Research on the Level of Indebtedness and Repayment Performance of Individual Borrowers in Kyrgyzstan

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Content

Acronyms

AMFI – Association of Microfinance Institutions

CEO – Chief Executive Officer

CIB – Credit Information Bureau

CU – credit union

EBRD – European Bank for Reconstruction and Development

ECA – Europe and Central Asia

ED – Executive Director

EFSE – European Fund for Southeast Europe

FD – Financial Director

CGAP – Consultative Group to Assist the Poor

GNI – Gross National Income

ICCO – Inter Church Organization for Development Cooperation

KGS – Kyrgyzstani som

MCC – microcredit company

MFC – Microfinance Centre

MFI – microfinance institution

MSFP – micro and small finance program

NBKR – National Bank of Kyrgyzstan Republic

USD – United States dollar

1. Introduction

The problem of over-indebtedness has been fervently discussed in the microfinance community in Kyrgyzstan because of the increasing numbers of loans and the amounts taken by borrowers.

Over-indebtedness occurs when borrowers owe so much that their loans have made them worse off than they would have been without the loans. It can be detrimental due to the material, psychological and social consequences.

However, there is no single indicator which could easily identify those with excessive debt. The response to the question 'how much is too much' is not an easy one. The indebtedness index measuring relative amount of debt can be calculated through the ratio of the amount spent on debt repayment to the disposable income but there is no common agreement on the threshold above which the debt load is too high.

The other measures for over-indebtedness are subjective indicators of difficulties in meeting debt obligations. These include the perception of debt burden or unduly sacrifices a borrower has to make in order to repay a loan.

In either case, measuring the indebtedness level of borrowers requires detailed primary research among borrowers.

The present study is the first attempt to understand the aspects of untimely repayments which are usually, although not always[1], a symptom of over-indebtedness. The study seeks to answer the question of the risk factors affecting timely repayments and generally understand the borrowing patterns in Kyrgyzstan.

The study was funded by ICCO within the three-year cooperation framework with MFC for Central Asia.

The research concentrates on the analysis of secondary data already available from the credit registry to understand the characteristics of credit use typical for clients with repayment problems. It further goes into the assessment of the perceptions of the risk of over-indebtedness voiced by the representatives of the largest microcredit providers.

The study does not attempt to assess the scope of over-indebtedness which would require conducting primary research among the borrowers to measure not only debt load relative to income, but also the perceptions of borrowers of their own financial situation.

The objectives of the present research are the following:

-   Measure the level of debt use in the population of Kyrgyzstan
-   Understand the patterns of credit use
-   Identify credit use characteristics and demographic features of borrowers with repayment problems
-   Identify factors considered by financial institutions to affect indebtedness level

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[1] The other reasons for late repayments are disconnected from over-indebtedness and may include short-term liquidity problems, general untimeliness, absence from the location, etc.

2. Methodology

The study was conducted in two phases:

- analysis of data on debt engagement of physical persons who are clients of the financial institutions reporting to credit bureau CIB "Ishenim"

The analysis was conducted on a sample of 2,603 active borrowers – private persons. The sample consisted of two sub-samples: (i) borrowers with all active loans repaid on time or with a delay not exceeding 30 days, (ii) borrowers with at least one loan overdue for more than 30 days.
Credit records of active and past loans were analysed.

- MFI interviews

Top management representatives (ED, CEO, or FD) of 7 institutions (Aiyl Bank, Bai Tushum, Elet-Capital, FINCA, Kompanion, Mol-Bulak and OXUS) were contacted with the request to respond to 35 questions about their perception of over-indebtedness, multiple borrowing (parallel loans) among their clients, lending procedures of their institutions as well as about the growth of microfinance sector and competition. The interviews were conducted face-to-face or via phone and each lasted for 1.5 hours.

3. Overview of the microfinance market

Microfinance in Kyrgyzstan is provided by a large number of institutions. In total, there is 397 microfinance institutions, 217 credit unions, one bank dedicated to serving small farmers and 6 commercial banks[2] with EBRD micro and small financing program (MSFP)[3].

The total value of microcredit portfolio reached over 20 billion KGS ($450 million) at the end of June 2011[4]. According to various sources, the number of active clients in November 2011 exceeded 400,000 active borrowers. AMFI statistics show that 426,673 clients were served by AMFI members, mainly MFIs, while CIB "Ishenim" records contain data of 416,000 clients with active loans from MFIs and banks.
This means that approximately 8% of the population uses credit. The penetration rate is low compared to the other countries in the ECA region which is understandable given country's low economic development[5,6].
The Figure 1 shows penetration rates of microcredit and credit from mainstream commercial banks in ECA at the end of 2009. Kyrgyzstan had the third lowest overall credit penetration but was among the first six countries (out of 19) with the highest microcredit penetration.

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[2] NBKR statistics and AMFI report „Research of Microfinance Sector in Kyrgyz Republic"
[3] EBRD MSFP discontinued new loan disbursements in 2011
[4] NBKR statistics
[5] Kyrgyzstan has the second (after Tajikistan) lowest GDP per capita in the ECA region (Source: World Bank Development Indicators http://data.worldbank.org/indicator/NY.GDP.PCAP.CD/countries
[6] Research findings of the World Bank team on Access to Finance identified the following factors associated with loan penetration: GDP per capita, population density, branch penetration, physical and financial infrastructure (Source: Financial Access 2010. The State of Financial Inclusion through the Crisis. CGAP/The World Bank Group 2010)

Although it is not possible to determine the degree of market saturation without knowing the scale of demand for microcredit, high penetration rate in Kyrgyzstan suggests that the outreach may not grow in the next years as easily as elsewhere.

Figure 1. Penetration rates of microcredit and credit from mainstream commercial banks among population in economically active age (15-65 years old) in 2009
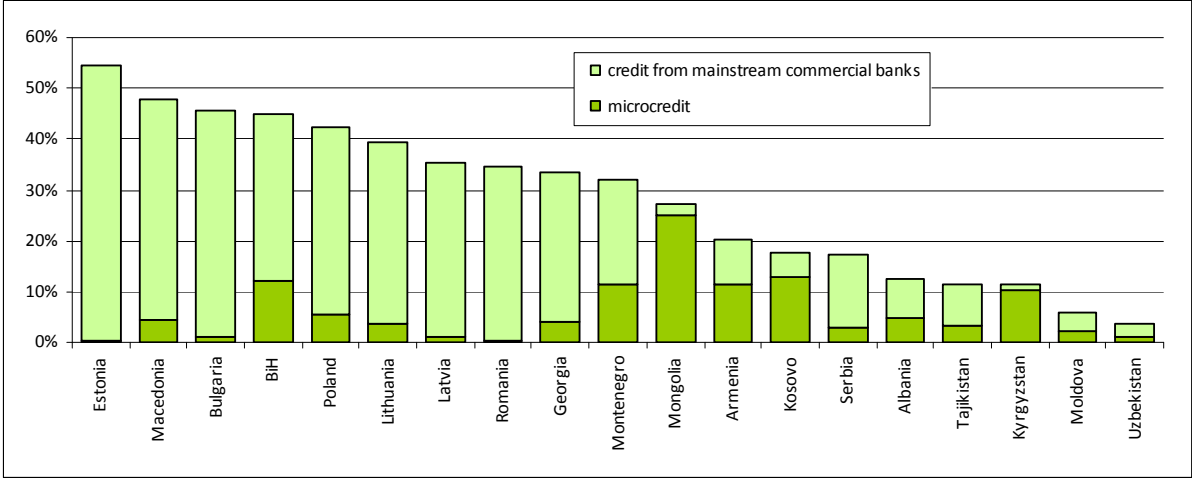
Source: 'Re-emerging from the Crisis – Microfinance in ECA. 2010 Edition', MFC 2010

Despite a large number of institutions the credit market in Kyrgyzstan is very concentrated – 84% of the clients are served by only 5 institutions: Aiyl Bank, Bai Tushum, FINCA, Kompanion and Mol Bulak which altogether manage 66 % of the loan portfolio.

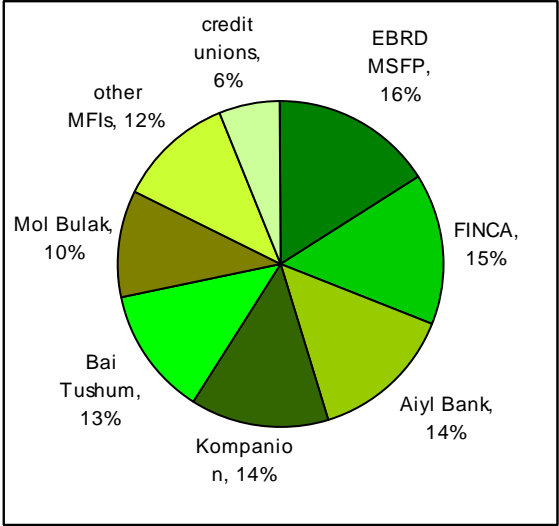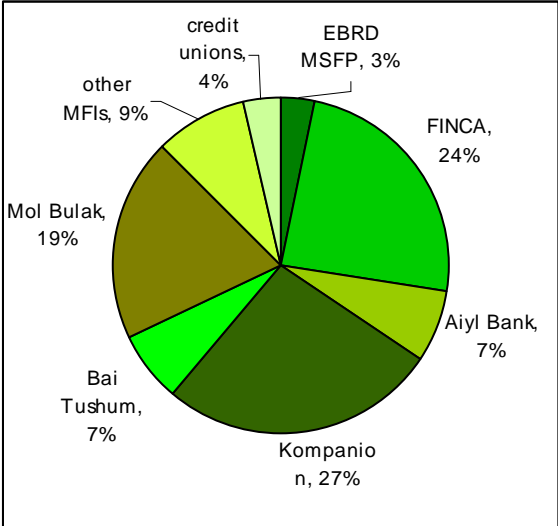Figure 2. Distribution of microcredit portfolio by institutions

Figure 3. Distribution of borrowers by institutions

Microfinance institutions – the main type of microcredit provider - have been increasing the outreach and the volume of loans over the years. The statistics of leading MFIs which report to the MIX Market show that after the peak year of the portfolio growth in

2007, the growth rates have been lower, especially during the crisis years of 2009 and 2010.[7] However, in the first 3 quarters of 2011 the loan portfolio has already increased by 46%.

