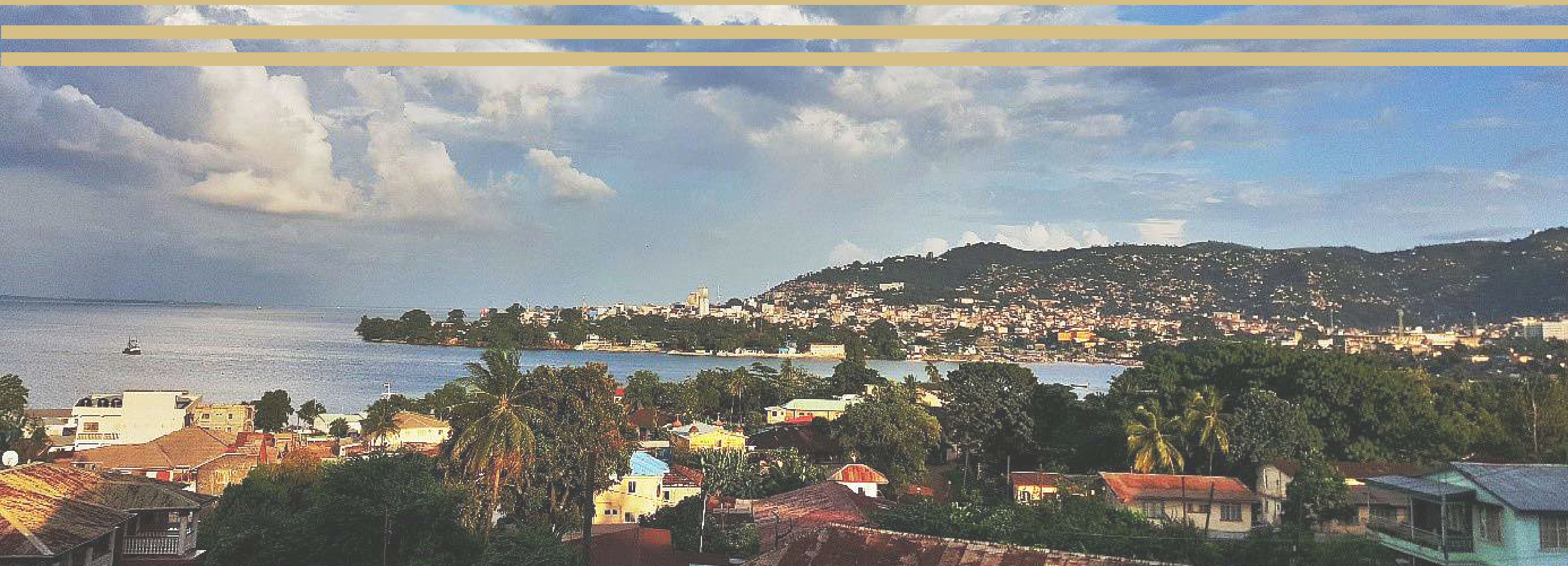
EXTERNAL RISKS: CONTINGENCY PLANNING GUIDE FOR MICROFINANCE INSTITUTIONS IN SIERRA LEONE



