Microfinance - Trends of top-up loans during covid-19 pandemic

The first wave of Covid-19 in India is characterized by its first case in January 2020 followed by a nationwide lockdown, which was announced in March 2020 and was implemented in phases until end of May 2020. The implementation of lockdown on an unprecedented scale affected livelihoods of all sections of people including microfinance customers. In past, resilience of microfinance industry was tested by many shock-inducing events like natural calamities, demonetization, political activism etc. The current pandemic is another event which has affected and continues to affect microfinance institutions and their clients.

In the beginning of pandemic, disbursements shrunk to an all-time low of 6,186 crores INR in Q1 FY20-21. As seen in exhibit 1, quarterly disbursements slowly picked up and reached pre-covid levels by Q3 FY 20-21. The demand for credit had steadily increased from Q1 FY 20-21 to Q3 FY 20-21 as economic activity picked up with many geographies starting the 'unlock' process during this period. As per our field monitoring visits during this period, the increase in disbursements was also contributed by demand for smaller amounts, in form of additional loans or top-up loans or emergency loans from existing customers.
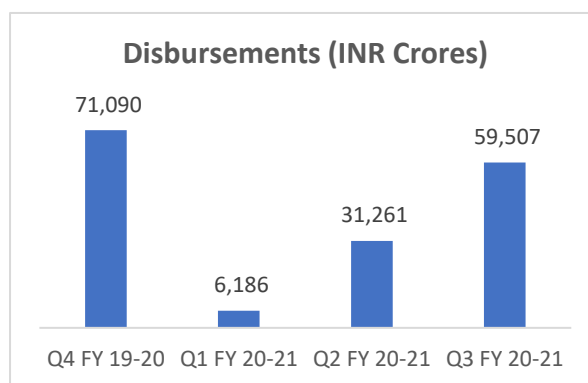
Disbursements (INR Crores)

Exhibit 1: MFI Quarterly disbursements

The top-up loans have been disbursed across multiple customer segments and geographies with varying purposes. Many organizations have disbursed these loans to existing customers who are in genuine need of short-term liquidity support and who showed an intent to pay by meeting at least one payment obligation during the pandemic period. While these top-up loans are considered as a measure to support the vulnerable segment by customer-centric, impact focussed microfinance institutions, there is an increasing perception of risk for these loans, especially when they are disbursed to overdue customers. In this blog, we intend to define what is a top-up loan and analyse trends of top-up loans in terms of customer segment and geography. Please note that we have not analysed performance of top-up loans in this blog, as it is too early to comment on the same. We will monitor these top-up loans and publish performance of these loans separately in subsequent blogs.

Data used for the analysis

Scrub repository of loans, which are part of pools securitized by Northern Arc Capital live as on Aug-20 is used for this analysis. The total repository of unique customers considered here is 2.66 Lakhs. The important fields which are part of this repository are
   o   Outstanding amounts of all the live loans of the borrower
   o   DPD (Days Past Due) status of all the loans of the borrower
   o   Loan start date of all the loans that the borrower has taken

Repayment frequencies of different underlying obligations of each customer can vary from bi-weekly to monthly. For EMI based analysis, using scrub data of all underlying customers, all live obligations of customers are converted into monthly frequency.

Definition of top-up loan

The top-up loan is defined based on the below mentioned criteria.

- The borrower should have at least two loans post Aug-20 with the same lender
- The latest loan disbursed should be after Aug-20 and the earlier loan should be live or closed after Aug-20
- The DPD status of the earlier loan at disbursement of the new loan should be between 1 DPD and 90 DPD

The end borrowers satisfying top-up criteria are flagged as borrowers who have availed top-up loan and the latest loan availed by the borrower is tagged as top-up loan.

Data analysis and findings

Summary of Top-up Loans

In the selected sample of 2.66 lakh customers, 21,573 customers, amounting to 8.09%, were identified as customers who have availed top-up loan basis the criteria outlined in the previous segment. Also, out of 1.08 lakh loans disbursed after August -20 to clients with existing relationship, 25.56% of loans or 27,642 loans can be classified as top-up loans.

Exhibit 2 shows the transition matrix of earlier loans before and after the disbursement of the top-up loan. For instance, 22.34% of overall top-up loans have been sanctioned to close the earlier obligations in 1-29 DPD. It can be clearly inferred that 46.7% of the top-up loans have been used to close the previous loans which are in >0 DPD and 43.67% of top-up loans have been used to improve the DPD status or help the earlier loan remain in the same DPD status. Only in less than 10% of the cases the DPD status has worsened after disbursement of the top-up loan

	Closed Account	Current Account	1-29 DPD	30-59 DPD	60-89 DPD	>89 DPD
1-29 DPD	22.34%	9.70%	6.94%	2.03%	0.58%	0.04%
30-59 DPD	11.90%	6.94%	5.04%	5.18%	2.52%	1.77%
60-89 DPD	8.81%	2.65%	3.82%	0.79%	2.23%	1.90%
>89 DPD	3.67%	0.13%	0.16%	0.07%	0.01%	0.78%
Total	46.72%	19.42%	15.96%	8.07%	5.34%	4.49%

Exhibit 2: Transition Matrix of account status of the earlier loan before and after disbursement of top-up loan

Indebtedness of borrowers

Exhibit 3 provides distribution of borrowers across different indebtedness buckets and percentage of top-up loans availed in each of the categories. The indebtedness level of a borrower is calculated by taking sum of principal outstanding of all live loans available in microfinance bureau. It can be clearly inferred that the percentage of top-up loans has increased as the indebtedness level of underlying borrower increases. Highest indebtedness bucket of >2L (greater than 2 Lakhs INR) has highest percentage of top-up loans, but they constitute only 0.45% of overall sample of customers.
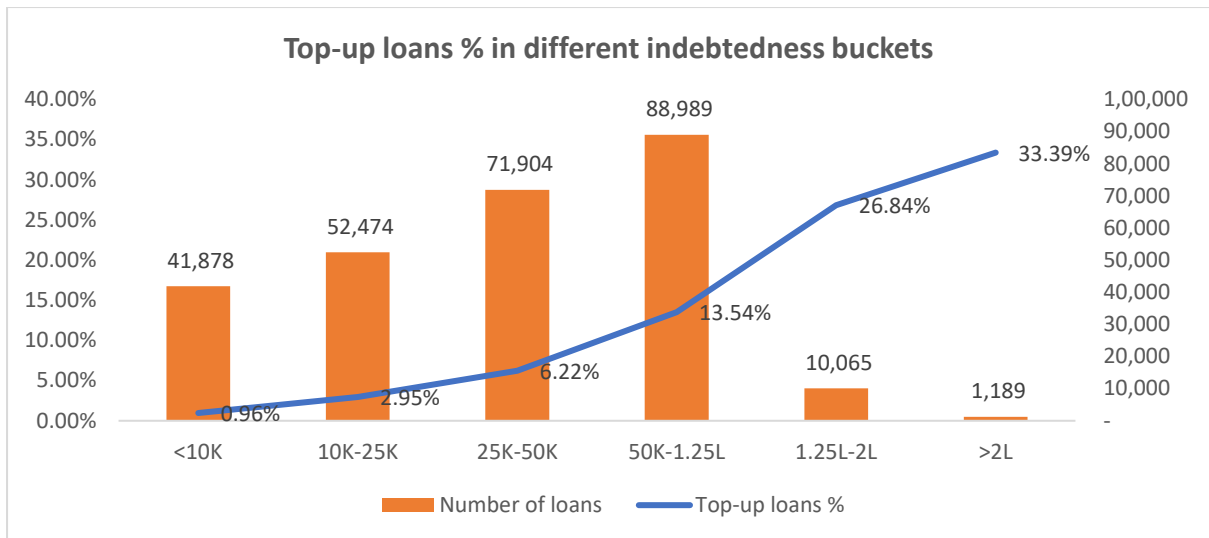
Top-up loans % in different indebtedness buckets

Exhibit 3: Indebtedness bucket wise split of top-up loans

EMI

Exhibit 4 provides distribution of borrowers across different EMI buckets and percentage of top-up loans availed in each of the categories. EMI level of a borrower is calculated by taking sum of monthly outstanding of all live loans available in microfinance bureau. It can be clearly inferred that the percentage of top-up loans has steadily increased as the EMI levels of the customer increases.
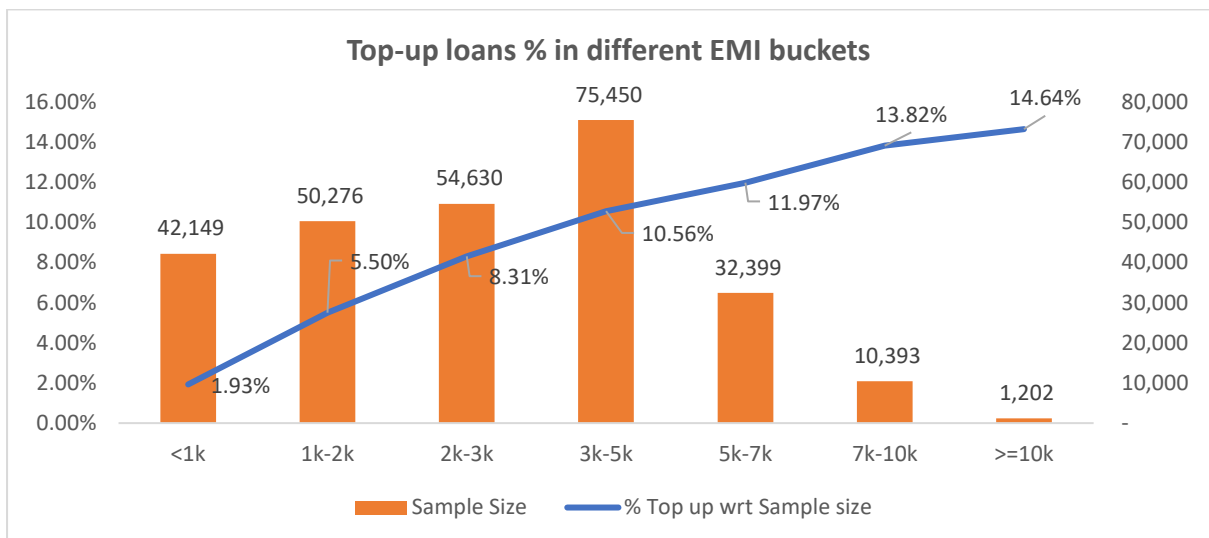

Top-up loans % in different EMI buckets

Exhibit 4: EMI bucket wise split of top-up loans

Geographical distribution of top-up loans

State wise percentage of top-up loans is depicted in exhibit 5. West Bengal, Maharashtra and Odisha are top 3 states in terms of highest percentage of top-up loans. Southern states like Tamil Nadu and Karnataka are geographies with lower percentage of top-up loans disbursed.
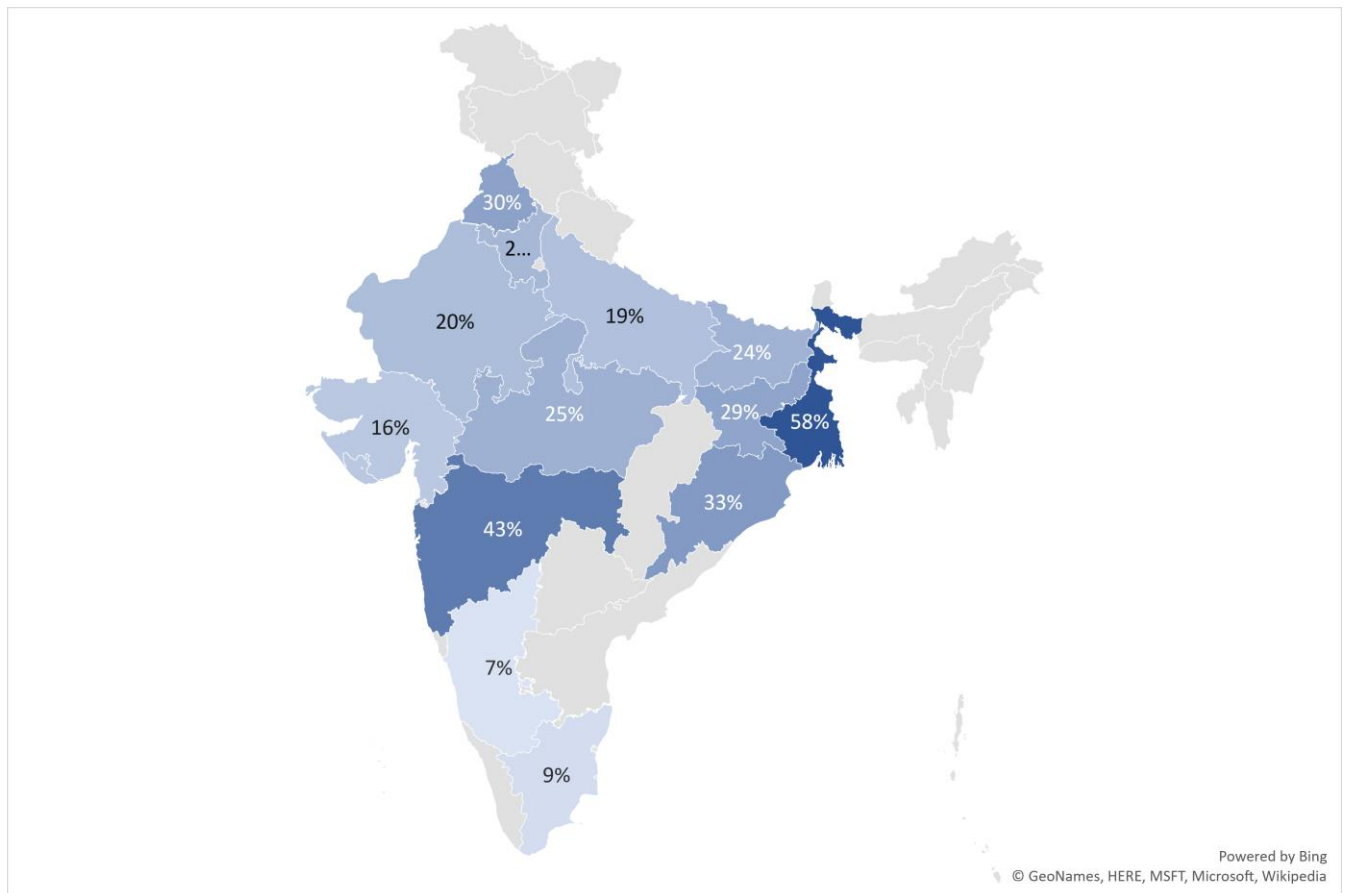
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Exhibit 5: State wise distribution of percentage of top-up loans

Conclusion

Microfinance institutions have disbursed top-up loans to underlying borrowers to help them wade through difficult times posed by covid-19 pandemic. This immediate support lent by financial institutions should help borrowers revive their economic activities, wherever there is a genuine need of it. While this is an essential support required from borrowers' standpoint, it would also be important for all lenders to closely monitor performance of these loans.

In this blog, we defined a methodology on how to identify top-up loans and analysed which borrower and market segments that have availed top-up loans in microfinance. Percentage of borrowers availing top-up loans is increasing with increase in both indebtedness levels and EMI levels. This corroborates with shrinking income levels in current pandemic and need for additional financing is more at higher indebtedness levels. Higher percentage of borrowers in markets like West Bengal, Maharashtra and Odisha have availed top-up loans, as economic activities in these geographies have seen severe impact due to stricter lockdowns.

It is too early to comment on performance of top-up loans as most of them have been serviced only for a short duration of 1-3 months when scrub output was pulled. We would post a subsequent blog on performance of these loans once a considerable repayment history is generated.