The number of active borrowers also has been increasing over the years at the slowing rate. The borrowers growth was in some years higher than portfolio growth, indicating that the loan size was going down, however, in 2011 the average loan size significantly increased. The average loan size at the end of September 2011 was $647, 21% than in 2010.

Figure 4. Growth of the gross loan portfolio of MFIs reporting to the MIXMarket
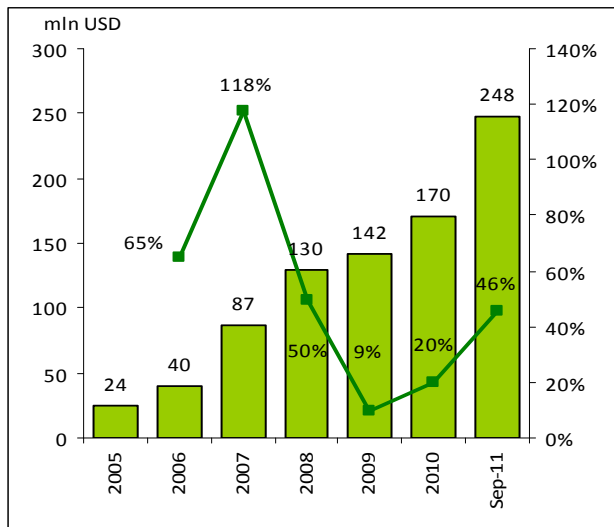
Figure 5. Growth of the number of active borrowers of MFIs reporting to the MIXMarket
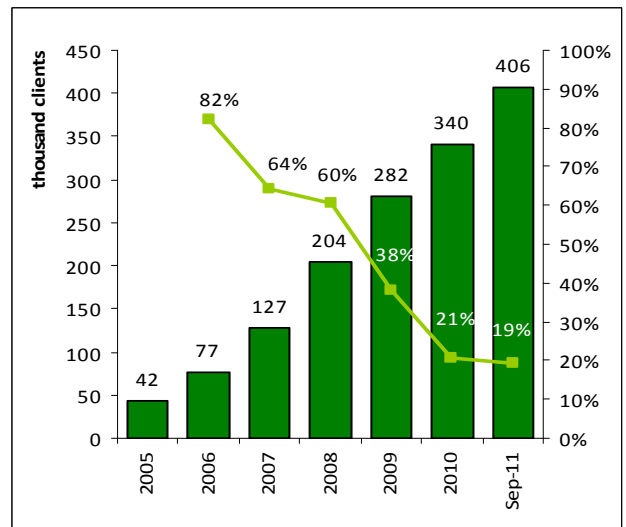
Microfinance institutions reporting to the MIX Market: AgroKredit Plus, Bai Tushum, Bereke-Credit, Credit Systems, Elet-Capital, FINCA, First MCC, Kompanion, Mol Bulak, OXUS
Source: MIXMarket www.mixmarket.org

The NBKR statistics show that the share of overdue loans of microfinance institutions has remained on a moderate level for the last 3 years, with a slightly downward tendency in 2011.

Figure 6. Share of overdue loans in the loan portfolio of microfinance institutions

Figure 7. Portfolio at risk over 30 days (PAR>30) of four largest MFIs

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[7] The growth rate of the loan portfolio was calculated from data recalculated to USD

The important role of the facilitator of the credit market in Kyrgyzstan is played by the credit bureau CIB "Ishenim" established in 2003.

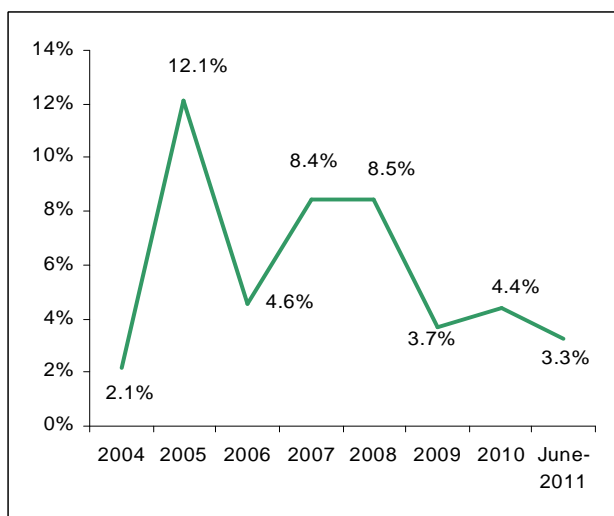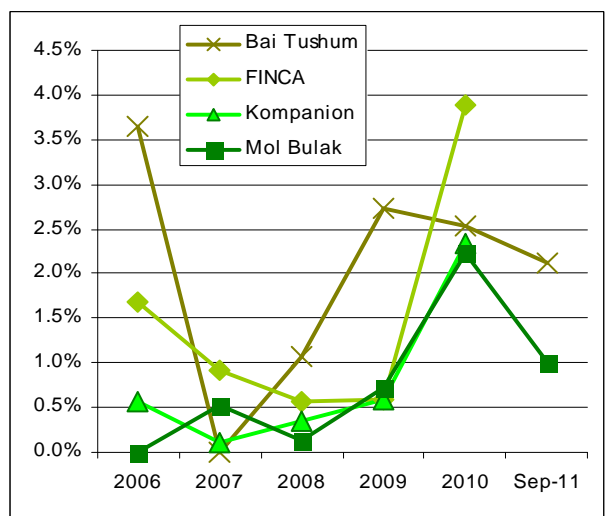Well functioning credit bureau is one of the factors preventing over-indebtedness[8] as well as the factor improving access to finance[9].

At the time of the study 47 largest institutions (banks, MFIs, credit unions) participated in the exchange of client data by providing information on credit disbursements and the timeliness of repayments. CIB "Ishenim" continues to expand its membership base by attracting not only credit institutions but also service providers such as telecom companies.

4. Main findings from the analysis of CIB "Ishenim" data

4.1. Indebtedness level

4.1.1. Penetration with credit - number of borrowers

According to the results of the analysis conducted on the sample selected for the study the clients were concentrated in three locations. The largest group of clients was located in the capital city of Bishkek (23% of active borrowers), Jalalabad (18%) and Issyk-kul (12%) oblasts.

But the penetration rate – percentage of the population with credit - was the highest in Talas oblast (15% of inhabitants being active borrowers) and Osh city (12%), followed by Bishkek and Issyk-kul oblast.

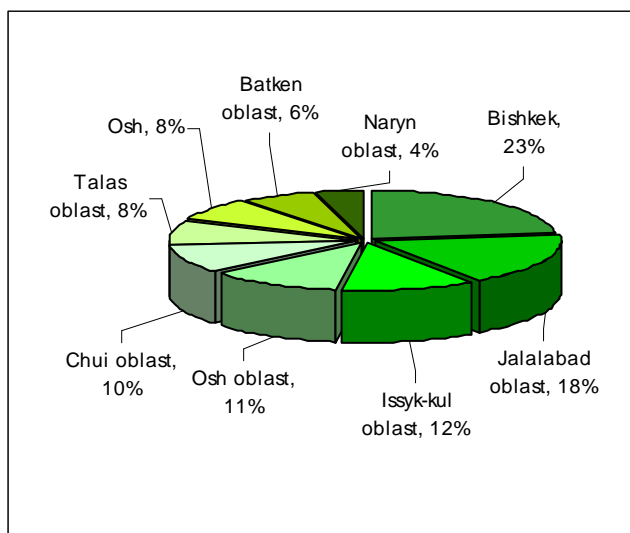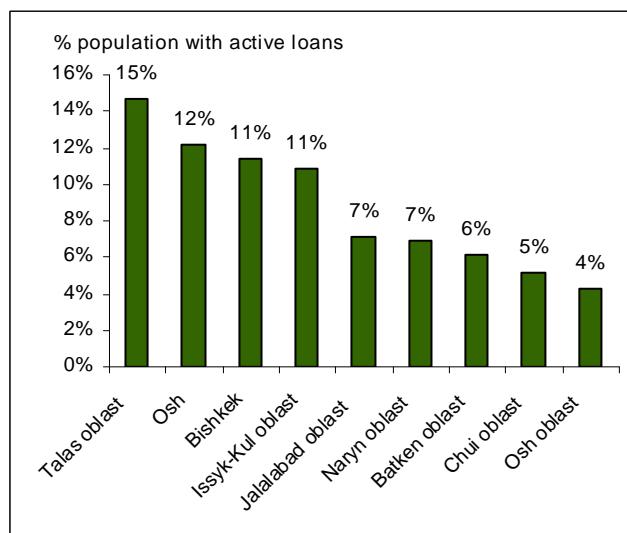Figure 8. Regional distribution of active borrowers

Figure 9. Share of population with active loans by region

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[8] 'Microfinance and Over-indebtedness: Understanding its drivers and challenging common myths', Schicks J. CED Working Paper No. 10/048, 2010
[9] 'Financial Access 2010. The State of Financial Inclusion Through the Crisis', CGAP/The World Bank Group 2010

4.1.2. Number of active loans per borrower

Despite worries about the increasing scale of multiple borrowing, the results show that parallel loans are not so frequent – only 31% of clients had more than one active loan. On average, one borrower was repaying 1.46 active loans and having more than 3 loans was very rare.

Figure 10. Average number of active loans per borrower
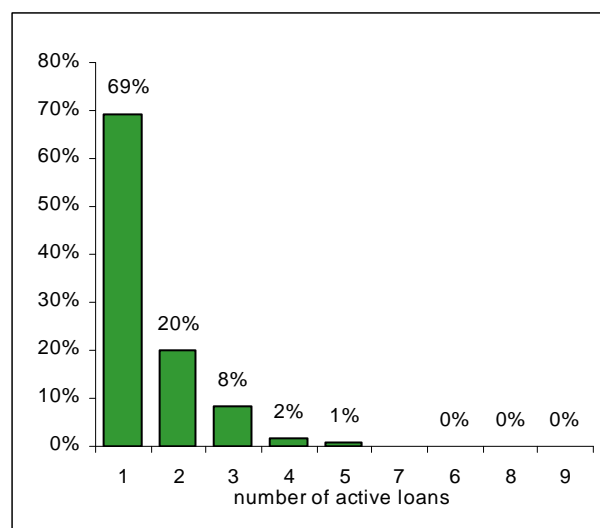
Figure 11. Average number of active loans per borrower by region

Location	Percent clients with multiple loans	Avg. number of active loans
Talas oblast	41%	1.59
Issyk-kul oblast	35%	1.55
Jalalabad oblast	30%	1.47
Osh	23%	1.32
Naryn oblast	23%	1.40
Osh oblast	22%	1.34
Bishkek	20%	1.28
Batken oblast	18%	1.30
Chui oblast	17%	1.25
Total	**31%**	**1.46**

Regional differences were seen – clients of Talas and Issyk-kul oblasts more often than in the other locations had over one loan and also had the largest number of loans per borrower. 41% of the borrowers in Talas oblast and 35% in Issyk-kul oblast had parallel loans. The lowest number of loans per person was in Chui oblast.

Higher incidence of multiple borrowing was seen in the regions with higher credit penetration. This indicates that taking several loans happens in the regions with are closer to saturation, where over-supply of credit may be seen.

Figure 12. Correlation between penetration rate in the regions and incidence of multiple borrowing
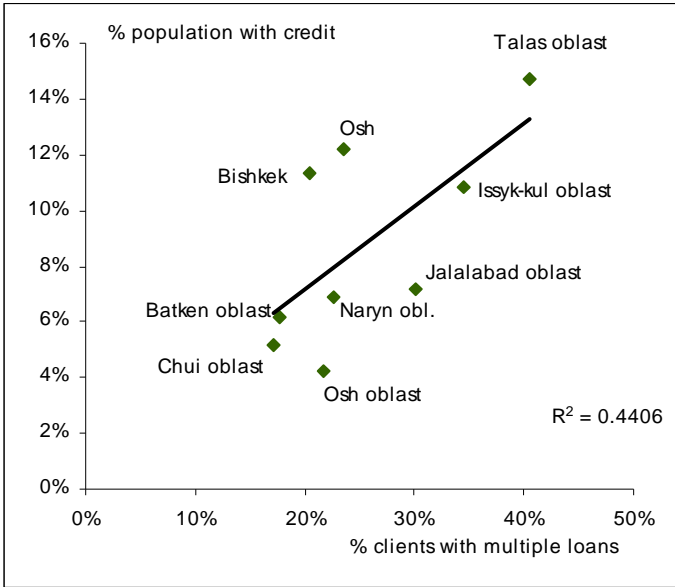
Women more often were engaged in parallel loans as 36% of them had more than one loan, while among men only 18% repaid multiple loans. On average, a woman had 1.55 active loans and a man - 1.25.

People with credit history more often had parallel loans which is understandable because of their experience in managing credit.

When compared to the other two countries in the ECA region, multiple borrowing in Kyrgyzstan is not as widespread as in Bosnia-Herzegovina but more common than in Kosovo.

Figure 13. Multiple borrowing in ECA countries

	% borrowers with multiple loans	Avg. number of loans per borrower
BiH	58%	2.30
Kyrgyzstan	**31%**	**1.46**
Kosovo	25%	1.37

Source: "Indebtedness of Microcredit Clients in Bosnia and Herzegovina", EFSE, 2009, "Indebtedness of Microcredit Clients in Kosovo", EFSE and MFC, 2011

4.1.3. Total value of loans per client

The average active client took loans of the total value of 201,300 KGS ($4,425) at disbursement.
The highest value of loans was seen in Bishkek ($5,200) and the lowest in Batken oblast ($2,900).

Figure 14. Average disbursement value of active loans per borrower by region

	Average disbursement value of active loans per borrower (expressed in KGS)	Average disbursement value of active loans per borrower (expressed in USD)
Bishkek	233,091	5,188
Jalalabad oblast	214,510	4,681
Osh	207,479	4,614
Issyk-kul oblast	188,225	4,121
Talas oblast	180,934	3,926
Chui oblast	176,209	3,866
Naryn oblast	158,898	3,486
Osh oblast	152,754	3,352
Batken oblast	134,229	2,944
Total	**201,269**	**4,425**

Clients with parallel loans took larger amount of debt – they on average repaid loans of the total value of 350,000 KGS ($7,680) at disbursement, while clients with only one loan took loans in the amount of 135,000 KGS ($2,300).

Unfortunately, the outstanding amounts were not available for all clients[10], so it was not possible to calculate the current debt load. But the comparative analysis for several countries in the ECA region allowed for assessing credit amounts in Kyrgyzstan.

Although borrowers in Kyrgyzstan took smaller loans than clients in Bosnia-Herzegovina and Kosovo in absolute values, when compared to the level of income in the country then their loans exceeded over 3 times the GNI per capita and were the highest among the three countries. The comparison of a loan size with the average salary places Kyrgyzstan in the middle between Bosnia-Herzegovina and Kosovo with the average debt load equal 1.6 the average annual salary in Kyrgyzstan.
This indicates that clients in Kyrgyzstan had relatively larger amount of credit than in Bosnia-Herzegovina and in some dimensions also higher than in Kosovo.

Figure 15. Average loan size at disbursement in selected ECA countries

	Average value of loans per borrower at disbursement (USD)	Average value of loans per borrower relative to GNI per capita	Average value of loans per borrower relative to average annual salary
Bosnia-Herzegovina[11]	7716	1.64	0.78
Kosovo[12]	8,105	2.61	2.05
Kyrgyzstan	**4,425**	**3.41**	**1.61**

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[10] Credit bureau requires from financial institutions to report the outstanding loan amount (principal and interest) only when the loan becomes overdue
[11] Own calculations based on the report 'Indebtedness of Microcredit Clients In Bosnia and Herzegovina', EFSE, 2009
[12] Own calculations based on the report 'Indebtedness of Microcredit Clients In Kosovo', EFSE and MFC, 2011

4.1.4. Loan size

The size of the average active loan was 138,000 KGS ($3,030) at disbursement with the median of $2,203, indicating that half of the loans were smaller than $2,000. But the use of very small loans (below $500) was quite limited with only 7.7% of active loans below $500.

Figure 16. Distribution of active loans by size and region
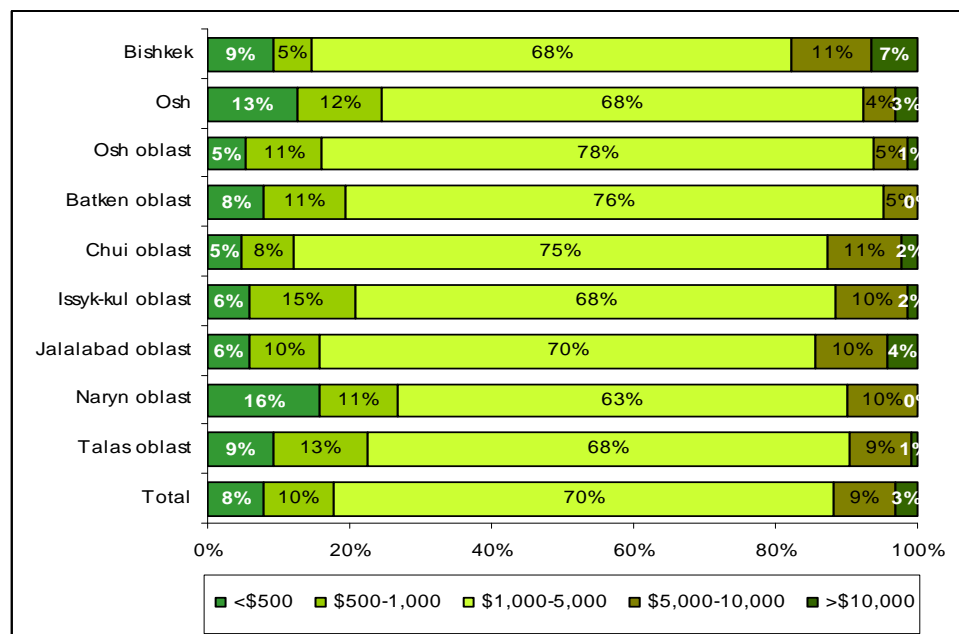
The largest share of the smallest loans (up to $500) was seen in Naryn oblast and Osh city. The largest loans over $10,000 were most often disbursed in Bishkek.

Figure 17. Average loan size at disbursement

	past loans (expressed in KGS)	active loans (expressed in KGS)	past loans (expressed in USD)	active loans (expressed in USD)	% change in USD value
bank	102,332	188,790	2,539	4,165	64%
MFI	92,328	122,769	2,089	2,695	29%
CU	47,984	89,777	1,182	1,961	66%
Total	**94,181**	**137,890**	**2,176**	**3,032**	**39%**

As it is seen on Figure 17, banks generally provided larger loans (on average $4,200 at disbursement) than MFIs ($2,700).

Such high size of MFI loans is surprising knowing that microfinance institutions predominantly disburse loans smaller than $1,000.

AMFI member statistics (microfinance institutions and credit unions) show that the average loan size at the disbursement has been 38,952 KGS ($832) since the beginning of the year. Information from the web-sites of the largest MFIs reveals that Kompanion's group loans which are used by 99.9% of their clients are up to $1,000 and FINCA's group loans which constitute 60% of their portfolio are up to $2,170.

This suggests that a significant share of microloans may not be reported to the credit bureau.

The disbursed amounts increase over time – the value of past loans was on average 94,000 KGS ($2,200) and the increase was more dynamic in the banks. While MFIs only increased the value by less than 30%, the bank loans increased by over 60%.
This indicates that clients graduate to larger loans faster in banks than in MFIs.

4.2. Other characteristics of loan use

4.2.1. Demographic characteristics of borrowers

Gender: women constituted 69% of the clients and more often were clients of MFIs rather than banks.

Age: credit clients were most often up to 50 years old, with the average borrower of 41 years. The youngest borrower was 18 years old and the oldest 78 years.

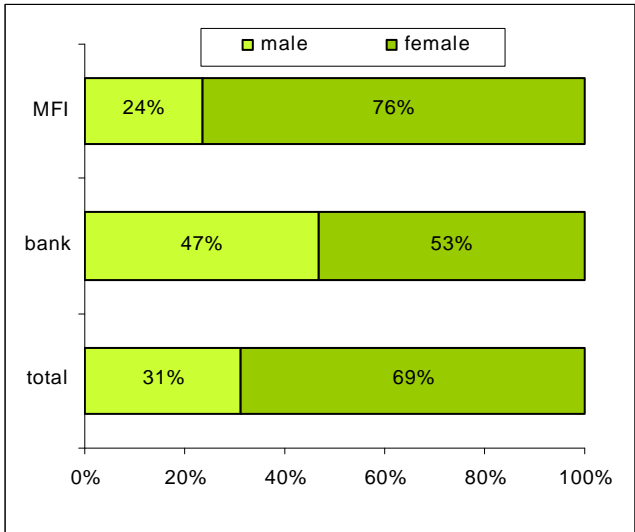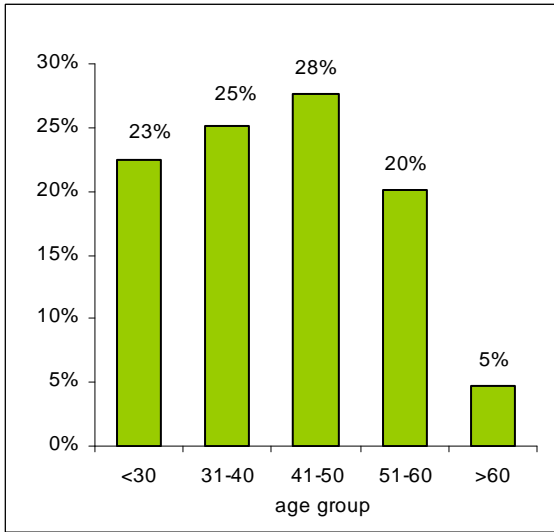Figure 18. Distribution of active borrowers by gender

Figure 19. Distribution of active borrowers by age group

4.2.2. Source

Microfinance institutions were the primary source of loans - 71% of active borrowers were clients of only MFIs and 19% were clients of only banks. However, 10% of the clients had at the same time active loans from both MFIs and banks. Loans from credit unions were marginal (0.6%) as only a few credit unions report to CIB "Ishenim".

When taking into account only clients with multiple loans, then 59% of them took loans only from MFIs but as many as 32% cross-borrowed from MFIs and banks (Figure 20). Cross-borrowing from two different types of institutions was associated with a higher number of loans. Clients who repaid loans to banks and MFIs has on average 2.71 active loans while clients with multiple loans from only MFIs had 2.39 and only banks 2.30 loans. Cross-

borrowing clients also took larger loans and were more experienced in credit use as they had more loans in the past.

Figure 20. Distribution of active borrowers with multiple loans by loan source
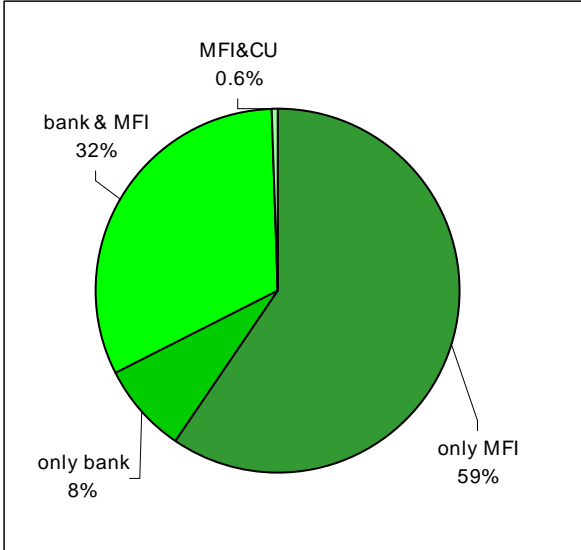
Figure 21. Average number of active loans per borrower among clients of banks, MFIs and both types of institutions
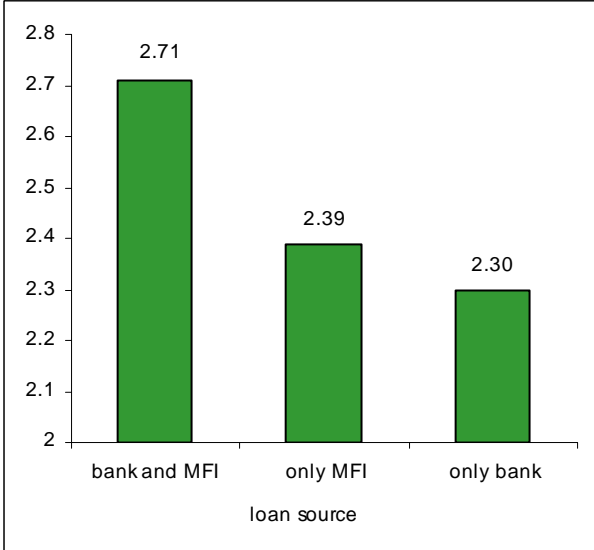
4.2.3. Loan type

Group loans are by far the most common type of loan presently repaid by active borrowers. The other types of credit are less often used – the percentage of clients with mortgage loans and credit cards is marginal.

Figure 22. Distribution of clients by loan type (% clients)
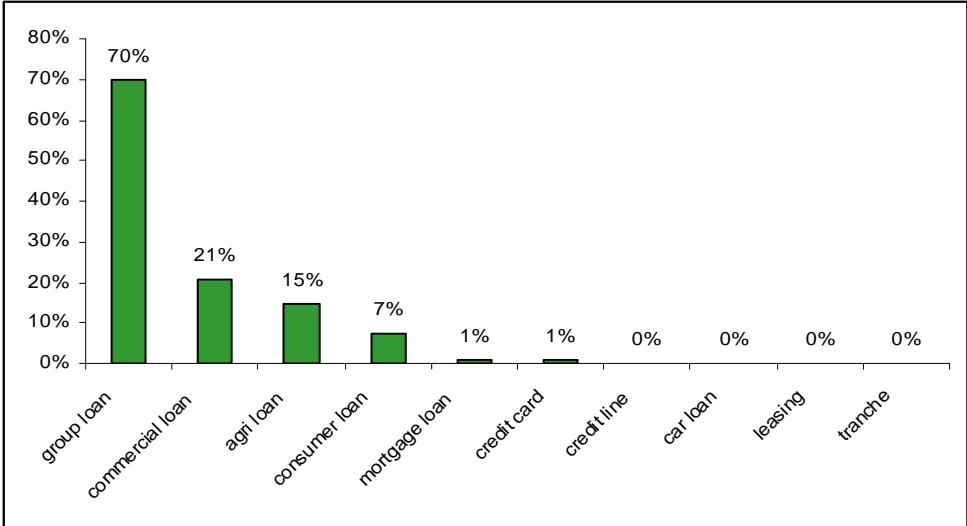
While group loans are a typical MFI product, the other two loan types – commercial loans and agricultural loans - are equally often disbursed by MFIs and banks. Consumer loans were more the domain of banks, as well as the other types of credit products, including credit card, credit line, leasing or mortgage loans (Figure 23).

As it can be seen on Figure 24, among the four most popular credit types agricultural and consumer loans are smaller, on average around $1,000 at disbursement, while group and commercial loans are twice as large (on average, over $2,000 at disbursement).

Figure 23. Source of active loans of the four most common loan types

Figure 24. Average loan size at disbursement

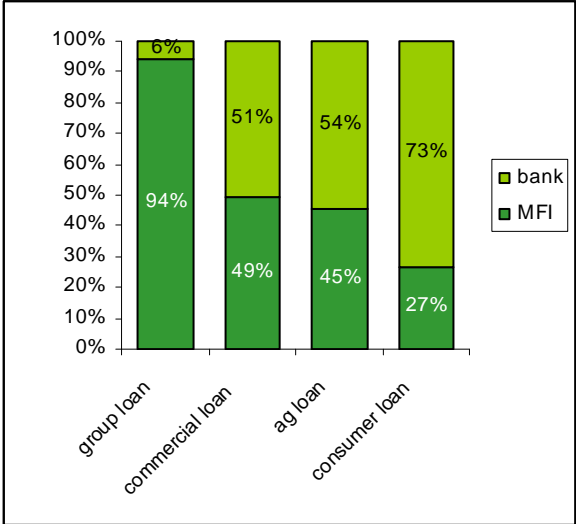|	Avg. disbursed amount (expressed in KGS)	Avg. disbursed amount (expressed in USD)
group loan	110,000	2,433
commercial loan	100,000	2,212
agri loan	47,670	1,053
consumer loan	50,000	1,098
mortgage loan	716,167	18,195
credit card	5,500	126
credit line	794,028	17,000
car loan	370,000	8,185
leasing	746,923	16,598
tranche	1,151,721	30,000

4.2.4. Currency

Local currency loans prevail. Only 3% of clients had active loans in foreign currencies, the vast majority in USD. Loans is foreign currencies were most often issued by banks – 8% of the loans from banks were denominated in USD while among the MFI loans this percentage was below 1.

Foreign currency loans have been less popular each year. While in 2007 the share of loans disbursed in USD was 17%, it dropped to 1% in 2011 disbursements.

However, it should be noted that some MFI loans are indexed to USD, so although they are disbursed in the local currency, the amount of repayment depends on the exchange rate of the local currency to USD.

Figure 25. Distribution of loan disbursements by currency
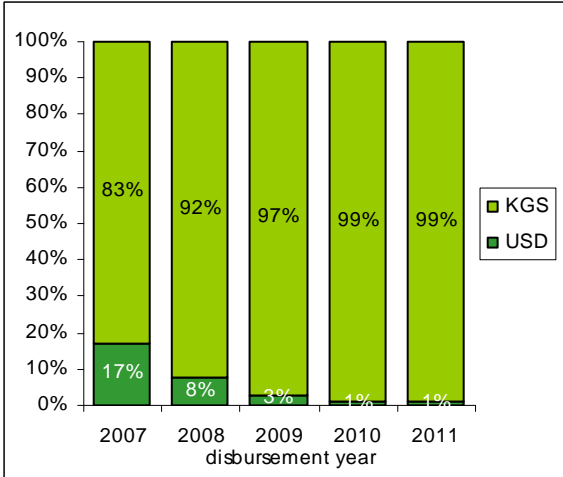
4.2.5. Duration

The average term of the active loan was 13.5 months, with bank loans having longer maturities, than MFI or credit union loans. Also, large loans over $10,000 had at least twice as long term as the small loans.

Over time, the average loan term had not changed – since 2007, the average duration of a loan was 11-13 months.

Figure 26. Average duration of active loans by source

Institution	Average loan term (in months)
bank	20.1
MFI	11.5
CU	9.7
Total	**13.5**

Figure 27. Average duration of active loans by loan size

Loan size	Average loan term (in months)
<$500	14.0
$500-1,000	12.3
$1,000-5,000	12.3
$5,000-10,000	16.2
$10,000-20,000	33.1
>$20,000	57.2

4.2.6. Disbursement date

Given the average loan term of about 1 year, 83% of active loans was originated in 2011.

Figure 28. Distribution of active loans by disbursement year
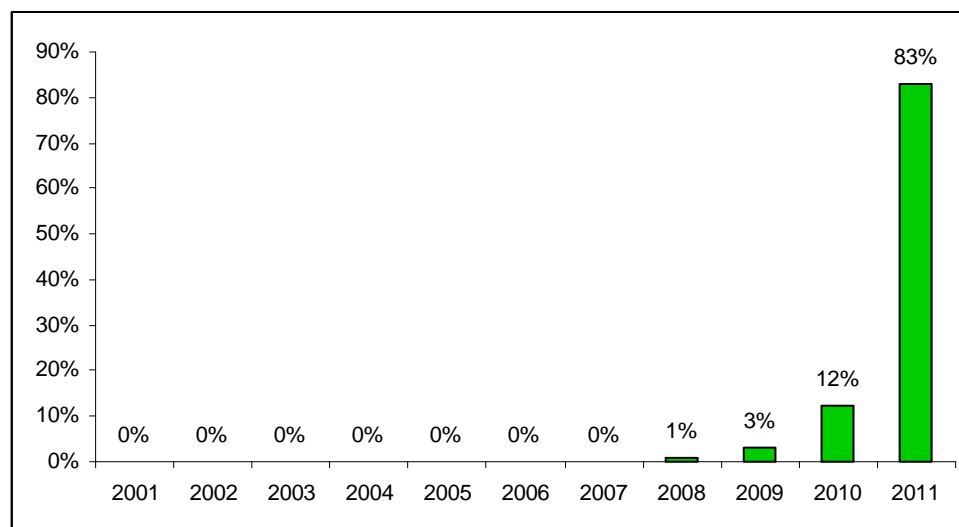
4.2.7. Credit history

57% of clients borrowed in the past and each of them, on average, had already repaid 3.1 loans. Clients with credit history were more often seen in such regions as Issyk-kul and Talas oblasts where 77% and 75% of clients, respectively, had loans in the past.

Figure 29. Distribution of active clients by number of past loans
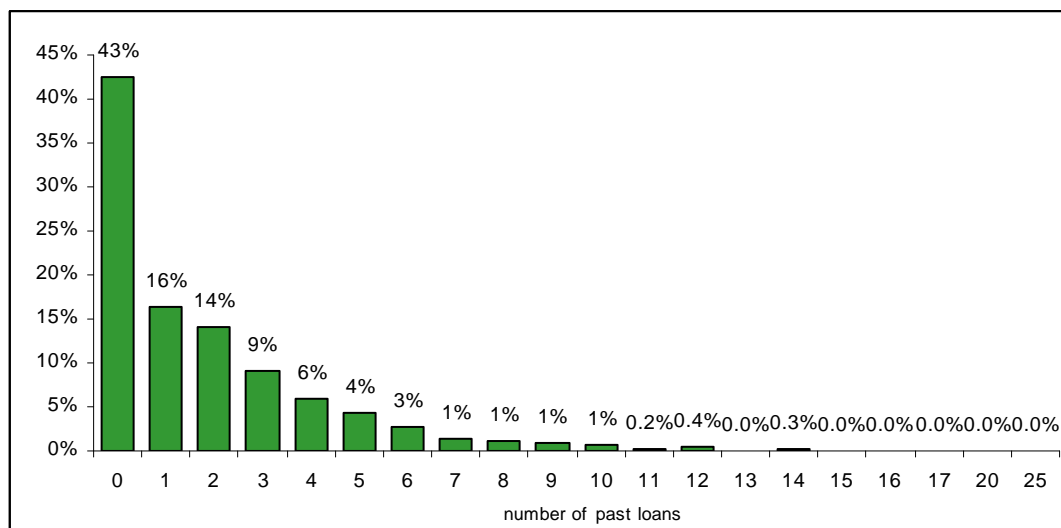
Past loans more often originated from MFIs than banks. Also, women more often than men borrowed in the past which shows that more men became new clients of institutions traditionally serving women.

Clients who at the same time had active loans from a bank and MFI more often had credit history (83% of them borrowed in the past). In their case the number of past loans was also higher and averaged 4.33.

4.2.8. Rejected loans

A small percentage of the current clients (9.2%) applied for a loan in the past but eventually it was not disbursed. Such loans were usually reported by banks.

In half of the cases (52%) the reason was the negative decision of the institution to not approve the application and in 36% of cases the client resigned from the loan. In the remaining 12% of cases it was not possible to contact the client (absence of connection).

4.2.9. Guarantees

The information about guarantees is often missing from the records of the credit bureau[13], however, among the clients about whom information was available the majority provided some kind of guarantee on their loans. Only 2% of clients had unsecured loans.

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[13] The information about guarantee status of 22% of clients was missing from credit bureau records

The most popular guarantee type was personal guarantee (90% of clients) – typical for group loans. Immovable property (house, flat or land) was put up as collateral by 8% of borrowers. MFIs more often relied on personal guarantees, while banks more often accepted hard collateral.

Figure 30. Share of clients with different types of guarantees (% borrowers)
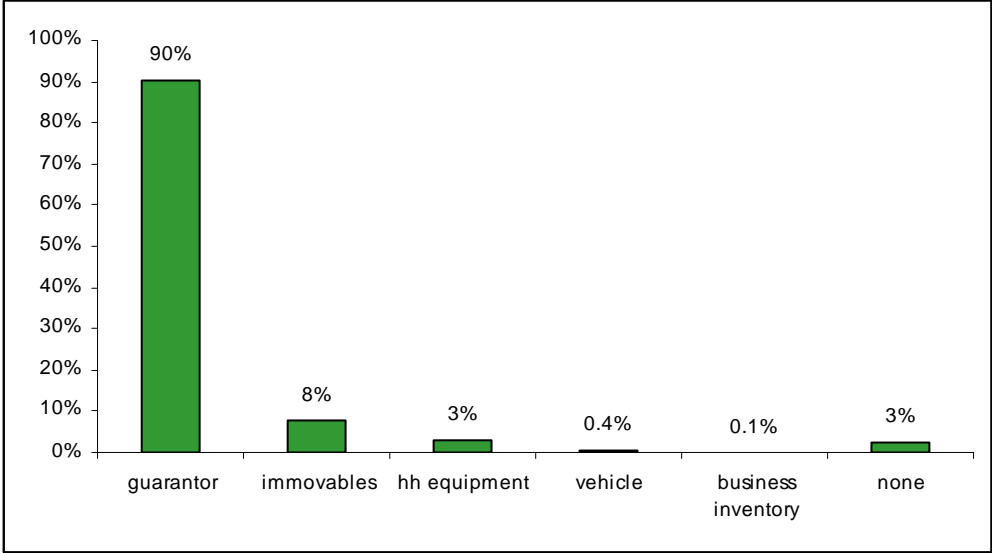
4.2.10.   Guarantors

8.4% of borrowers acted as guarantors at the time of repaying their own loans.
Guarantors are typically people who repay larger loans than non-guarantors, have a credit history, but not necessarily without any violations. 55% of guarantors had some kind of violation (mainly delays in repayment) on their loans in the past.

4.2.11.   Prolongations

Although less than 1% of clients had any prolongations reported, 59% of the clients had term prolongation dates reported in the database. This suggests that quite a significant number of people renegotiated the duration of their loans. In particular, borrowers with multiple (parallel) loans more often had loan term extended.

4.3. Repayment performance

Out of the total pool of active borrowers recorded in the credit bureau database 1.34% repay their loans with the delay of more than 30 days, and another 1.65% has only smaller delays of up to 30 days.

Figure 31. Distribution of clients by repayment status on active loans (% borrowers)
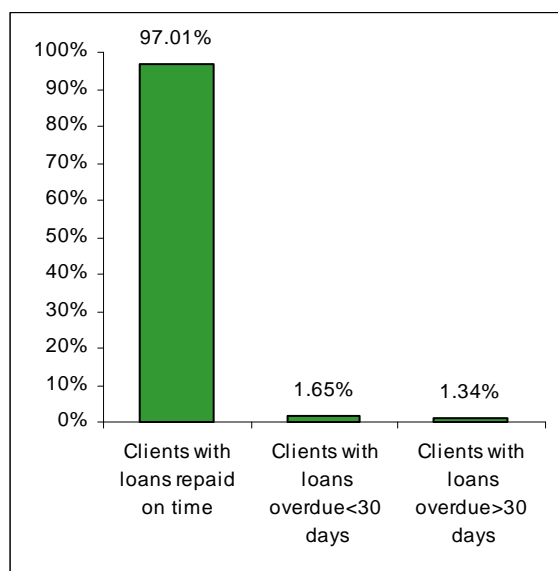
Figure 32. Share of clients with loans overdue for more than 30 days by region
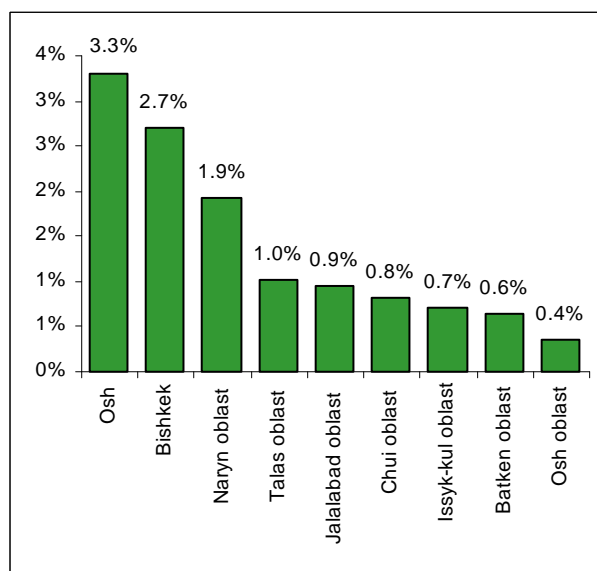
The largest percentage of clients with loans overdue for more than 30 days was seen in Osh city (3.3% of borrowers overdue >30 days), followed by Bishkek (2.7%).

In comparison with Bosnia-Herzegovina and Kosovo, the repayment timeliness of Kyrgyz borrowers is excellent.

Figure 33. Distribution of borrowers by timeliness of loan repayment

	Share of clients with loans on time or overdue <30 days	Share of clients with loans overdue >30 days
Bosnia-Herzegovina[14]	84.00%	16.00%
Kosovo[15]	91.60%	8.40%
Kyrgyzstan	**98.66%**	**1.34%**

The incidence of repayment problems was less correlated with the rate of penetration of credit in the population but more with the presence of many financial institutions. As it can be seen on Figure 34 in regions with a higher number of financial institutions per 100,000 citizens non-repayment for more than 30 days was more frequent than in the regions with lower concentration. This indicates that repayment defaults may result from competition between financial institutions.

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[14] Source: 'Indebtedness of Microcredit Clients In Bosnia and Herzegovina' EFSE, 2009
[15] Source: 'Indebtedness of Microcredit Clients In Kosovo', EFSE and MFC, 2011

Figure 34. Correlation between concentration financial institutions and repayment performance
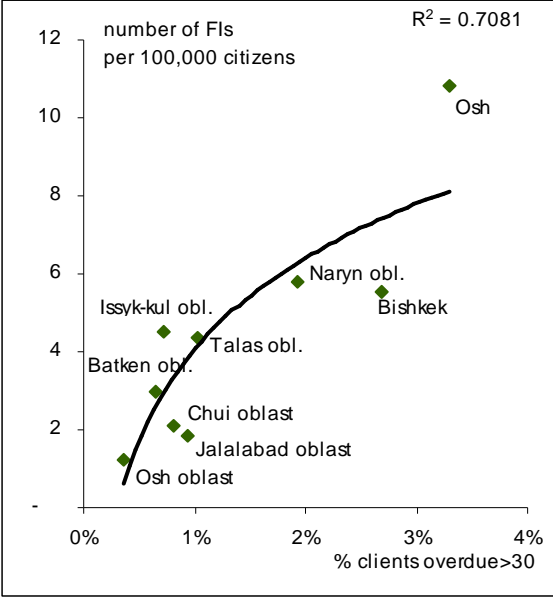
Figure 35. Correlation between credit penetration and repayment performance
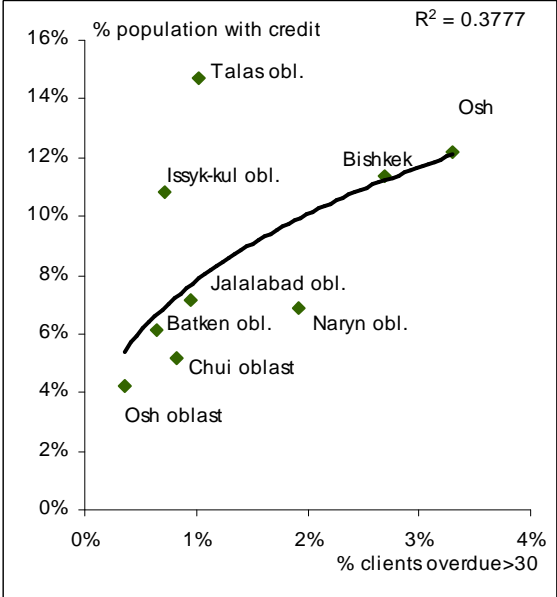
The analysis of past repayment performance revealed that 45% of clients with credit history had contract violations in the past. In most cases they violated the repayment schedule at some point of time during the loan term (41% of clients using loans in the past). This shows that even if almost all loans had been eventually repaid the problems with meeting the deadlines occurred among a considerable number of clients.

4.3.1. Characteristics of clients with overdue loans >30 days

Clients who at the time of the study had delays on loan repayment of more than one month were further analyzed to find out what factors may have contributed to such untimeliness.

4.3.1.1. Socio-demographic features

Age: the youngest and oldest clients were the most disciplined ones in the repayment. The percentage of those delayed over 30 days was below 1% in both groups. The ones most often overdue were middle-aged.

Figure 36. Share of clients with loans overdue for more than 30 days by age groups
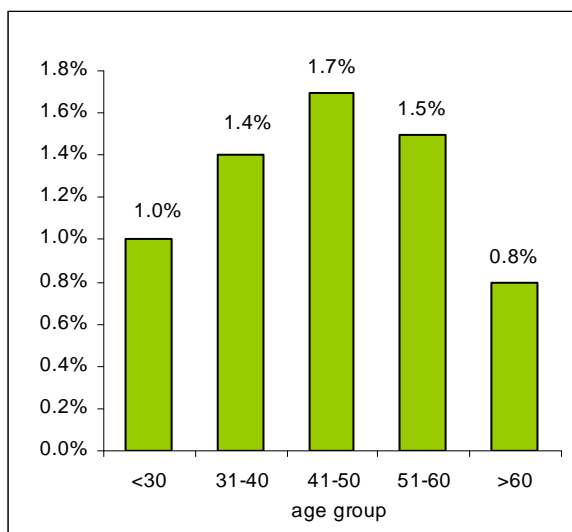
4.3.1.2. Number of active loans

Clients with at least one loan overdue for more than 30 days had on average 1.6 active loans compared to 1.5 active loans among the clients who repaid all loans on time or with a short delay of less than 1 month. Additionally, the distribution of overdue clients shows that more of them was in the category of 2+ active loans (Figure 38).

Figure 37. Average number of active loans by client group

Client group	Average number of active loans
Clients with all active loans repaid on time or overdue<30 days	1.45
Clients with at least one loan overdue >30 days	1.59

Figure 38. Distribution of active clients by number of loans and repayment status
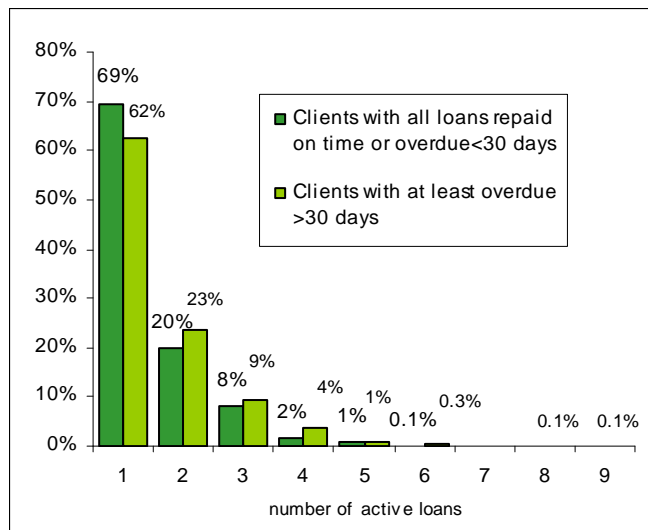
4.3.1.3. Loan size

The smallest and the largest loans were more often repaid with a delay of over 30 days. As Figure 39 shows loans of $500 or less as well as those over $10,000 far more often were repaid with a delay of over 30 days.

Figure 39. Share of loans overdue for more than 30 days by size group
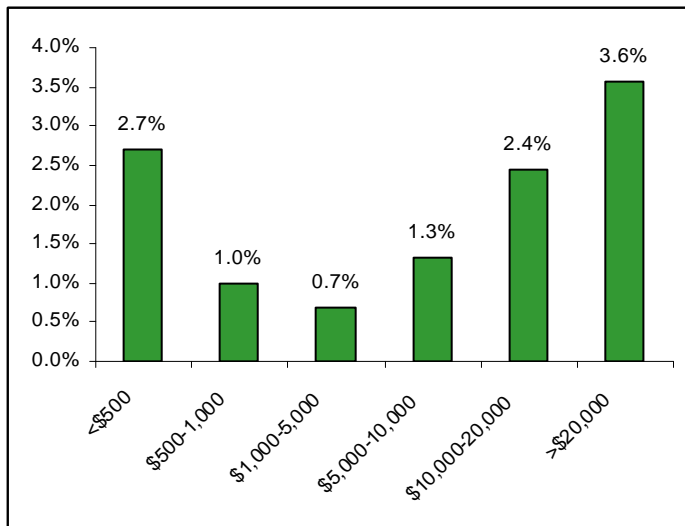
Figure 40. Share of clients with loans overdue for more than 30 days by loan type
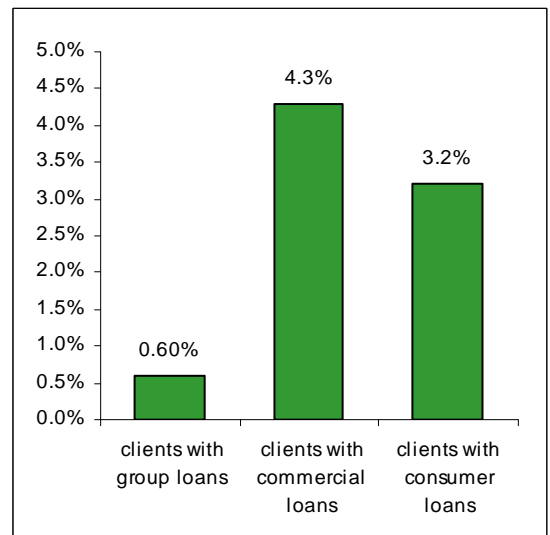
4.3.1.4. Loan type

Clients with group loans more often repaid timely while those with commercial and consumer loans were more often overdue for more than 30 days (Figure 40).

4.3.1.5. Currency

Clients with loans disbursed in USD repaid with longer delays. This finding cannot be explained by the changes in the exchange rates as in the period of 2010 and 2011 monthly exchange rate fluctuations did not exceed 3%.[16]

Figure 41. Share of clients with loans overdue for more than 30 days by currency
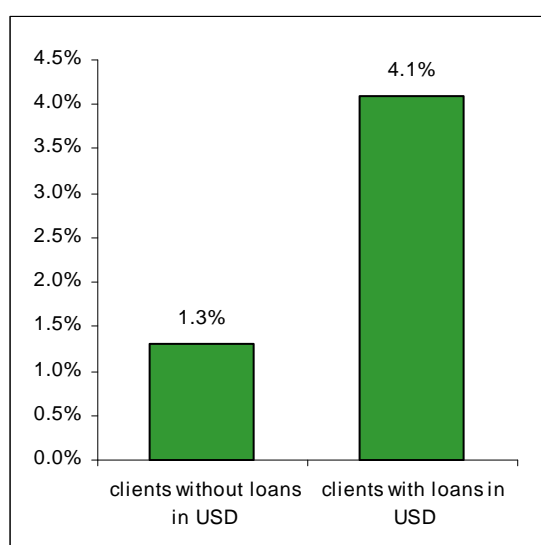
Figure 42. Share of clients with loans overdue for more than 30 days by prolongation status
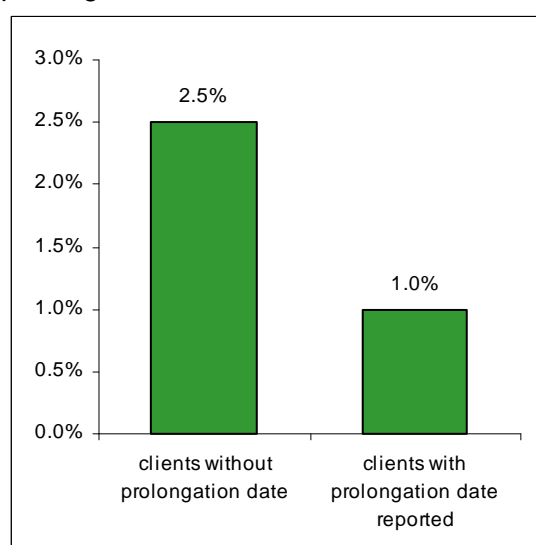
4.3.1.6. Prolongation

Clients with the prolongation date on one of their loans reported to credit bureau more often repaid timely (Figure 42). This suggests that people whose repayment schedule has been renegotiated were able to make timely repayments more often than those without any changes in the loan duration.

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[16] Source: own calculations based on official exchange rate of KGS to USD available at http://www.nbkr.kg/index1.jsp?item=1562&lang=ENG

4.4. Main findings from MFI interviews: factors affecting the level of indebtedness

Microfinance institutions identified the following factors which lead the over-indebtedness of the clients: practices of financial institutions, client behavior, economic situation, political situation and regulations. These factors were grouped into three main categories: supply-side, demand-side and external environment.

4.4.1. Supply-side

- Focus on financial rather than social performance

When financial institutions are focused on reaching their financial goals then the growth rates become more important than the quality of loan portfolio. The staff bonus system of fast growing MFIs prioritizes the increase in the number/volume of loans over portfolio quality. This way they disburse loans to clients who do not have sufficient repayment capacity.

- High growth of the loan amount per borrower

The statistics of the 2011 loan disbursements show that the average loan size per borrower has increased, unlike in the previous years when the loan portfolio of the largest MFIs was growing more slowly than the number of clients reached. Increasing debt load may lead to over-indebtedness among the clients whose income does not sufficiently grow.

- Insufficient assessment of repayment capacity

This happens when the institution is focused on growth and does not pay enough attention to the capacity of the client. There were cases when an institution had a special offer for a limited period of time when a client could get a loan without the analysis of the capacity.
However, there are also cases when credit bureau information is not used because of the inefficiency of internal system. Additionally, some institutions find it too expensive to obtain information from the credit bureau about every new loan applicant.

- Lack of transparency about interest rates and fees

When institutions do not show full information about all terms and conditions on their products then clients cannot compare offers of different institutions to choose the most suitable one. Additionally, in unfair competition, financial institutions may purposefully misinform clients about high cost of loans of other institutions.

- High interest rates

High cost of debt servicing negatively influences the financial situation of the borrower who may not have sufficient income to cover the repayment of not only the principal but also the interest and fees.

- Non-reporting to credit bureau

When institutions do not report to the credit bureau or only report some of their clients then the others cannot fully assess whether the client will be able to repay yet another loan.

4.4.2. Demand-side

- Loan misuse

When clients use business loans for non-productive purposes then their income does not increase to the expected amount projected in the business analysis and may be insufficient to cover loan repayment.

- Deceit

Sometimes clients take several loans from different institutions instead of one larger to avoid providing collateral. In such cases they may have problems in managing multiple repayment schedules.

- Lack of financial education

Clients who do not have skills to assess their financial standing are at risk of taking too much debt. They are also prone to the manipulations of financial institutions.

4.4.3. External environment

- Lack of business development opportunities

Because of weak economic situation micro and small businesses have low survival rates and if fail, then the borrower is left with no income to repay the loan. SME development strategy of the government is weak and inconsistent, so businesses do not receive significant support to survive and grow.

- Poverty

In some regions people use loans as a source of income when they cannot earn enough money to cover living expenses and thus fall into the debt trap.

- Financial crisis

The global financial crisis did not have very strong effect on Kyrgyzstan, apart from rising prices of fuel which lowered the domestic demand and increased costs of running business and living expenses.
But it indirectly further affected some enterprises. For instance, clients engaged in export to Russia and Kazakhstan had lower revenues because of lower demand from those countries. Also, traders from Dordoi market were affected by the financial crisis.

- Unstable political situation

Closing of the borders with Kazakhstan affected borrowers who generated income from cross-border exchange. Also, clients engaged in tourism industry observed lower business because of fewer tourists coming to the politically unstable country. Violent clashes in Osh in June 2010 disrupted many businesses leaving them unable to repay loans.

- Lack of government regulation of financial institutions

There are no regulations restricting financial institutions from exposing clients to excessive debt load.

- Lack of regulations concerning participation in credit bureau

Currently, reporting to the credit bureau is voluntary, therefore, institutions may choose not to provide information about their clients. At the moment the risk of that is low, as the majority of banks and the largest MFIs report to the bureau, but in the future some institutions may opt out without any consequences.

5. Discussion of the results

The results of the study showed that the amount of debt per borrower in Kyrgyzstan is considerable in relation to the average income of citizens as it exceeded by more than 3 times the annual GNI per capita. However, this result is quite likely to be over-estimated because of under-reporting of some part of small loans in the segment of loans up to $1,000. Therefore, the result should be treated with caution.

The relative debt amount per borrower is higher than in Bosnia-Herzegovina or Kosovo – the two countries where in-depth research on over-indebtedness was conducted. The comparisons with other countries were not possible because of the lack of information on the outstanding balances of Kyrgyz borrowers, the indicator most often reported in other countries to measure the level of credit use.

Both drawbacks (full reporting of small loans and outstanding amounts) are currently being resolved by CIB "Ishenim", so future analysis of the data will provide more representative results.

Multiple borrowing which is the biggest concern of lenders in Kyrgyzstan was confirmed as one of the drivers of repayment defaults. The scale of multiple borrowing varies from region to region and is higher in the regions with higher penetration of credit. Therefore, further expansion of financial institutions is very likely to increase the scale of simultaneous borrowing and deepen repayment problems.

Additionally, the repayment performance is directly related with the number of institutions in the area. The availability of credit from several providers leads to less timely payments. The repayment delays over 30 days were found to be more frequent in Bishkek and Osh, where the largest number of financial institutions operates. The scale of multiple borrowing was below average there, indicating that the effect was independent of the number of loans, as it was seen also among clients with only one loan. The latter can be a result of competition among lenders and expansion to the segments of clients with low repayment capacity. On the other hand, it can also be explained by low incentive for clients to repay in locations where the next credit can be taken from other providers (low loyalty to the institution).

Still, it needs to be highlighted that the repayment performance of Kyrgyz borrowers is very good and only a fraction of clients are delayed with repayments.

Financial institutions interviewed during the project attribute over-indebtedness mainly to multiple borrowing resulting from competition. But all interviewed institutions do not see yet see the over-indebtedness as deep. Rather, the first worrying signals alert them to think of averting the trend by taking preventive actions.

The fact that clients are allowed to take too much debt is mainly a result of insufficient verification of their credit status by financial institutions – either because of their inefficiencies (no systematic use of credit bureau data) or because of the focus on growth. The competitive pressure sometimes drives financial institutions to lend to clients who already have several loans in order to 'take them over' from other lenders. Additionally, lack of transparency about the interest rates results in limited opportunities for clients to compare credit offers and make informed choices. This adds to low financial education of clients who may not have sufficient knowledge to borrow wisely and skills to manage debt.

6. Conclusions

The analysis of the credit market in Kyrgyzstan conducted in this study allowed for diagnosing the situation in the country in terms of the level of credit use, multiple borrowing as well as the repayment performance.
The first in-depth analysis of CIB "Ishenim" database of borrowers showed that quite a lot can be learned from credit bureau data, especially if it is conducted regularly and presents changes over-time.

CIB "Ishenim" can be praised for its efforts to provide deep and reliable information. It constantly improves the database set-up and the quality of data, and also attracts new members to report their clients. This very well positions CIB "Ishenim" to be the main information provider and periodically publish main indicators concerning the level of debt and repayment performance of Kyrgyz borrowers.

Additionally, the results of the analysis show that although the amount of debt per borrower is relatively high the repayment performance remains very good.

What remains unknown is how the level of debt relates to the income of the borrowers, whether the repayment takes away a significant part of people's income. As importantly, the story from the point of view of clients is not heard yet. Research is needed to answer the question of the perception of debt burden and sacrifices which will allow for assessing the degree of over-indebtedness. This calls for more in-depth research among the borrowers to understand how serious the problem of over-indebtedness is.

Moreover, this is a good moment to introduce preventive measures to avoid over-indebtedness on a scale seen in some other countries. The chapter below presents the recommendations for different stakeholders.

7. Recommendations

Based on the above findings the following recommendations can be made to the participants of the credit market. As this was the first study of the issue of indebtedness in Kyrgyzstan, the recommendations indicate areas for the improvement rather than ready solutions to the problem.

In general, the study results call for more responsible conduct of both sides of credit contracts (lenders and borrowers) but also for some preventive activities among the support institutions.

General (donors, investors, AMFI association)
- Support further research on the issue of indebtedness/potential over-indebtedness

Primary research is needed among the borrowers to find out the degree of over-indebtedness in the country, identify most susceptible groups and better understand the mechanism of falling into over-indebtedness.

- Support the development of the capacity of credit bureau

In order to improve the availability of information about borrowers CIB "Ishenim" needs further support in improving its database system, so that it could collect more types of information and ensure good quality of data.

CIB "Ishenim"
- Inform the population about the scale of borrowing and repayment untimeliness

At present CIB "Ishenim" produces a variety of reports for its member institutions however, little information is released to the public. Some of the information about the development in the credit sector should be publicly available through periodic reports presenting basic statistics such as the number of active borrowers, value of loans, number of clients with parallel loans, share of overdue clients[17].

- Introduce obligatory reporting of credit amount of all clients, individually by name, including those with group loans

In order to have comprehensive information about borrowers CIB "Ishenim" should continue working with the financial institutions on the disclosure of full credit information on all borrowers.

- Introduce outstanding loan size as one of variables

Currently, financial institutions report to the credit bureau the disbursed loan amount but they do not update the outstanding amount, unless the client is late with repayments. However, the outstanding amount is more informative as it allows the financial institution considering the next loan disbursement to determine the current debt load of the loan applicant.

- Introduce filters which will prevent inconsistencies, errors and omissions in data reported by financial institutions

In order to ensure good data quality provided by financial institutions the credit bureau should continue improving the database design which will prevent errors made at data entry.

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[17] The example of such report is presented in Annex 1

- Simplify the classification of clients for easier identification of active clients and their repayment status

Currently, the database design provides an opportunity for including a lot of information about the loan status, but the level of detail can sometimes be constraining the analysis. It is therefore advisable that the categories for classifying the clients be reduced.

CIB 'Ishenim' is already in the process of improving the database, reports and services for its members and is open to discuss any suggestions from his partners.

Financial institutions

- Become a member of credit bureau

All financial institutions engaged in credit provision should be active members of CIB "Ishenim" and provide information about the disbursements and repayments of their clients.

- Report to credit bureau full information about all borrowers in a timely manner

In order to ensure that the data of the credit bureau are complete and reliable, financial institutions should work out the way to report group loans for each group member individually. Each borrower – member of the group – should be listed in the credit bureau database by name and full information about his share of liabilities should also be disclosed.

- Strengthen the assessment of the repayment capacity, including the use of credit bureau data

As it is becoming more and more evident that people take parallel loans, more attention should be given to the assessment of not only the costs of living but also any costs associated with servicing of debt. Therefore, credit bureau data check should be an obligatory part of the client assessment procedure.

- Limit lending to clients with multiple (parallel) loans

In the assessment of loan applicants financial institutions should place more emphasis on the number of active loans the applicant already repays, especially if they are taken from several different institutions.

- Be transparent about interest rates and fees

Disclosure of the costs associated with loan servicing should be available to any interested party – current and potential clients, other institutions, general public. This way clients will be able to assess the affordability of credit products and make informed decisions about the debt amount they are able to repay.

- Jointly conduct over-indebtedness prevention campaign among clients

As the issue of (potential) over-indebtedness is new in Kyrgyzstan many current and future borrowers may not be aware of the risk involved in borrowing. It is important that financial institutions engage in activities promoting wise and safe borrowing. Messages can be developed using materials from financial education programs and can be disseminated through leaflets, posters and other printed materials.

- Support financial literacy programs for clients

Financial institutions can either directly engage in delivering financial education to their clients or liaise with other organizations (NGOs, educational institutes, etc.) which are already engaged in educational activities.

Financial education can be provided by an MFI in the form of training or counseling and can take place during group meetings, or individually at the time of placing a loan application or making monthly repayments.

Clients

Borrowers should be more self-reliant in the assessment of their credit needs and the capacity to repay their loans. Rather than leaving it up to a financial institution to come up with the repayment schedule, clients should be aware of how much they can repay monthly taking into account the seasonality of income:
- Monitor household financial flows
- Know the repayment capacity

Clients should also be more wary about the offers of the financial institutions and make sure that they understand the obligations before signing the agreements:
- More carefully choose products by comparing credit offers of various institutions
- Read loan agreements and make sure everything is clear and understandable

Additionally, clients should also avoid the risk by refraining themselves from overspending financed by credit:
- Limit debt load only to the necessary amount
- Limit multiple (parallel) borrowing from different institutions
- Use credit according to its original purpose

Regulator

- Obligate financial institutions to report to credit bureau

The participation in the exchange of credit information facilitated by the credit bureau should be made a necessary requirement for all financial institutions. Reporting client data to the credit bureau is necessary for other institutions' credit decisions, so it should not be left to the discretion of the lender whether to participant in the data exchange or not.

- Obligate financial institutions to use credit bureau data in the repayment assessment procedure

In the interest of not only the financial institution but also a borrower financial institutions should be mobilized to use credit information available at CIB "Ishenim" in the assessment of credit worthiness of the client and determination of the credit amount.

- Actively engage in client protection

The involvement of the regulator in customer protection can either take a form of general promotion of the Client Protection Principles among financial institutions, or more specific guidance (for instance, development of acceptable dispute resolution procedures, fair conduct and collections codes) or the introduction of certain requirements (for instance, minimum information disclosure requirement).

- Engage in awareness raising on the dangers of over-indebtedness

The regulator can initiate the information campaign for the population explaining the risks involved in borrowing and the consequences of excessive indebtedness. Such information campaigns in public media can be in a form of a series of social advertisements on radio or TV – short spots highlighting the risk of over-borrowing.

It can also take a form of leaflets, posters and other printed materials which will be distributed among the population.

- Engage in programs promoting financial education

The authorities should support initiatives strengthening financial knowledge and finance management skills of the population. This can be done through the coordination of the activities of non-government institutions already implementing educational programs for adults or by influencing the educational decision-makers (Ministry of Education or other) to upgrade school teaching programs.

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# Annex 1 – Proposed template for CIB "Ishenim" reports

Main Statistics November 24th, 2011

Number of active loans	**603,704**
Number of active borrowers	**415,812**
Total disbursement value of active loans	**83.7 trillion KGS**
Borrowers overdue>30 days	**5,550 (1.34%)**
Total outstanding value of loans overdue >30 days	**697 million KGS**

Active loans

77% of active loans were disbursed by microfinance institutions and 23% by banks.

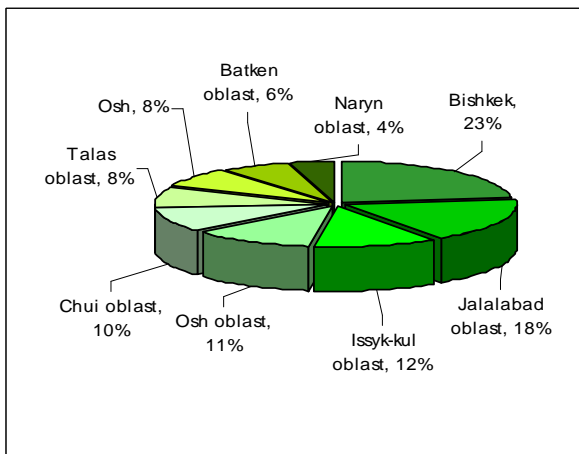*Distribution of active loans by source*
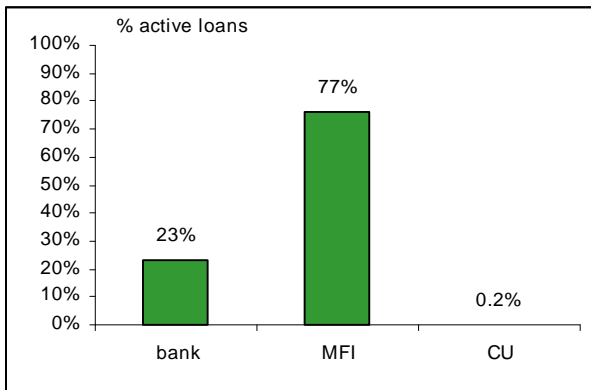
The average size of an active loan was 138,000 KGS (3,030 USD) at disbursement.
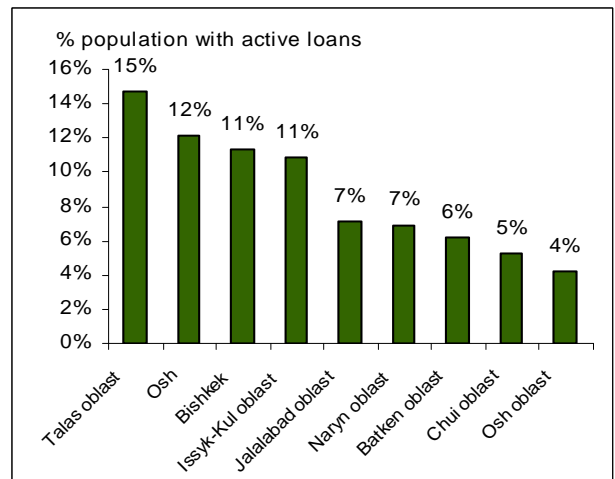
Active borrowers

The largest number of borrowers was located in Bishkek.

Distribution of active borrowers by region

The average credit penetration rate was 8% with the highest share of the population using credit in Talas oblast (15%).

Share of the population with active loans by region


Parallel loans

31% of active borrowers had parallel loans. The average number of parallel loans per borrower was 1.46.

Location	% clients with parallel loans	Avg. number of active loans
Talas oblast	41%	1.59
Issyk-kul oblast	35%	1.55
Jalalabad oblast	30%	1.47
Osh	23%	1.32
Naryn oblast	23%	1.40
Osh oblast	22%	1.34
Bishkek	20%	1.28
Batken oblast	18%	1.30
Chui oblast	17%	1.25
Total	**31%**	**1.46**

Repayment performance

The largest share of clients with repayment delays over 30 days was located in Osh and Bishkek.

Share of active borrowers overdue for over 30 days by region
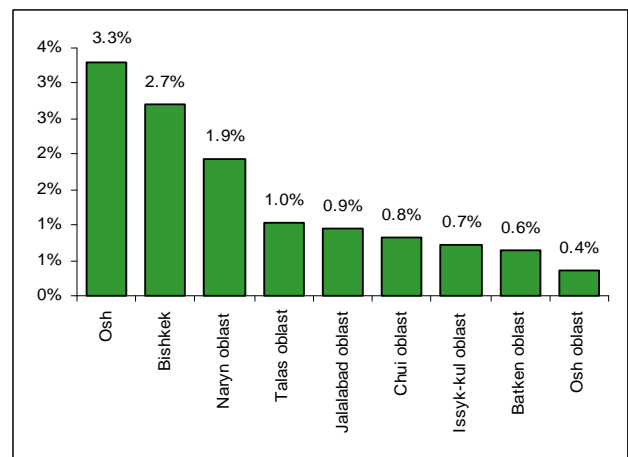
Number of financial institutions

48 financial institutions providing credit, members of CIB "Ishenim", took part in the exchange of data.

The largest number of credit providers was in Bishkek, but given the size of the population in each of the locations the concentration of the financial institutions differed from region to region.

Number of financial institutions in each region

The largest concentration was seen in Osh city with 10.8 credit providers per 100,000 people.

Number of credit institutions per 100,000 inhabitants