Cordaid

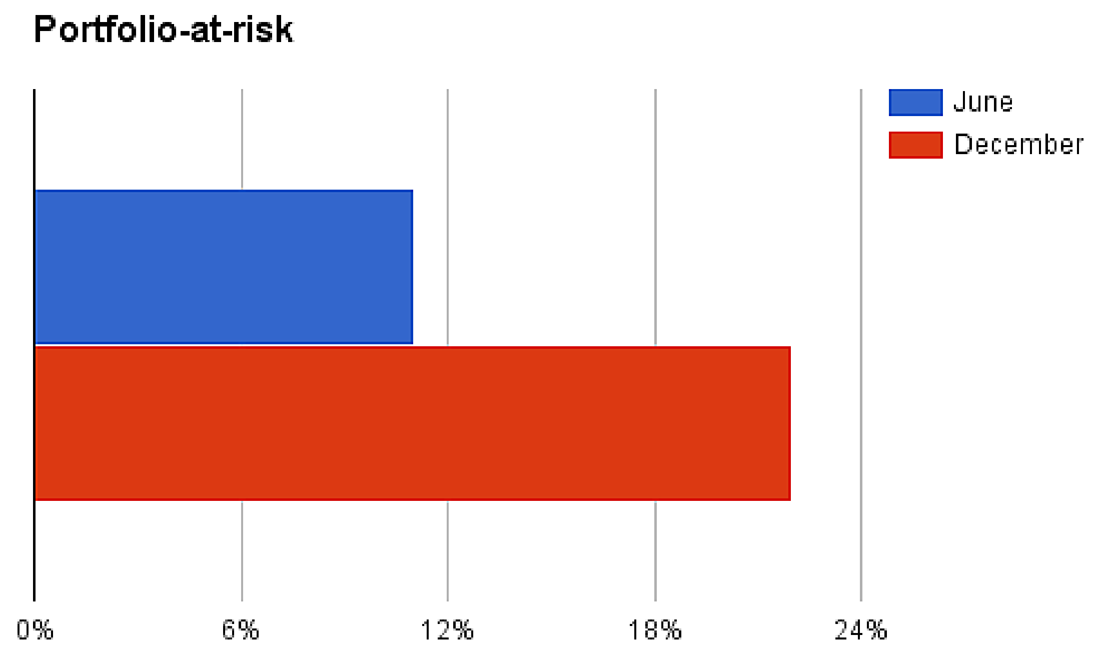
SLAMFI
Sierra Leone Association of Microfinance Institutions

AYANI
inclusive financial sector consultants

Table of Contents

1. INTRODUCTION

The Ebola crisis that lasted for 18 months had a profound impact on microfinance institutions (MFI) in Sierra Leone. Loan disbursements declined by 36% during the peak crisis period of *July to December 2014*, as compared to the same period in the prior year. MFI growth plans were disrupted, and business plan implementations were suspended in the context of uncertainties posed by the crisis.



Portfolio-at-risk over thirty days (PAR>30) stood at 11% *in June 2014* and had doubled to 22% *by December 2014.*

Meanwhile, 3,074 borrowers fell into delinquency during the period. Prior to the Ebola crisis, eight (8) MFIs had achieved or were approaching 100% Operational Self-Sustainability (OSS); however at the end of 2014, seven of these had registered a decline in OSS, and the sector reported an average OSS of only 78% -- an unacceptable level. [1]

The microfinance sector needs to consolidate lessons learned to be able to manage external shocks such as the Ebola crisis and build resilience. External risks are beyond the control of MFIs but risks and impacts can be minimized. Sierra Leone is also a fragile country characterized by exposure and vulnerability to climate-related extreme events, and other economic, social and environmental shocks. It needs to build adaptive capacity. Furthermore, foundations that promote economic, social and political inclusion need to develop and when such are weak there is a potential for violence or conflicts to emerge.[2]

Contingency Planning Guide

This Contingency Planning Guide is designed to help MFIs prepare its own pre-disaster contingency or business continuity plan to reduce the risks and impacts from external risks, natural and man-made disasters, and resume normal service delivery to clients as quickly as possible.

In order to prepare this guide, the following activities were undertaken:

• External risks assessment survey amongst MFIs to prioritize the risks which are considered to be the most likely to happen in Sierra Leone, the areas of vulnerability and the expected extent of impact.

• A discussion forum with members of the ***Sierra Leone Association of Microfinance Institutions* (SLAMFI)** as an after action review to assess the measures undertaken by MFIs during the Ebola crisis and specifically on what measures worked and what could have been done better.

• Secondary research and review of existing studies on pre and post disaster risk management specifically for the microfinance industry and businesses in general. **SLAMFI** is instrumental in the validation of assumptions and relevance of findings for the Sierra Leone context.

[1] Cordaid, SLAMFI and Ayani BV. Sierra Leone: The Impact of the Ebola Crisis on the Microfinance Sector. March 2015.
[2] OECD. States of Fragility 2015: Meeting the Post 2015 Ambitions. OECD Publishing. Paris.

2. EXTERNAL RISKS ASSESSMENT

Based on the external risk assessment survey, the top 5 risks considered by MFIs in Sierra Leone are the following:

i. Pandemic diseases
ii. Flooding
iii. Political disturbance
iv. Technological failure specifically severe power outage
v. Armed Conflict

↓

The top vulnerabilities considered by MFIs are the following:

i. Staff safety and security
ii. Loan portfolio
iii. Business chain of operations
iv. Supply of required goods / services
v. Property – building, other fixed assets, documents, and MIS (for flooding, political disturbance, and armed conflict risks)

↓

The following aspects are the expected major impacts:

i. Staff trauma / infections / injuries / deaths
ii. Loan portfolio quality / defaults / write-offs
iii. Cash liquidity
iv. Financial losses
v. Loss of access to staff and existing clients
vi. Business interruption

3. INSTITUTIONAL PREPAREDNESS

This section briefly describes measures that can be undertaken by MFIs to prepare itself for external risks and are selected based on their significance towards addressing the major vulnerabilities and impacts identified by the MFIs. The following also provides a basic outline of what can constitute an *MFI's Disaster Contingency Plan*:

i. Creating a Crisis Management Team
ii. Ensuring Staff Safety and Security
iii. Protecting Infrastructure and Equipment
iv. Safeguarding the Management Information System
v. Internal and External Communication
vi. Loan Portfolio Management
vii. Liquidity Management
viii. External Coordination

3.1. Creating a Crisis Management Team

The main responsibility of the *Crisis Management Team (CMT)* is to assess the crisis situation and decide on how to respond to reduce the adverse effects of the crisis on the organization. MFIs may use its regular senior management team for this purpose. However, a broad cross-section of people from the MFI may also be useful but focused on those with oversight or expertise vital to the functioning of the MFI during the crisis at hand and the regular assessment of the situation.

The CMT may therefore be composed of a core team - the senior management team who will then decide to extend the composition of the team to a handful of people based on the nature and extent of the emergency. One of the members of the Board of Directors may also be permanently assigned as a member of the CMT.

The key steps that the CMT could undertake are:

i. Assess the nature of the external risk / emergency, determine the MFIs vulnerabilities and expected major impacts.
ii. Prioritize the issues and identify specific measures how to reduce the impacts.
iii. Assign team members responsible to lead implementation of specific measures.
iv. Double check information before finalizing the plan.
v. Meet daily or as often as possible to review the situation, and obtain feedback from team members on the effectivity of the plan.

3.2. Ensuring Staff Safety and Security

Some emergencies require that operations have to stop and employees have to leave quickly. The decision to do so may be made by local authorities. If not, it should be decided in advance who in the MFI will make that decision to cease operations. That person could also be the same person who will declare an all-clear and return to work.

- Also decide who is responsible to call and monitor the situation of staff.
- Staff employment records should have contact numbers of person to call in case of emergency.
- Department heads and branch managers must have this list of staff emergency contact numbers readily retrievable as well contact numbers of hospital, ambulance service, police and other relevant local authorities.

There will also be situations when it is best to stay where you are to avoid any uncertainty outside. In general, employees cannot be forced to stay. However, there are circumstances when local authorities will order that everyone stay put.

- Account for all workers, visitors and customers that are in your premises.
- Lock the doors and windows.
- Local authorities may not immediately be able to provide information on what is happening and what you should do. However, you should watch television or listen to the radio for official news and instructions as they become available.

3. INSTITUTIONAL PREPAREDNESS

For disease outbreaks, plan to raise awareness and educate staff on precautions and preventions. One way is to invite officials from the *Ministry of Health and Sanitation (MoHS)*, or engage an NGO or private expert to educate staff about the disease. Disseminate printed materials about the disease. If there are available funds, purchase and provide staff with prevention kits or supplies. Maintain a First Aid Kit and basic medications in each branch location.

Support staff health after disasters and provide for time at home to care for family needs, if necessary. Create opportunities for breaks where co-workers can talk openly about their fears and hopes as sharing with others can speed personal (mental and emotional) recovery. Based on MFI's financial position or available resources, the Senior Management Team or Crisis Management Team may develop policies on financial or in-kind assistance to affected staff members. Also provide health and life insurance for staff as part of their employment benefits.

3.3. Protecting Infrastructure and Equipment

Obtaining adequate insurance cover for property and equipment is necessary. Inadequate insurance can lead to major financial loss if MFI assets are damaged or destroyed. Review the coverage at least annually with your insurance agent.

Your MFI could closed offices or branches when there is a major political disturbance that could possibly lead to riots or armed conflict. Develop a policy on vehicle and other equipment evacuation, including assigning responsibilities to staff members. This could include taking down signages if necessary to avoid being particularly targeted as a financial institution. Develop policies to ensure the security of the safe and office keys so that none is left in the office at the time of a natural disaster.

Ensure that your MFI has a functioning back-up power supply (generator and / or batteries). Severe power outage is considered as one of the top risks in the country. The current energy generation, transmission and distribution capacity in Sierra Leone is frail. If there is prolonged or severe outage, the immediate impact will be high costs, specifically expenses on back-up power supply, and inefficient delivery of services to clients due to business interruptions. This can only be mitigated by having well-maintained power supply at each branch and ensure that costs of energy is reasonably factored in the pricing of loan products without undue passing on MFI inefficiencies to clients.

After a disaster, plan what you will do if your building or equipment becomes unusable. Consider if you can run the MFI from a different location. Develop relationships with other organizations to use their facilities in case a disaster makes your location unusable or to borrow much needed equipment.

3.4. Safeguarding the Management Information System

Regular back-up of loan portfolio and financial information is considered a regular internal control practice of MFIs. With the advent of cloud computing and better internet connectivity, MFIs can now have databases function and stored in the cloud. At the very least, regular back-up of portfolio and accounting databases in the cloud should be undertaken. Important documents must also be scanned and electronic copies also stored in the cloud. Basic cloud storage services include email folders and Dropbox. Log in and password information must be securely kept where only selected senior managers can access.

MFIs should also plan for emergency payroll, expedited financial decision making and accounting systems to track and document costs in the event of a disaster.

Furthermore, ensure that MIS is robust or has adequate capacity to offer preparation, response and recovery services to clients while continuously providing accurate portfolio quality reports. [3]

- Make sure your portfolio management system can track additional products (e.g.emergency response products).

- Ensure that the portfolio management system can track restructured loans, or adjust interest rates and compulsory savings when necessary.

- Customize your MIS system so that it can track and consolidate loans by geographic region and by business category to better monitor those clients or areas most affected by the disaster.

- Track non-financial service costs related to disasters separately in the accounting system.

[3] World Bank. Surviving Disasters and Supporting Recovery: Guidebook for Microfinance Institutions. Disaster Risk Management Working Paper Series No.10. February 2005.

3.5 INTERNAL AND EXTERNAL COMMUNICATION PLAN

The ability to effectively communicate with staff, clients, local authorities, funders and the public during an emergency can make a major difference in how well your MFI is able to recover from a disaster.

Identify the key stakeholders of your MFI and clear messages must be conveyed to them. The Crisis Management Team may have to decide or develop the key messages to each stakeholder. MFI internal stakeholders are staff, board, management and shareholders. External stakeholders include clients, funders, local authorities, suppliers, banks, or the public in general.

Examples

Staff: Be prepared to provide staff with information on when, if and how to report and undertake their work following an emergency.

- Identify channels to disseminate warnings or instructions. Set up a telephone call tree to communicate with staff in an emergency.
- Be clear on how their jobs may be affected.
- Encourage open communication from employees concerning procedures before, during and after an emergency.

Management: Clearly define roles or responsibilities, and when to provide feedback. Each member of the management team will provide relevant and credible information needed for the assessment of the crisis situation in order to protect staff, clients, and assets of the MFI.

Clients: This involve pre-establishing a communications chain - from management to field staff to clients wherein key messages are authorized, clear and consistent across all clients. Regularly update your clients on whether and when services will be rendered.

Public: It may be important to update the general public with calm assurance that all resources are being used to protect staff and the community. Being able to communicate that plans are in place for recovery may be especially important.

Local authorities: Tell officials what your MFI is prepared to do to be able to help the community. Also communicate what emergency assistance is needed for you to continue essential activities.

Funders: Regularly update them of the crisis situation, what the impacts are and the actions undertaken by your MFI. Ensure transparency at all times.

Ensure a back-up communication plan in case any phone, road or postal communications are cut off. - Identify in advance institutions (*e.g. government, hospital*, NGOs) with access to radio or satellite communication which could assist during a natural disaster.

VSAT installation in PortLoko Treatment Center.
Photo Credit: Eugene Tani-Luke/Inveneo

3.6 PORTFOLIO MANAGEMENT

Being the core business and main asset of MFIs, portfolio management must be carefully planned for during emergencies. Certain crisis situations can even lead to significant portfolio losses that can put the MFI's sustainability in grave risk. MFIs must ensure lending practices remain robust at all times.

It is evident from the experience of the Ebola crisis, that high quality client selection and appraisals protected the loan portfolio from significant deterioration. It is quite known that clients who are unable or unwilling to pay in normal times are much less able or willing to pay in times of disaster.

Despite all of the precautions and pre-planning, deterioration in the loan portfolio quality must be expected. The key focus is to minimize the extent of deterioration so that in the end it does not overwhelm your institution. Based on a discussion forum with MFIs, the following are the various measures that can be undertaken, and the possible criteria or triggers to undertake such measures:

	RISK MITIGATION MEASURE	UNDER WHAT CONDITIONS OR CRITERIA?
1	RAPID PORTFOLIO REVIEW	• Slow onset disasters (e.g. pandemic diseases) - Frequently do client visits and market assessments but with high precautions for highly infectious diseases. Preferably done in regular intervals or to focus on specific affected areas, sectors, markets, or segment of clients. • Rapid onset disasters (e.g. flooding) - Immediately after the disaster when it is considered safe to go out and visit clients and local markets.
2	SUSPENSION OF LOAN COLLECTIONS	• There are government imposed-restrictions on movements. • Highly unsafe and insecure to undertake field work and collections such as when there is political disturbance/riots or armed conflicts.
3	MORATORIUM ON LENDING	• Highly unstable political situation or when there is an armed conflict. • Local markets or business activities are halted. • The country is experiencing hyper-inflation. • High risks in a specific economic sector (e.g. due to new regulations/legislation, highly volatile market situation)
4	CREDIT RATIONING	• MFI's liquidity position is deteriorating. • High risks in specific economic sectors and MFI would like to avoid exposure to these sectors.

3.6 PORTFOLIO MANAGEMENT

	RISK MITIGATION MEASURE	UNDER WHAT CONDITIONS OR CRITERIA?
5	RESTRUCTURING LOANS	• Repayment problem is expected to be short-term as business is expected to pick-up again.
6	WRITING OFF LOANS – PRINCIPAL & INTEREST	• Death of client and when there is no credit risk insurance. • After a period of time of extensive collection efforts since the disaster struck (e.g. 180 days) and still no possibility of collection is seen including that from guarantors.
7	WRITING OFF INTEREST INCOME – PRINCIPAL STILL TO BE COLLECTED	• Client is still visible although there might be no business. • There is still a prospect to recover payment perhaps through alternative sources.
8	SWITCHING FROM GROUP-BASED LIABILITY TO INDIVIDUAL LIABILITY DURING THE DISASTER	• Peer guarantee will be relaxed but group responsibility to motivate each other for repayment will continue.
9	PROVIDING EMERGENCY LOANS	• When restructuring does not work and new loan will provide re-start of business and capability to grow. • Should be given immediately after the disaster to recover. • Client has good credit history and there is renewed or potential ability to pay.
10	ALLOWING WITHDRAWAL OF FORCED SAVINGS	• While this is undertaken in some disaster stricken-countries, MFIs in Sierra Leone consider this as not helpful because compulsory savings are very minimal.
11	PROVIDING REMITTANCE / MONEY TRANSFER SERVICES	• This is a very good service to provide to clients even during non-crisis situations. This is best set-up during a normal period. • Remittances received can be used for loan repayments.
12	PROVIDING NON-FINANCIAL EMERGENCY / RELIEF SERVICES	• To increase goodwill, or as part of Corporate Social Responsibility. • Limited in scope and in-kind (not cash) so as not to confused clients with regular financial services.

3.7 LIQUIDITY MANAGEMENT

The following are usually the impacts on liquidity during and after a crisis:

• Loan collections slow down or halted but operating expenses (e.g. payroll) and payment to creditors will continue.

• Clients will save less and deposits as source of liquidity will reduce.

• Restructuring of loans result to postponed availability of funds to meet loan demand.

The following are examples of internal and external sources of liquidity during and after a crisis [4] :

INTERNAL	EXTERNAL
• MFIs own savings • Funds previously committed to new loan outlays or special projects • Credit rationing • Negotiating late payments on rent, utilities, salaries • Sale or lease of fixed assets • Shareholders' loans or capital infusion • Drawing on special cash reserves or emergency funds set aside during normal times and invested in short term, secure investment instruments (e.g. time deposit, Treasury bill). MFIs in Sierra Leone find this very costly to undertake. