;
    - Such lower leakage is, however, offset by higher incomes and, thereby, drawings from the business (possibly funded by loan monies) are not recognised as being the effective (albeit indirect) usage of loan funds for domestic consumption;
    - However, despite the apparent focus to support the continuity of such business activities, this segment (and particularly the retail and service sectors) is exposed to the wider economic and market liquidity risks. These present a generic 'portfolio risk' to this type of lending.
- Lending to this type of borrower requires particular skills:

- The relationship and credit management demands in depressed market conditions require different skills and responses from those in a more buoyant, growth environment;
- The sensitivity of different business to varying external trends (economic, market demand) needs to be continuously monitored;
- The level of market liquidity and demand will vary in relation to wage levels, loan levels and distribution to individuals, the level of retailer credit (to maintain turnover but at the expense of liquidity), and in ward remittance. These factors may be at a quite local, community level – and there is, therefore, a great challenge to the lending institutions to identify these different trading environments;
- Each lending institution will have a somewhat different profile of its 'own business' clients – however, in view of the strategic importance of this segment, it is necessary to gain a strong understanding of the dynamics and sensitivities of the clients.

- The following table seeks to relate these different dynamics to the distribution of borrowers, based upon their perceived risk profile. 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.
  - The basic financial profile of these segments is shown the following tables:

Risk Dimensions[12]	Income	Household and Utility Costs	Loan Repayment	Net Disposable Income	Outstanding Loan
Arrears	3,281	1,357	1,353	571	7,700
Lender Refusal	2,819	1,347	666	806	7,300
Repayment Difficulty	2,738	1,281	778	679	7,600
Expenditure >75% Income	2,763	1,407	1,093	264	8,700
Remainder	3,314	1,276	477	1,561	5,800

  - This table shows the low level of net disposable income for those four segments which demonstrate pressures on the domestic financial budget. The net disposable income is based only on expenditures of food, essential household, utilities and loan repayments. Other domestic costs (such as travel, clothing, education, health and …) need to be met from the NDI amount shown above – and it is primarily such costs which have been impacted by the higher inflationary trends.

[12]Risk Dimensions are based upon: [1] Arrears: payment arrears with current loan; [2] Lender refusal: a lender has refused a loan application by the borrower in the last 12 months, although a loan was subsequently obtained from another lender; [3] Repayment difficulty: the borrower acknowledges to have difficulty in making the loan repayments; [4] Expenditure > 75% Income: the aggregate of essential household, utility and loan repayment expenditures exceed 75% of household income; [5] Remainder: all borrowers not included in segments 1 – 4. No borrower is included in more than one segment.

- The following tabl shows starkly the scale of borrowers and loan balances which are under pressure – and the significant extent to which this has deteriorated in the last 2 years.

2016	MFI				Bank			
	Distribution		Net Disposable Income (post loan)	Loan Balance	Distribution		Net Disposable Income (post loan)	Loan Balance
	Clients	Loan Value			Clients	Loan Value		
Arrears	14%	26%	589	13,512	17%	26%	530	14,786
Lender Refusal	12%	14%	824	8,831	9%	16%	846	16,830
Repayment Difficulty	32%	26%	691	5,903	35%	32%	680	8,687
Expenditure > 75%	22%	25%	258	8,222	19%	18%	259	8,659
Remainder	21%	9%	1,558	3,187	20%	9%	1,501	4,126

Adverse trends shown in red	MFI				Bank			
	Distribution: Clients		Distribution: Loan Value		Distribution: Clients		Distribution: Loan Value	
	2014	2016	2014	2016	2014	2016	2014	2016
Arrears	3%	14%	4%	26%	4%	17%	4%	26%
Lender Refusal	4%	12%	3%	14%	5%	9%	5%	16%
Repayment Difficulty	26%	32%	27%	26%	23%	35%	22%	32%
Expenditure > 75%	40%	22%	44%	25%	40%	19%	49%	18%
Remainder	28%	21%	22%	9%	28%	20%	20%	9%

- These tables highlight:
  - The increased recognition of financial difficulty amongst borrowers;
  - The significant level of borrowers (c.20%) with a high commitment of basic expenditures in relation to income, but who do not acknowledge the pressures which they face. (It should be noted that this segment (>75%) showed greatest change between 2014 and 2016);
  - The very low level of borrowing being undertaken by clients who demonstrate a reasonably sound financial position.
- Nevertheless, these segments continue to show a high level of demand for continued debt finance. However, it is necessary to assess how much of such demand reflects a fundamental debt dependency and how much is discretionary.

	I need to continue to borrow to maintain how my family and I live	Loans improv e the quality of life	Debt repayments cause problems within my family	I would like help to resolve debt problems with my lending institution	Food expenditure has been reduced to make loan repayments
Arrears	86%	49%	67%	61%	62%
Lender Refusal	82%	65%	49%	63%	48%
Repayment Difficulty	92%	61%	76%	72%	52%
Expenditure > 75%	71%	80%	16%	34%	24%
Remainder	64%	76%	13%	26%	19%

- This table shows the strong 'debt dependency' which is perceived by the majority of borrowers – despite the recognition of their inability to handle such situations and the social consequences of the debt burden.

o The usage of loan funds is shown in the following table:

	Business	Domestic			Property
		Asset	Expenses	Health, Education, Family Events	
Arrears	47%	6%	18%	13%	13%
Lender Refusal	24%	9%	25%	18%	21%
Repayment Difficulty	30%	5%	27%	18%	18%
Expenditure > 75%	31%	7%	29%	14%	19%
Remainder	28%	6%	28%	16%	20%

- The diversity of the risk categories and the usage of the last loan demonstrates clearly that there is a need for a differentiation in the recognition, readiness and capacity of these segments to address future lending needs;
- The lending institutions should, ideally, establish differentiated service and product propositions to address the principal characteristics which are reflected in this table.

o The following comments provide observations on these different risk category segments.

o *'Arrears'* this segment clearly has severe repayment problems, together with relatively high levels of informal debt. The repayment period of current residual outstanding debt, based upon current contractual repayment levels, has been lengthened to about 12 months (2014 – about 8 months), which reflects to some extent the refinance / reschedule initiatives of the lending institutions. 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 and may involve further rescheduling. The adverse credit ratings arising from the arrears status may preclude further borrowings in the near future.

o *'Lender Refusal'* the incidence of 'lender refusal' indicates 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 (particularly retailers). The current residual repayment period is 14 months (compared to 8 months in 2014) and probably reflects the more recent renewal of such debt with a new lender. However, the average loan amount is comparatively high and whilst the reschedule / refinance may have provided a short-term stability, this segment remains highly vulnerable to any continuing market pressure. This suggests that the level of outstanding in this current segment will remain stable with some slight net reduction over the next 12 months.

o *'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 greater from family than from retailers.

The proportion of borrowers who recognise their financial problems has increased substantially since 2014. The above table shows that this segment has the highest perception of debt dependency as a means of maintaining their lifestyle, whilst, at the same time, recognising the social impact on their families.

This borrower presents a paradox – the problem of debt is recognised, but yet debt is perceived as the solution. The self-recognition of the debt problem may be considered to be a most important 'first step' in a process towards the establishment of a greater understanding of financial management – it appears that the essential challenge for this segment is a mixture of financial / budgetary education and a more focused use of loan products to address particular needs – for example, the elimination of loan interest in relation to consumption loans would boost disposable income, whilst targeted health or education loans could be structured to meet those usage characteristics.

There appears to be little capacity to increase lending to this segment. A cautious strategic approach to the overall risk exposure of the loan portfolio may cause these borrowings to be reduced whenever possible;

- *'Total expenditures greater than 75% of income'* this segment has a high commitment of current income to basic expenditures and there is minimal residual net income. This segment has not adjusted their lifestyles to reflect their financial situation to the same extent as the other borrower segments. This suggests that this segment may have a more 'laissez-faire' approach towards their financial position. However, in the current market and economic conditions, this segment is extremely vulnerable – not least because they have not acknowledged that they have a problem.

  The lending institutions are strategically vulnerable to this segment of borrowers. The more stringent credit standards may identify some of this segment, but the average outstanding loan amount is relatively high.

- *'Remainder'* this represents only 9% of loan value and21% 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 unchanged atonly 8 months, a substantial proportion of these loans may be anticipated to 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. The proportion of such clients who consider that they need to borrow to maintain family lifestyle increased substantially to 64% (from 27% in 2014), whilst only 19% reduced food expenditure to enable loan repayments. This suggests that this segment have a relatively high discretion in their decision for loan renewal.

  This segment demonstrates a cautious approach to the financial management, maintain higher levels of savings and appear to take a more discretionary approach to borrowings (c.60% have had only one loan in the last 2 years). 74% of this segment anticipate to have a lower level of debt over the next 12 months. These are clearly ‘premium, lower risk’ clients for whom the lending institutions should establish a service proposition which seeks to optimise the retention of the relationship.

- 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”as a result of an entrenched debt dependency– unless there is a deliberate intervention by the lending institutions;
    - 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, which may involve:
        - Continuing use of refinance / reschedule as a necessity to address entrenched debt positions;
        - Differentiated loan product and service propositions to reflect different loan purposes and client segments – which would involve a much greater alignment of the period and terms of the loan with the purpose for which the loan is needed;
        - Particular loans to meet the focused needs of education and health finance;
        - Clarification of the opportunity cost / trade-off between the use of loan funds and the related interest cost for domestic consumption, against the reduction of the use of loans for such purposes thereby generating increased cash flow to the household as a result of lower loan repayment amounts.

5.2 What is the Sensitivity of Affordability?

The loan portfolios show significant sensitivity to relatively modest increases in the costs of basic foodstuffs and household essentials – this presents a significant structural and strategic risk to the lending institutions – there should be close and continuing review of the dynamics of this sensitivity.

- During the period 2014 – 2016, the inflationary cost pressures on foodstuffs have been reasonably stable (see Attachment 4 for review of external economic data sourced from Tajikistan National Statistics). This has contributed to an improvement in the net disposable income of borrowers – with relatively stable underlying household costs and an underlying increase in wage levels.

  This review identifies other actions which have contributed to an improved net disposable income, but this section is focused solely upon the sensitivity of the costs of foodstuffs and essential household needs.

- The following table shows the current distribution of food and household expenditure, together with the impacts of increases of 5% and 10% in such costs. This shows the basic profile of such expenditures.

Monthly Food and Household Expenditure: TJS	< 500	501-800	801-1,000	1,001-1,500	> 1,500	Average	Ave Exp per person
Survey Responses	14%	22%	27%	18%	20%	1,158	202
Increase + 5%	7%	19%	15%	30%	29%	1,216	212
Increase + 10%	7%	19%	15%	29%	30%	1,274	222

- The following tables show the sensitivity of only cost increases to food and essentials being applied to the wider ratio of household income and total committed expenditures (including loan repayments) in relation to income (*note: all other costs (utilities and loan repayments) remain unchanged).*

Household expenditure as % of Income	<25%	26-50%	51-75%	76-100%	>100%
Survey Responses	14%	58%	26%	3%	0%
Increase + 5%	10%	48%	37%	5%	0%
Increase + 10%	9%	45%	39%	7%	0%

Total expenditures as % of Income	<25%	26-50%	51-75%	76-100%	>100%
Survey Responses	2%	12%	32%	41%	13%
Increase + 5%	2%	11%	30%	39%	19%
Increase + 10%	2%	10%	28%	38%	23%

  - These tables show the sensitivity of ‘affordability levels’ in response to relatively modest increase in one dimension of domestic costs – a dimension which has been constrained during the last 2 years. They provide some indication of the additional strains which would have been present in the loan portfolios if such cost increases had occurred;
  - The increase in the proportion of borrowers with committed expenditures (food, household essentials, utilities and loan repayments) in excess of 100% of income (+10%) is substantial. The estimated average loan amount could be about TJS 8,500. This shows the sensitivity of small increases in food costs upon vulnerable domestic budgets in which loan repayments are a substantial component.
- Such sensitivity appears to present a significant structural risk exposure to the credit performance of the loan portfolios. This is further emphasised by the reductions to food expenditures which have been made to enable loan repayments. The lending institutions should monitor such costs trends closely, together with wage trends – if may be anticipated that these provide a strong indicator of future credit performance and are likely to have different regional dynamics.

6 IMPACT OF BORROWING

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

Substantial downturn in attitude towards benefits of loans – stronger recognition of debt repayment difficulties and impact upon lifestyle.

- The impact of the adverse economic and market conditions is reflected in a significant down-turn the borrowers' perceptions of the benefits of loan indebtedness and the impact upon lifestyle.
  - There remains a core attitude which perceives that debt provides a useful contribution to their lives;
  - However, the responses show different attitudes to issues which reflect the need for funds and, in contrast, the impact of such borrowings.
- The contribution of lending is summarised in the following table. The responses of MFI and bank clients are highly similar and, therefore, the responses relate to all borrowers:

Adverse changes shown in red	Demand for Loan			Impact of Loan		
	Loans improve the quality of life	I need to continue to borrow to maintain how my family and I live	I borrowed too much	Debt repayments cause problems within my family	My loan repayments are / were more than I can afford	I would like help to resolve debt problems with my lending institution
2016	67%	80%	35%	47%	50%	52%
2014	93%	48%	25%	22%	29%	29%
Change	-26%	32%	10%	25%	21%	23%

  - These responses appear to indicate that many clients do not perceive an option to continued borrowing – and do not recognise that no loan debt, or a reduced loan amount, would create a greater net disposable income cash flow and thereby greater capacity for food expenditures;
  - This may suggest that borrowers become inured to financial pressure and deprivation of food. Again, this is a fundamental challenge for 'responsible finance' and the responsibility (if at all) upon the lending institution;
  - The amount of the loan reflects what was needed; however, the impact of repayments is somewhat dis-connected from the cause of the problem.

- This interpretation appears to be supported by the responses across the different income ranges.

Household Income 2016: Adverse changes shown in red	Demand for Loan			Impact of Loan		
	Loans improve the quality of life	I need to continue to borrow to maintain how my family and I live	I borrowed too much	Debt repayments cause problems within my family	My loan repayments are / were more than I can afford	I would like help to resolve debt problems with my lending institution
< 1,200	70%	81%	35%	51%	52%	58%
1,201-1,800	65%	85%	32%	50%	50%	53%
1,801-2,600	67%	79%	33%	45%	49%	53%
2,601-3,400	69%	78%	36%	43%	51%	52%
>3,400	65%	79%	37%	45%	48%	47%
Change: 2014 - 2016						
< 1,200	-23%	32%	14%	25%	27%	32%
1,201-1,800	-31%	34%	11%	27%	20%	24%
1,801-2,600	-26%	23%	8%	25%	17%	23%
2,601-3,400	-22%	29%	11%	22%	19%	21%
>3,400	-27%	44%	4%	24%	23%	19%

- These trends may be simply a reaction to the economic and market pressures of the last 2 years. Alternatively, they may indicate a painful lesson about the potential real costs of indebtedness. This is not to suggest a dramatic change of attitude or behaviour – but, it may indicate that behavioural change could occur amongst those borrowers who have the financial capacity to exercise discretion over borrowing, those who have a higher aversion to risk, and those who have particularly suffered as a result of direct and identifiable consequences of over-indebtedness.

6.2 Do microfinance institutions stimulate greater 'financial inclusion'?

No substantial difference in profiles of MFIs and bank borrowers – both MFIs and banks have reduced exposure to lowest income clients.

- Whilst the dimensions of 'financial inclusion' can be widely defined, the core aspects involve:
    - [i] the provision of financial services (including loans) to lower income groups,
    - [ii] wider inclusion, equal treatment and empowerment of female clients, and
    - [iii] respect for the individual by the lending institution.
- The borrower profiles of MFI and bank clients are very similar – with few indications of any significant differentiation in the market positions undertaken by the MFIs.

% of borrowers 2016	Own Business	Household Income less than TJS 1,200	Number of Dependents	Rural Location	Receipt of Remittances
MFI	36%	14%	3.5	28%	15%
Bank	40%	11%	3.6	26%	15%
2014					
MFI	47 %	19 %	3.2	24 %	28%
Bank	47 %	13 %	3.3	29 %	31%

- However, there has been a reduction / exclusion of lower income households during the period 2014 – 2016.

Distribution of borrowers 2016	< 1,200	1,201-1,800	1,801-2,600	2,601-3,400	>3,400
MFI	14%	19%	25%	17%	24%
Bank	11%	17%	27%	17%	28%
2014					
MFI	19%	19%	27%	14%	21%
Bank	13%	18%	28%	15%	26%
Change: 2014 - 2016					
MFI	-5%	-	-2%	+3%	+3%
Bank	-2%	-1%	-1%	+2%	+2%

  - The 2014 survey responses showed the lower income segments to be experiencing particular financial pressures and that the level of lending and loan repayments were, for many borrowers, excessive in relation to net disposable income (after food, essential household and utility costs);
  - The reduction in the proportion of clients in the lowest income segments does, therefore, reflect a prudent and responsible action by lending institutions;
  - However, such clients had been brought to lending by 'financial inclusion' strategies which for the survey respondents, primarily involves loan finance (the levels of savings and insurance with financial institutions has been shown to be very low);
  - The loan repayment performance is, for many clients, being supported by greater social and community actions being demonstrated by increased requirement for inter-personal guarantees from friends, informal loans from family and friends, retailer support and reduction to the food expenditure and lifestyle of the family;
  - This marginal segment of clients presents a dichotomy which is particularly sensitive to fluctuations in external influences (economy, market, remittance levels) – all of which are outside the direct control of the borrower.
- This situation presents a fundamental challenge to the strategy of 'financial inclusion':
  - The lending institutions have a responsibility to undertake stable lending policies which, as in the last 2 years, can appear contrary to 'financial inclusion';
  - The strategy for 'financial inclusion' should address the continuing role of financial services across a range of economic scenarios, rather than a potential see-saw of 'inclusion' and 'exclusion' actions;
  - The fluctuating actions of financial institutions in relation to the inclusion of the more marginal borrowing client segments may undermine the reputation of the industry towards this group.

7 LENDER / BORROWER RELATIONSHIP

7.1 What is the reputation of the lending institutions?

Continuing overall strength but at reduced levels from 2014.

- The reputation of the lending institutions was considered in relation to the perceptions of respondents of both cultural values and also operational performance;
- The survey responses show that there has been some erosion of the strong reputation of financial institutions which was shown in 2014. Against a background of difficult economic and market conditions, it may not be surprising that public opinion has faded somewhat – however, the reputation continues to remains relatively strong.

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	96%	89%	87%	84%	87%
Current: Bank	96%	87%	84%	81%	85%
Former[13]: MFI	97%	85%	81%	81%	83%
Former: Bank	94%	86%	84%	79%	83%
Non-Borrowers	94%	75%	78%	74%	73%

2014	Respect	Trustworthy	Integrity	Understand needs	Improve lives of clients
Current: MFI	98%	96%	96%	95%	94%
Current: Bank	98%	97%	96%	95%	95%
Former[14]: MFI	97%	97%	94%	93%	95%
Former: Bank	96%	91%	90%	92%	85%
Non-Borrowers	97%	91%	90%	90%	90%

- There is minimal difference in the attitudes of current MFI and bank borrowers, although former bank clients do show a slightly less positive view;
- The perceptions of non-borrowers have deteriorated to a greater level than those of borrowers. This may suggest a more concerning trend for the financial institutions and that such reputational issues should be within their strategic development:
  - It may be noted that savings are taken principally outside the financial institutions;
  - If the broader development of 'financial service inclusion' is to increase the focus upon savings, then the reputational issues will become even more important.

[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

[14] 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

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 – recognition by 58% that the risks in foreign currency lending were explained.

- There is a continuing and strong recognition that the terms of the loan (in national Somoni currency) are being explained. This is reflected by about95% of the borrowers of both MFIs and banks;
- The communication of loan terms in relation to foreign currency lending presents a more complex situation.
    - In relation to the explanation of the basic terms of the loan, it appears that the lending institutions are recognised to have achieved this satisfactorily.

% of borrowers who 'Agree'	Lending institutions explain the terms and obligations of the loan			
	MFI		Bank	
	2014	2016	2014	2016
TJS Currency	98%	94%	98%	95%
Foreign Currency	96%	86%	99%	89%

- This table shows strong recognition of the explanation by the lending institution, even for the foreign currency loans which have been subject to the extreme pressures of severe devaluation of the TJS Somoni.

- However, there is a difference between an explanation of the terms of the foreign currency loan and the particular risks of foreign currency debt. The 2016 survey responses show that 58% of foreign currency borrowers agreed that the lending institution did explain the risks of exchange rate changes (MFI: 59% and Bank 57%). However, after several years of exchange stability, the risks of such extreme devaluation may not have been well-understood or recognised at the time of the loan inception.

7.3 Do lenders understand the borrower's financial position?

Continuing favourable perception of lending institutions – minimal change in the ease with which loans can be obtained – some deterioration in the resolution of debt problems with lending institution.

- The responses suggest that whilst a majority of borrowers perceive that the lenders have understood their borrowing needs and capacity, there is a sizeable minority (about 25%) 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	96%	84%	74%	32%	49%	37%
Bank	95%	81%	66%	40%	53%	43%
2014						
MFI	84%	95%	79%	26%	29%	24%
Bank	83%	95%	76%	25%	28%	25%

- This series of questions reflect a continuum in the borrowing process which appears to show a relatively positive attitude to the lender / borrower relationship. It may be anticipated that there will always be some tensions between borrower and lender – however, the above table does not suggest any systemic relationship problem at this stage, although there has been a deterioration since 2014.

   i. The 'assessment of affordability' has strengthened in 2016. This may suggest that respondents are indicating that they provided 'reliable' information to the lending institution and, therefore, any repayment difficulties should have been identified at the time of loan application / approval. *(This is simply a possible interpretation by the writer);*

   ii. The 'understanding of customer needs' shows a reduction in 2016 which, perhaps, suggests a perception that the lending institution is not fully aware of the 'on-the-ground' experience of the borrower – or possibly that the motivation of the loan officer is driven by targets which are not aligned the client situation;

   iii. 'Loan access' is only slightly reduced. This does not suggest that the lending institutions have been unduly draconian in any revision of credit approval criteria;

   iv. 'Borrowed too much' may reflect two principal dimensions:

      - The borrower requested more than was needed; or
      - The lending institution encouraged the borrower to take an excessive loan amount. Whilst the responses show an increase, it does not suggest that this was major cause of problem lending.

   v. 'Loan repayments' show a strong increase. This is widely discussed elsewhere in this review;

   vi. 'Resolve with lender' shows a strong increase in the difficulty of resolution with the lending institution. This seems to be an inevitable adverse trend as many borrowers will have few immediate options by which to address their problems. Other responses indicate some increase in refinance (albeit not widespread) and an increase in the average repayment period. This situation is linked also to the recognition (about 50-55%) by borrowers that they need some assistance in their discussions with lenders.

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

Some deterioration in ability to resolve debt problems – substantive regional differences – increased recognition by borrowers of need for assistance in dealings with lending institution.

- About 40% (2014 - 25%) of borrowers (similar levels in MFIs and banks) considered that it is difficult to resolve debt problems with their lenders – and – about 50% (2014 – 30%) recognised that they would like assistance in dealing with their lending institutions about problem debt.

- This varied significantly across the regions which suggests different client relationship strategies being applied at local levels.

	It is / was difficult to resolve debt problems with my lender		I would like help to resolve debt problems with my lending institution	
	2014	2016	2014	2016
Dushanbe	23%	48%	20%	51%
Khatlon	40%	34%	20%	51%
Sogd	14%	46%	22%	39%
RRP	4%	29%	38%	37%
GBAO	44%	37%	47%	83%

- Such attitudes are focused, not surprisingly, upon those client segments which recognise their debt management problems.

	It is / was difficult to resolve debt problems with my lender		I would like help to resolve debt problems with my lending institution	
	2014	2016	2014	2016
Arrears	46%	50%	44%	61%
Lender Refusal	31%	42%	37%	63%
Repayment Difficulty	40%	56%	59%	72%
Expenditure > 75%	18%	21%	15%	34%
Remainder	17%	18%	18%	26%

Attachment 1a.

Survey Structure

A survey was undertaken during June 2016 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 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.

The operational implementation of the 2016 was consistent with that undertaken for the 2014 survey. The following dimensions of such consistency may be noted:

- The same research agency, Middle Asia Management Consulting, was employed;
- The structure and questions of the survey were largely unchanged, together with the briefing notes for the interviewers;
- The dates of the survey interviews were similar (May 2014 and June 2016);
- The locations of the interviews were unchanged within the regions (see below);
- The slight reduction in the number of bank borrowers in certain regions reflects the difficulty of the research agency in finding such persons

The survey was undertaken and co-ordinated by a local research agency and was conducted in five regions. (Comparable figures for 2014 are shown in brackets)

Location	Total Number of Respondents	Number of Borrowers from Microfinance	Number of Borrowers from Banks	Non – Borrowers
Dushanbe	850 .. (850)	396 ... (427)	293 .. (310)	179 .. (145)
Khatlon	800 .. (850)	413 .. (379)	269 .. (328)	135 .. (147)
Sogd	800 .. (850)	402 .. (428)	259 .. (299)	139 .. (141)
RRP	800 .. (850)	387 .. (412)	260 .. (317)	154 .. (122)
GBAO	750 .. (600)	364 .. (398)	261 .. (210)	155 .. (0)
Total	4,000 .. (4,000)	1,962 .. (2,044)	1,342 .. (1,464)	762 .. (555)

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

Source: LonelyPlanet.com

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:
  - persons currently with a loan with a microfinance institution;
  - 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[15]	Dushanbe	Khatlon	Sogd	RRP	GBAO
City	71% (100%)	32% (34%)	32% (26%)	34% (32%)	32%(33%)
Urban	29% (0%)	33% (33%)	35% (30%)	33% (35%)	33% (37%)
Rural	0% (0%)	35% (33%)	33% (34%)	33% (33%)	35% (31%)

A summary of the principal demographic characteristics (based on the above sample process) is set out in the following table (Attachment 1b.)

Validation of Data

Survey responses for the 2014 and 2016 were compared with available, appropriate, published external data, involving:

Statistical Agency, Tajikistan :	Food Security and Poverty Report No. 1 2013
Statistical Agency, Tajikistan :	Labour Workforce Survey
Statistical Agency, Tajikistan :	GDP Economic data
Statistical Agency, Tajikistan :	Impact of migration and remittances, August 2010
National Bank, Tajikistan:	Statistics Review, 2013

Survey 2016 was compared with 2014 and also trends identified by national statistics (see attachment 4).

Survey Response: Detailed review and validation of individual survey responses was undertaken by the independent local research agency.

15 City / Town: an area of relatively concentrated population and housing
Urban: away from more densely-populated areas of the city/town, but within convenient distance for easy transportation to a nearby city/town
Rural: primarily a village or agricultural community

Attachment 1b.

Principal Demographics of Survey Respondents

The comparable distributions in the 2014 Survey are shown in brackets. The totals may exceed 100% as a result of multiple borrowings with different institutions.

Age

	16-25	26-35	36-45	46-55	> 55
Borrowers: MFI	13% .. (9%)	34% .. (35%)	27% .. (28%)	21% .. (22%)	5% .. (7%)
Borrowers: Bank	9% .. (11%)	34% .. (33%)	24% .. (27%)	26% .. (22%)	6% .. (6%)
Non-Borrowers	22% .. (14%)	36% .. (31%)	15% .. (26%)	19% .. (22%)	7% .. (7%)

Location

Borrowers only	16-25	26-35	36-45	46-55	> 55
City - MFI	16% .. (10%)	33% .. (36%)	27% .. (28%)	20% .. (22%)	5% .. (5%)
City - Bank	12% .. (13%)	35% .. (36%)	25% .. (27%)	23% .. (20%)	5% .. (4%)
Urban - MFI	10% .. (10%)	34% .. (31%)	30% .. (29%)	21% .. (21%)	5% .. (10%)
Urban - Bank	7% .. (11%)	34% .. (31%)	24% .. (29%)	28% .. (21%)	7% .. (8%)
Rural - MFI	13% .. (8%)	36% .. (37%)	25% .. (25%)	21% .. (23%)	5% .. (7%)
Rural - Bank	7% .. (9%)	33% .. (32%)	24% .. (24%)	29% .. (28%)	8% .. (7%)

Number of Persons in the Household

	< 2	3	4	5	> 5
Borrowers: MFI	3% .. (3%)	10% .. (9%)	19% .. (20%)	22% .. (23%)	47% .. (45%)
Borrowers: Bank	4% .. (3%)	8% .. (9%)	18% .. (17%)	22% .. (20%)	48% .. (51%)
Non-Borrowers	5% .. (4%)	13% .. (8%)	21% .. (20%)	20% .. (20%)	41% .. (49%)

Location

Borrowers only	< 2	3	4	5	> 5
City - MFI	4% .. (4%)	9% .. (11%)	19% .. (24%)	24% .. (23%)	44% .. (38%)
City - Bank	4% .. (4%)	8% .. (12%)	19% .. (23%)	25% .. (19%)	44% .. (42%)
Urban - MFI	2% .. (3%)	10% .. (9%)	20% .. (16%)	20% .. (21%)	48% .. (51%)
Urban - Bank	4% .. (2%)	7% .. (7%)	16% .. (14%)	21% .. (21%)	52% .. (57%)
Rural - MFI	4% .. (3%)	10% .. (6%)	17% .. (15%)	21% .. (23%)	49% .. (53%)
Rural - Bank	4% .. (2%)	8% .. (6%)	19% .. (12%)	17% .. (21%)	51% .. (59%)

Attachment 2.

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 money lender;
- 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.

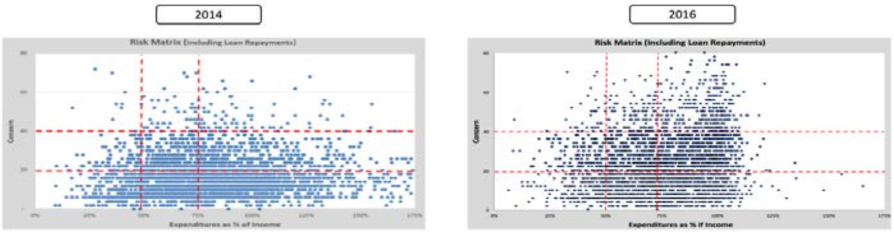


Chart: Expenditures include household and utilities, including loan repayments

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

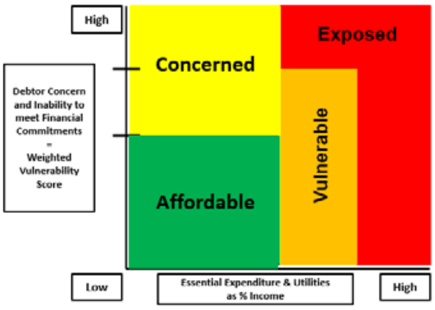


Chart 3. Client risk matrix

Such a matrix enables a broad differentiation between those clients who have possibly 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.

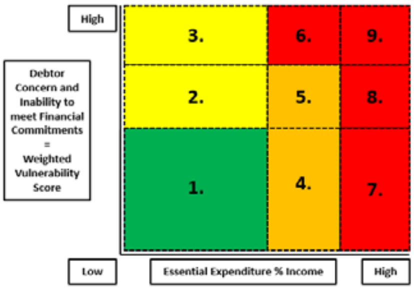


Chart 4. Segmentation of client risk and vulnerability

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.

Attachment 3.

Survey Questionnaire

CLIENT SURVEY - INDIVIDUAL

We would like to better understand about how you undertake loan repayments.
All responses will remain confidential - No Personal Identification or Contact Details are requested

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	Micro-finance institution					Q.1.a	
Q.2	Commercial bank					Q.2.a	

3-9 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 ☐

Q. 9 How long have you lived in this neighbourhood *years* ☐

10-13 Income *(All Respondents)*

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

Q.10 Regular work ☐ Irregular work ☐ Own Business ☐ Remittance ☐ Other inc. occasional sales and social subsidies ☐ None ☐

Q.11 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.12 How would you describe the receipt of your income payments *(Tick any which apply)*
From employer by bank transfer ☐ From employer by cash / cheque ☐ Income from social subsidies ☐ Occasional or irregular payments ☐ Income from own business ☐

Q.13 How many people earn income in your household *(Please enter number)* ☐

14-24 Household Budget *(All Respondents)*

Q.14 How much is the average **total monthly** income into your household budget *(Please enter amount)* TJS ☐

Q.15 How much do you spend **each month** (on average) on food and household expenditure TJS ☐

Q.16 How much do you spend **each month** (on average) on gas, electricity, water, rent, garbage collection TJS ☐

Q.17 Do you have any payment arrears with any of electricity, gas, water, or housing costs Yes ☐ No ☐

Do you have loans from non-financial institutions :

		Yes, loan outstanding	Not now, but in last 2 years	Never
Q.18	Family			
Q.19	Friends			
Q.20	Retail shop : to purchase higher-value assets (such as car, washer, refrigerator)			
Q.21	Retail shop : to obtain normal domestic items (such as food, personal items, household needs)			
Q.22	Moneylender or Pawnshop			
Q.23	Employer			
Q.24	Other			

25-37 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.25	I lost my job			**Q.26**	My business was not successful		
Q.27	My spouse / partner lost his/her job			**Q.28**	I had to sell a major asset to repay a loan		
Q.29	Major illness of self or family			**Q.30**	Remittance income stopped, or reduced		

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

		Strongly Agree	Agree	Disagree	Strongly Disagree	Do Not Know / No Opinion
Q.31	My financial situation has improved in the last 6 months					
Q.32	I feel in control of my financial situation					
Q.33	My children will have a better life than me.					
Q.34	My household expenses have risen faster than income in the last 6 months					
Q.35	The quality of my life has improved in the last 12 months					
Q.36	I can afford to buy 'treats' for myself or my family					
Q.37	Most of my friends have difficulties meeting their domestic budget needs					

38-42 Loan Dimensions ***(Current and Former Borrowers)*** Please tell us about your loan(s)

Q.38 What type(s) of loan do you use now and in which currency *(Please tick all which apply)*

	TJS	Fgn Ccy
Business loan		
Individual loan : fixed repayments		
Individual loan : other		
House / property mortgage loan		
Agricultural loan		
Education loan		
Credit card		
Overdraft		

Q.39 What was the main reason(s) for your last loan and your next loan *(Mark up to two reasons)*

	Last loan	Next loan
Business : Asset acquisition		
Business : Trading finance		
Domestic : Asset acquisition		
Domestic : Living expenses		
Domestic : Property acquisition		
Domestic : Property improvement		
Domestic : Health or education		
Domestic : Holiday or travel or family event		
Repay / increase existing loan		

Q.40 During the last 2 years, how many loans have you taken *Enter number*

Q.41 How many lenders have you used for these loans *Enter number*

Q.42 How many guarantees have you given for debts which are still outstanding *Enter number*

43-58 Loan Dimensions ***(Current Borrowers)*** Please tell us about your loan(s)

Q.43 Total amount outstanding of all loans

Q.44 How much is total **monthly** repayments for all loans (include MFIs, banks, house mortgage)

(Please enter TJS amounts for Q. 43 and Q.44)

		Yes	No
Q.45	Have you pledged any assets as collateral to secure your loan		

Q.46 If 'yes', which collateral was provided *(please tick all which apply)*

Business Property ☐ Residential Property ☐ Business Equipment ☐ Domestic Asset(s) ☐ Vehicle ☐ Guarantee ☐ Gold / Jewellry ☐

		Yes	No
Q.47	Is any of your loan indebtedness (Q.43) outstanding in a currency which is not Tajikistan Somoni		

Q.48 If 'Yes' (Q.47), what is the foreign currency loan balance US$ ☐ Euro ☐ Other ☐ Amount

Q.49	If 'Yes' (Q.47), did the lending institution explain the risks of exchange rate changes to you		
Q.50	Are any of your loan payments in arrears or not fully up-to-date		
Q.51	Have you refinanced, or consolidated your debts during the last 12 months		
Q.52	Have you applied for a loan in the last 12 months		
Q.53	Has any lender refused to lend to you in the last 12 months		
Q.54	Have you received any formal legal action for debt non-repayment in the last 12 months		
	When you took your loan, did you obtain your credit rating		

Q.55 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.56	Compared with 12 months ago your present total loans are	Much Higher	☐	Higher	☐	The Same	☐	Less	☐	Much Less ☐
Q.57	After the next 12 months, do you expect your debt level to be	Much Higher	☐	Higher	☐	The Same	☐	Less	☐	Much Less ☐
Q.58	Who undertakes the loans in your family	Only you	☐	Only your spouse/partner	☐	Jointly	☐	Both of you independently	☐	

59-66 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.59	Clients are treated with respect	☐	☐	☐	☐	☐
Q.60	The institutions respond well to people with repayment problems	☐	☐	☐	☐	☐
Q.61	Lending institutions are trustworthy	☐	☐	☐	☐	☐
Q.62	Lending institutions seek to improve the lives of its clients	☐	☐	☐	☐	☐
Q.63	Lending institutions act with integrity	☐	☐	☐	☐	☐
Q.64	Lending institutions understand customers' needs	☐	☐	☐	☐	☐
Q.65	Lending institutions explain the terms and obligations of the loan	☐	☐	☐	☐	☐
Q.66	Lending institutions want to lend to people like me	☐	☐	☐	☐	☐

67-80 We would like to know your opinion, and how much you agree with the following statements *(Current and Former Borrowers)*

		Strongly Agree	Agree	Disagree	Strongly Disagree	Do Not Know / No Opinion
Q.67	Loans improve the quality of life	☐	☐	☐	☐	☐
Q.68	When I took my last loan, the charges (interest and fees) were explained to me and I know how much I am paying	☐	☐	☐	☐	☐
Q.69	I understand which type(s) of loan should be used for different needs	☐	☐	☐	☐	☐
Q.70	Loans are easy to obtain	☐	☐	☐	☐	☐
Q.71	I borrowed too much	☐	☐	☐	☐	☐
Q.72	It is / was difficult to resolve debt problems with lending institutions	☐	☐	☐	☐	☐
Q.73	Debt repayments cause problems within my family	☐	☐	☐	☐	☐
Q.74	My loan repayments are / were more than I can afford	☐	☐	☐	☐	☐
Q.75	I need / needed to continue to borrow to maintain how my family and I live	☐	☐	☐	☐	☐
Q.76	I would like help to resolve debt problems with my lending institution	☐	☐	☐	☐	☐
Q.77	It is better to borrow from only one institution, rather than to change lenders	☐	☐	☐	☐	☐
Q.78	When I drew my last loan, the lender knew what I could afford	☐	☐	☐	☐	☐

Q.79	Food expenditure has been reduced to make loan repayments	Yes	☐	No	☐
Q.80	I (or my spouse) have taken additional work to make loan repayments	Yes	☐	No	☐

81-83 We would like to know your attitudes towards saving. *(All Respondents)*

Q.81	Do you make savings with a financial institution	Yes	☐	No	☐
Q.82	Do you make other regular cash savings	Yes	☐	No	☐
Q.83	Have you bought an insurance product(s) from your financial institution	Yes	☐	No	☐

84-85 From which institution(s) have you borrowed in the last 2 years *(Current and Former Borrowers)*

(Please tick all which apply)

Q.84	Microfinance Institution		**Q. 85**	Commercial Bank	
	Imon International	☐		Agroinvestbank	☐
	Arvand	☐		Amonatbank	☐
	Humo	☐		Tojiksodirotbank	☐
	Finca	☐		Tajprombank	☐
	Matin	☐		Bank Eskhata	☐
	Dastras	☐		Sohibkorbank	☐
	Tamvil	☐		First MicroFinanceBank	☐
	Oxus	☐		AccessBank	☐
	Other' : Please name institution :			*Other' : Please name institution :*	

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

External Data

Comparative Assessment of Survey Findings

The following observations[16] are derived from external 'public domain' data sources. They reflect issues which relate to the 2016 Indebtedness Survey. The principal data sources are:

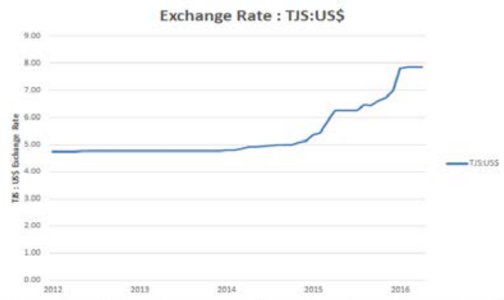
- Tajikistan Statistical Office;
- National Bank of Tajikistan;
- World Bank Group (economic updates and "Listening to Tajikistan";
- MixMarket microfinance data.

There is a range of available data dates. It is intended that these provide some broad positioning for the survey responses – either to directly validate the findings, or to identify issues on which there appears to be reasons for difference.

Exchange Rate and Inflation: Consumer Price Index (CPI)

The trends of exchange rate and inflation are important dimensions in any assessment of the financial capacity of individuals in recent years.

The major devaluation of the TJS Somoni (against the US Dollar) is highlighted in the following graph.



Devaluation pressures occurred also in relation to the value of TJS against the Russian Rouble[17]. The substantive implications of such adverse currency movements will be highlighted in relation to the borrowings by individuals in currency (predominately in US$) and the inward remittance of funds by overseas workers (predominately in Russian Roubles).

Survey Observation: The proportion of respondents receiving remittances fell substantially in 2016, compared with 2014. Borrowers reduced from 29% of respondents in 2014 to 15% in 2016; amongst non-borrowers, receipt of remittances fell from 34% to 18%.

The following chart contrasts the dramatic devaluation of the TJS Somoni against the continuing increase in inflationary pressure.

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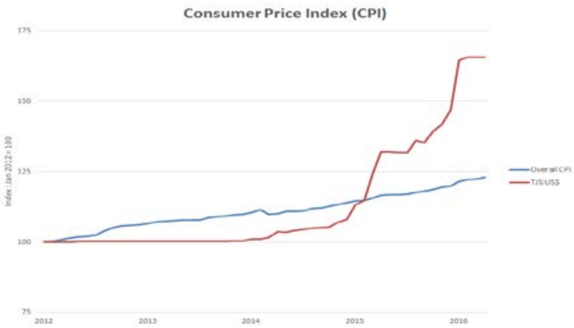
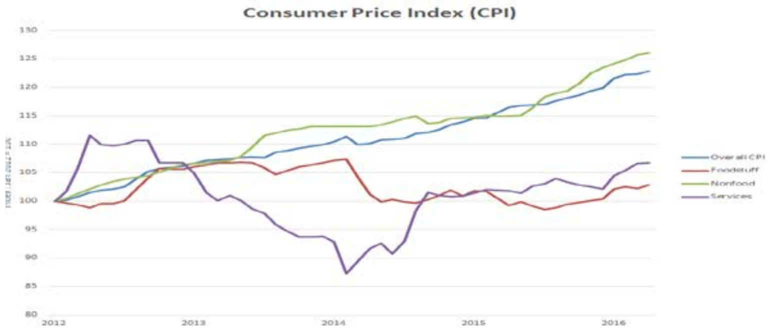
[16] This external reference was undertaken prior to the analysis of the survey findings. It is written, therefore in a somewhat objective manner to provide a 'benchmark' for the survey findings. Comparative observations from the survey are shown in italics.

[17] Source: Exchange Rate: Russian Ruble: TJS Somoni: XE Converter
http://www.xe.com/currencycharts/?from=RUB&to=TJS&view=5Y



However, within the overall growth of CPI, there have been different inflationary pressures.



This chart demonstrates that there has been minimal net change in the current level of the nominal costs of foodstuffs and services, compared with 2012. This contrasts with the substantive increase in the cost of household goods (non-foodstuff). Such increases occur particularly in 2015-2016 and reflect the high level of imports of such goods – and thereby the adverse effect of the exchange rate devaluation.

Such price dynamics will have a direct, and immediate, impact upon the financial capacity and expenditure pattern of household budgets. It must be further anticipated that different income segments will have varying capacities to respond to such pressures.

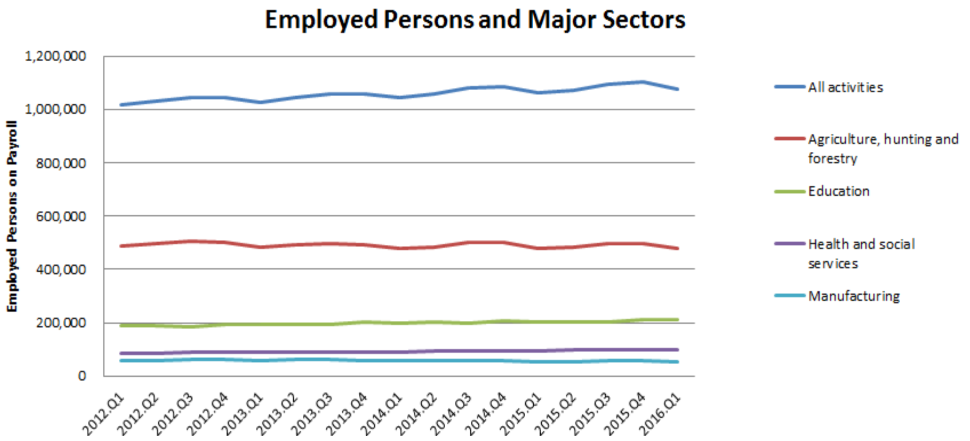
Furthermore, such volatility and uncertainty in market conditions and prices may be anticipated to impact upon the attitudes of individuals towards their risk appetite, or aversion, in their financial management and borrowing (or savings) behaviour.

Survey Observation: The level of domestic expenditures on foodstuffs and other household essential was broadly unchanged in the 2014 and 2016 surveys(see following table). Whilst this containment of basic food expenditure improved the net domestic disposable income, the higher price rises in non-foodstuffs was starkly reflected in the deterioration of the borrowers' overall financial position.

TJS	Food and Basic Household Expenditure		Food and Basic Household Expenditure per person	
	2014	2016	2014	2016
Borrowers	1,145	1,158	203	202
Non-Borrowers	1,134	1,140	197	213

Employment and Trade Sectors

National statistics indicate that formal employment has remained steady during recent years. This is shown in the following chart:



These principal trade sectors account for over 80% of formal employment. This does not indicate that there has been any substantive overall increase in the levels of redundancy. However, separate research data indicates that there was also an increase in the level of informal economic activity. This data is only available to end-2014 and does not, therefore, reflect the economic pressures of the last two years – but it does, perhaps, suggest a change in the earnings profile of households which may be anticipated to have continued in the latest years of financial pressure and austerity.

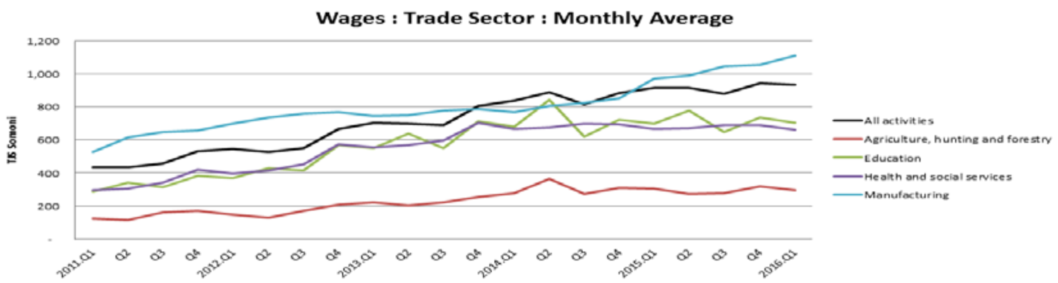
The following table shows that formal employment levels of the major trade sectors. This shows clearly the dominant role of agriculture in employment – a later section will show that agriculture has also the lowest level of income. It may also be noted that the next two largest segments are in the 'public sector' and the constraints upon the income of these are shown later.

	Agriculture	Education	Health & Social Services	Manufacturing
% of total formal employment	45%	20%	9%	5%

Survey Observation: The levels of 'job loss' were slightly higher in 2016 compared with 2014: 8% against 5% in relation to the borrower, and 20% against 13% for the spouse of the borrowers. The highest levels of 'job loss' were seen in the engineering and service sectors.

Income

The following chart shows that the trade sectors of largest employment provided lower-than-average monthly wages. (The graph shows nominal income levels).

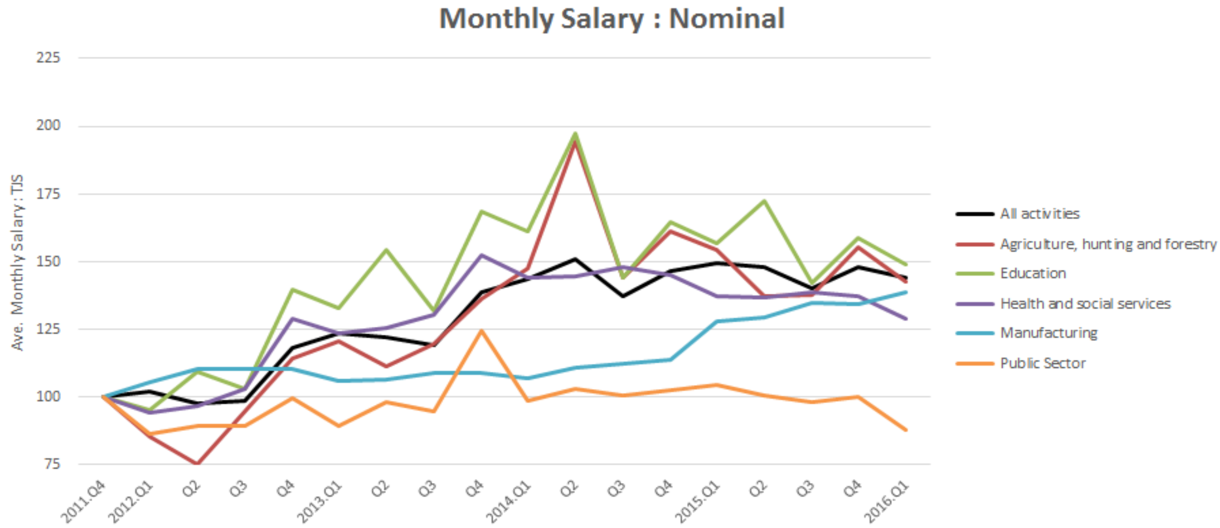


This chart shows that the three largest employment sectors have shown minimal change in average income levels since Q4.2013. This suggests that there is likely to have been increasing pressure on the domestic household budgets during this time.

Survey Observation: The following table compares the average monthly income per earner for the principal trade sectors of respondents. This highlights the particular constraint upon the 'public sector' employees.

	Average Monthly Income per earner		
	2014	2016	Change 2014-16
Retail	1,520	1,737	14%
Engineering	894	1,183	32%
Building - Property	1,270	1,431	13%
Service	1,037	1,375	33%
Agriculture	894	1,128	26%
Public Sector	1,045	1,070	2%

The following chart shows the changes in average monthly income levels, indexed against 2011.Q4. This shows the progressive reductions in most trade sectors (particularly those with higher employment levels) over the last two years. This identifies the need for a differentiated assessment of the borrowing clients in relation to the various trade segments.



The following charts demonstrate how incomes have been eroded by inflation during recent years.

The left-hand chart shows nominal average monthly salaries, whilst the right-hand chart emphasises the erosion of inflation, indexed against 2011.Q4.

Such continuing erosion of the real disposable income of wage-earners will have placed increasing pressure upon the domestic household budgets and the prioritisation of expenditures. It may be further noted that any sustained, or substantive, development of the self-employed / informal economic activities by household members will require a continuing buoyancy of the purchasing power of the local economies of their communities. The impact of inflation upon the real spending power of households will constrain the capacity for such 'own business' activity.

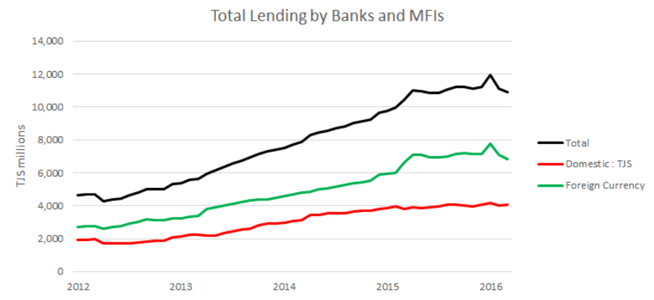
Survey Observation: ***The average monthly income per wage-earner in the 2016 survey was affected by the structural redistribution of the loan portfolio towards higher income clients. The overall average of wage increase per earner of 16% is, therefore, not comparable with the overall 12% shown by the national statistics. However in a relatively tightly defined client sector as 'public sector employees', the increase of 2% in borrower income (2014-2016) is consistent with the national statistics.The 2016 survey identified a significant increase in the pressure on the 'own business' segment, together with a higher level of 'own business' failures. These borrowers are primarily in the retail sector and the constrained levels of CPI-adjusted income will be reflected in the pressures on consumer demand.***

Lending

Lending statistics by the National Bank show lending levels in domestic and foreign currencies by lending institutions, but do not provide separate figures to show the components of loans to businesses and individuals. The following charts show, therefore, total advances by lending institutions. The trends should, therefore, should be regarded as possibly indicative of the underlying trends.

The trend in outstanding loan balances (expressed in TJS Somoni) is shown in the following chart[18].

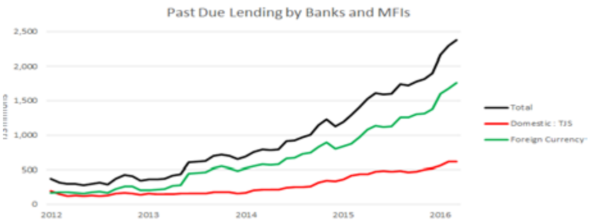
This shows that the level of lending in domestic currency has broadly been unchanged over the last year, whilst the TJS Somoni equivalent liability of foreign currency advances has increased substantially (until 2016.Q1).

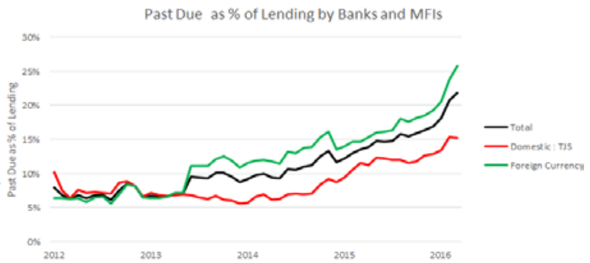


Survey Observation: ***There has been a slow-down in the level of new / renewal lending in the 6 months prior to the survey (January – June). This reflects the trend of domestic lending in the above graph.***

The impact of economic pressures, inflation, and adverse exchange rate movements (TJS against the US$) are clearly shown in the following trends of 'past due' arrears in lending.

[18] Note: the significant effect of the US$ / TJS exchange rate movements will be shown later.





This is clearly a substantive deterioration of the credit quality of the loan portfolio. (It may be noted that the 2014 Survey of the Indebtedness of Individuals demonstrated the delicate vulnerability of the majority of individual borrowers to adverse trends upon their domestic household budgets).

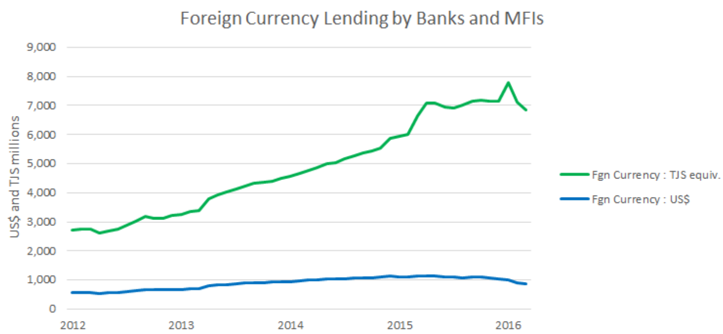
Survey Observation: Loan Arrears increased sharply in 2016 compared with 2014. The level of arrears amongst TJS Somoni loans of survey respondents was 13% (2014: 3%), whilst arrears in relation to loans in foreign currency was 40% (2014: 5%).

Whilst the deterioration of the foreign currency borrowers is particularly severe (reflecting the colliding pressures of constrained income, price inflation and adverse exchange rate movements), the performance of the domestic currency loan portfolio also shows a significant adverse trend. (It may be further noted that loan arrears are usually only the 'tip of the iceberg' of financial pressure, as borrowers will seek to meet their financial commitments and, for some, seek to avoid the potential loss of assets being held as collateral for the loan indebtedness).

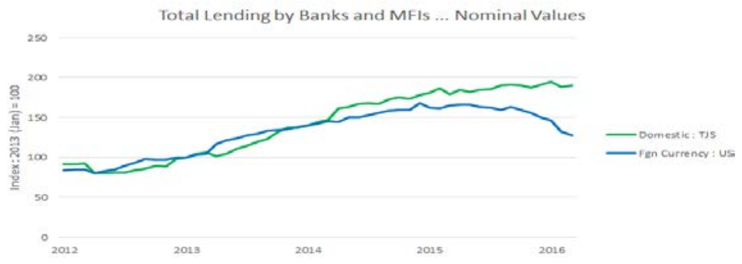
The credit quality appears to have declined more sharply in the last 6 months in both domestic and foreign currency loan portfolios. As the economic pressures continue, this may suggest that borrowers are finding ever-less capacity to maintain their repayments – alternatively, it may suggest that those borrowers with some greater capacity to effect repayments, have been able to achieve debt reductions / repayment, whilst a greater proportion of the residual borrowers have a worse credit profile and increasingly constrained financial capacity.

This may be summarised as a 'flight to quality' and a reduced willingness of those with some financial capacity to maintain / undertake indebtedness. This will be further considered later in relation to trends in savings by individuals.

The substantive increase in foreign currency lending (expressed in TJS equivalent) is, of course, significantly impacted by the adverse movement in the TJS / US$ exchange rate. The following chart contrasts the TJS equivalent liability with the underlying US Dollar exposure.



This shows that the level of US Dollar exposure has been largely unchanged for the last 5 years, with some reduction occurring in the last year. This trend may be contrasted with the similar growth rate of domestic lending until 2014, after which domestic lending showed a comparative increase . (Note: It is not known if the National Bank imposed limitations on the availability / drawdown of foreign currency lending).

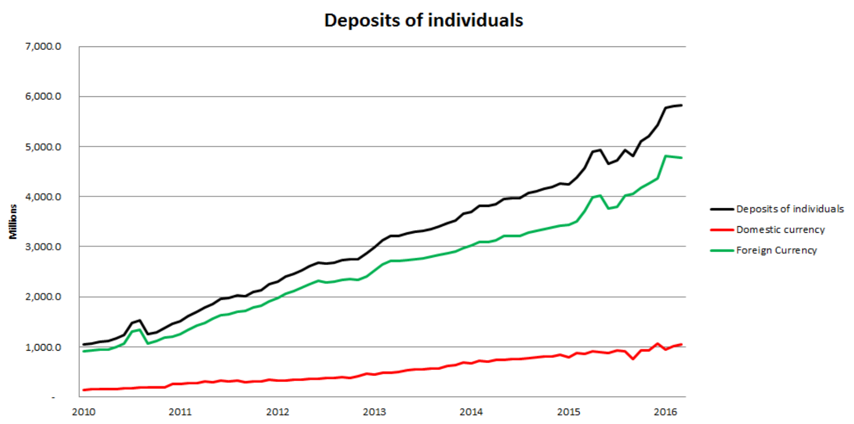


Survey Observation: Between 2014 and 2016 there was a significant reduction (in the survey samples) in the level of foreign currency loans – with the proportion of borrowers falling from 27% to 7%, and the related value of outstanding loans (in TJS equivalent) reducing from 43% to 27%.

Deposits

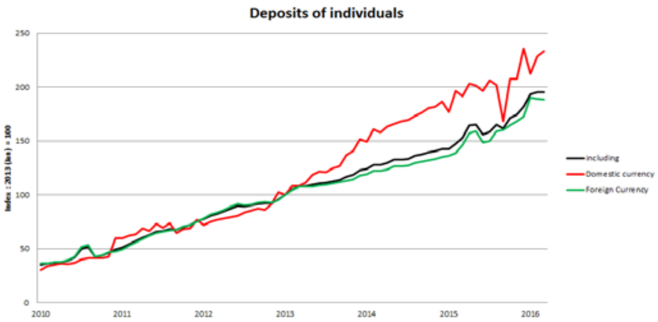
The trends in deposits with financial institutions provide an important insight of the attitudes and behaviour of individuals during this period of changing economic conditions and turbulence.

The following chart shows the levels of deposits by individuals[19] with financial institutions (expressed in TJS Somoni equivalents).



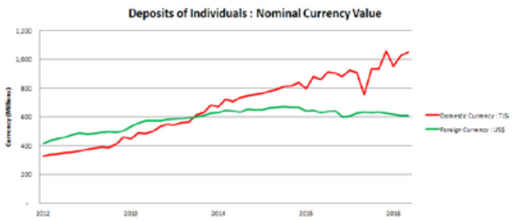
Whilst the TJS value of foreign currency balances has increased sharply (reflecting the favourable benefit of exchange rate movements for depositors), the growth of domestic deposits increased at a greater rate after 2013. This is shown in the following chart, indexed at 2013.Q1.

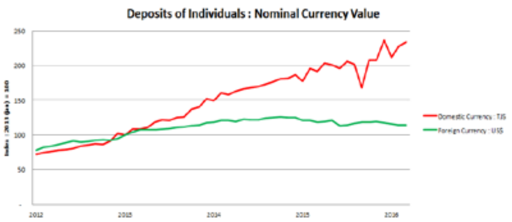
[19] Source: National Bank. Available data identifies separately the deposit holdings of individuals



This suggests that, despite the erosive effects of inflation upon purchasing capacity, individuals sought to maintain / increase their cash liquid assets levels. This may reflect (although it is an inference by the writer) that the financial profile of individuals may have become increasingly polarised towards the extremes of [i] increasing cash holdings to meet the uncertainties of the economy, inflation and the needs of the household and dependent of the individual, and [ii] increasing dependency upon borrowing which may reflect an [increasing] inability to repay indebtedness.

The growth of TJS Somoni domestic deposits is further illustrated in the following graphs (which show foreign currency deposits in the nominal US$ value, rather than the TJS equivalent).

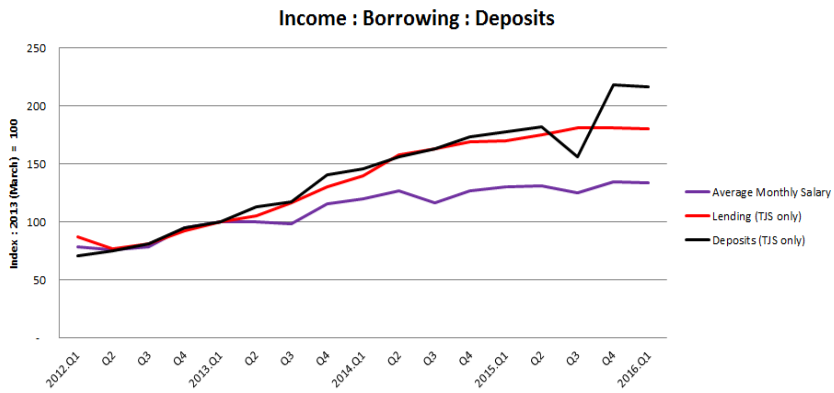




Note: As with the comment on foreign currency lending, the writer is unaware of any action by the National Bank to restrict the use / availability of foreign currency deposits by individuals during the recent years of severe economic pressure

Financial Behaviour of Individuals

The above sections have reviewed the separate dimensions and trends of income, borrowing and deposits. These are summarised in the following chart which shows the comparative trends of each of these components, indexed to 2013.Q1.



This chart shows the following principal characteristics:

- Income levels increasing at a lower rate than either borrowings or deposits (domestic currency only);
- Borrowing and deposit increases at similar rates until mid-2015, after which there was a strong surge in deposits.

This chart may suggest the following possible implications:

- The lower increase in salary levels than outstanding borrowings may reflect one or more of the following:
    - Greater pressure upon the borrower to maintain repayments – which is reflected also in the significant increases in the levels of 'past due' arrears
    - Changein credit affordability criteria by lending institutions;
    - Potential higher levels of loan rescheduling / refinancing – which may be greatest in relation to the substantive changes in foreign currency borrowings (not reflected in the above chart – see earlier comments).

Survey Observation: Borrowers show a significant deterioration in loan repayment capacity and their recognition of financial pressures. The lending institutions achieved an upward shift in the distribution of incomes of borrowers. The survey responses appear, therefore, consistent with these national statistics.

- The sustained increase in domestic currency deposits:
    - Despite the erosive effects of inflation, a significant segment of individuals demonstrate a strong commitment to maintain liquid cash savings;
    - The average amount of individual savings is likely to be much lower than the average outstanding loan balance. This would suggest that there are more 'savers' than 'borrowers' in the segment of society which has the financial capacity to access the financial institutions. (There will, of course, be a substantial number of people with insufficient financial capacity to undertake either financial service – the WBG reports indicate a poverty level of 32% [late-2015] with a monthly per capita income less than TJS 158.71 (US$22-24). The income level at which individuals enter the financial services market is likely to be much higher than this threshold figure).

Attachment 5.1.

Governance

External

1. Are meetings undertaken by the lending institution with:	Yes	No	Regular formal meetings				Occasional
			Annual	Half-Year	Quarterly	Monthly	
Central Bank							
Ministry of Finance							
Regulatory Authorities							
2. Are the following issues reviewed at these meetings							
Influences upon the risk profile of the institution							
Social impact of lending							
3. Is there a national, or regional, Association of lending institutions	Yes	No	If so, what is the membership				
If there is a national, or regional, Association:							
4. Is the lendinginstitution a member, and what is the frequency of meetings							
5. Does the Association represent its member institutions on (multi-institutional) industry issues at meetings with:							
Central Bank							
Ministry of Finance							
Regulatory Authorities							
6. Does the Association review:							
Aggregate risk performance measures and trends for the industry							
Impact of lending practices or debt levels upon clients							

Governance

1. Does the Board of the lending institution have	Yes	No	Regular formal meetings				Occasional
			Annual	Half-Year	Quarterly	Monthly	
Committee, or group of directors, with particular responsibility for the risk management profile and performance of the institution							
Committee, or group of directors, with particular responsibility for the social impact of lending and the protection of client interests							

2. Does the lending institution have policies to establish and define its responsibilities as a lender in relation to:			
The affordability of debt, or debt exposure, of borrowers			
The management of problem lending situations			
The social impact of lending policy and practice			
The financial education of its clients			

3. Are reports provided to the Board or Executive Management for the profile and performance of different client segments in relation to:			
Product			Please describe
Arrears and/or PAR (Portfolio at Risk)			
Client Income			
Social impact of lending			
Level of poverty within the client base			
Other			Please specify

4. Have threshold / 'cap' limits been established to determine maximum exposure to any client segment portfolios			
Product			Please describe
Arrears and/or PAR (Portfolio at Risk)			
Client Income			
Level of poverty			
Other			Please specify

5. Have 'standards', or norms, been established for acceptable levels of loan exposure as a multiple of net disposable income prior to loan repayments, in relation to:			
Product			
Client Income Segments			

6. Is responsibility for the risk management of the lending institution differentiated from that of credit management within the Executive Management responsibilities			
			If yes, how is this structured
7. Does the institution monitor or, by some means, assess:			
i. the profile and trends of the financial capacity of borrowers to meet debt commitments			And if so, by what methodology
ii. the attitude / commitment of clients to meet their debt repayment obligations:			And if so, by what methodology

Attachment 5.2.

Rationale for Proposed Reporting Requirements

The following notes provide a brief rationale for the proposed additional reporting requirements. These reflect the dimensions of structural risk management, but do not seek to provide an exhaustive assessment of their potential contribution to an assessment of the respective microfinance institution or national industry.

External

1. Are meetings undertaken by the lending institution with Central Bank, Ministry of Finance, or Regulatory Authorities?
    a. Recent events in various locations have emphasised the need for a constructive relationship between the government / public sector and the microfinance industry;
    b. This can provide the lending institution with the opportunity to clarify its objectives, strategy, and operational issues with the public sector authorities;
    c. The authorities may have different financial and social objectives from those of the lending institutions. It may be beneficial, therefore, to identify any issues of mutual alignment or potential conflict;
    d. The role of lending by both microfinance institutions and banks in the economies of local communities can be identified;
    e. This can provide an opportunity for a periodic up-date of market trends and client issues.

2. Are the following issues reviewed at these meetings: [a] influences upon the risk profile of the institution and [b] social impact of microfinance?
    a. These issues impact directly upon a segment of society which must depend heavily upon the integrity and responsibility of the lending institutions (not all of which are subject to direct regulation or review/control by government or public sector authorities);
    b. The social impact of debt can have a significant impact upon popular opinion. It is appropriate, therefore, to optimise the mutual understanding of the various trends and impacts. (This may, therefore, have direct implications for the level of political interest).

3. Is there a national, or regional, Association of lending institutions (MFIs and banks)?
    a. This provides an opportunity for the establishment of operating standards and practices;
    b. Aggregate statistics can be collated of industry trends;
    c. The opportunity for the establishment of initiatives which are of collective benefit to the participating institutions;
    d. Without an umbrella organisation, microfinance institutions must operate with imperfect information of market conditions.

4. Is the lending institution a member [of the Association], and what is the frequency of meetings

   a. The Association needs widespread membership to be an effective collective voice;
   b. The frequency of meetings must be appropriate to be responsive to developing issues.

5. Does the Association represent its member institutions on industry issues at meetings with [a] Central Bank, [b] Ministry of Finance, [c] Regulatory Authorities?
   a. How do lending institutions present a coordinated position of issues which have broad commercial and market implications;
   b. How is the aggregate effect of lending activity, and the respective roles of MFIs and banks, assessed and evaluated.

6. Does the Association review: [a] aggregate risk performance measures and trends for the industry, [b] impact of lending practices or debt levels upon clients.
   a. Without such a central body, the individual institutions will not have any current and coordinated market information.
   b. There will be different policies and strategies towards social responsibility by lending institutions.
   c. Social reaction to lending institutions can be affected by a range of factors (such as external factors).

Governance

1. Does the Board of the lending institution have [a] focused risk management responsibilities, and [b] focused client impact and protection responsibilities?
   a. How are the strategic issues of the client and risk exposure assessed by the Board. These represent the two primary activities of the lending institution and are integral to the development of lending institutions;
   b. If there is no formal segmentation of these particular responsibilities, how does the Board allocate agenda time to assess the strategy and performance of the institution;
   c. What skills and experience is held in the Board membership to address and review these issues

2. Does the lending institution have policies to establish and define its responsibilities as a lender in relation to [a] the affordability of debt, or debt exposure, of borrowers, [b] the management of problem lending situations, [c] the social impact of lending, and [d] the financial education of its clients?
   a. The implications of ‘lending responsibility’ become more acute in relation to a microfinance client base which has a limited experience of financial management;
   b. The wider encouragement of financial inclusion of the ‘marginal poor’ has implications for the treatment of such clients who have repayment difficulties;
   c. The social implications of over-indebtedness can be significant. These can impact upon not only the client, but also the reputation of the institution.

3. Are reports provided to the Board or Executive Management for the profile and performance of different client segments in relation to [a] product, [b] arrears/PAR, [c] client income, [d] social impact, [e] level of poverty, or other segments?
    a. The 'poor' is not an homogenous group and it is important to identify the principal market segments which are being served, and the differentiated performances;
    b. Segmentation should be aligned to both the core objectives of the institution and also the target client groups.
4. Have threshold / 'cap' limits been established to determine maximum exposure to any client segment portfolios in relation to [a] product, [b] arrears/PAR, [c] client income, [d] level of poverty, or other segments?
    a. Portfolio concentrations can impact the risk profile of the institution, with implications for greater volatility and sensitivity to particular market and environment changes;
    b. Threshold limits provide a strategic framework for the development of the business;
    c. Such 'cap' limits also stimulate particular consideration and comparison of the performance and dynamics of different client segments.
5. Have 'standards', or norms, been established for acceptable levels of loan exposure as a multiple of net disposable income prior to loan repayments in relation to [a] product and [b] client income?
    a. Client income can vary significantly within a single loan product;
    b. Over-indebtedness can arise if there is inadequate differentiation of client income;
    c. Some microfinance loan products incorporate an 'automatic' increased loan option at renewal – how is this validated for affordability.
6. Is responsibility for risk management of the institution differentiated from that of credit management within the Executive Management responsibilities?
    a. Risk management has a much wider span than operational credit risk management;
    b. Structural risk management requires different reporting and control processes;
    c. Board and management must consider potential pressures and risks in relation to systemic risk.
7. Does the institution [a] monitor or, by some means, assess the profile and trends of the financial capacity and attitude / commitment of clients to meet their debt repayment obligations; and if so, [b] how is such information obtained and assessment undertaken?
    a. Over-indebtedness is not simply a formulaic approach towards disposable income and repayment levels;
    b. Individuals have different tolerances, or risk appetites, to affect the extent to which they feel vulnerable to their debt obligations, or sensitive to changes in their lifestyle (such as insecurity of work employment for their spouse);
    c. A risk matrix approach enables a quantitative approach of affordability to be related to a qualitative approach of the client's behavioural and attitudinal profile.

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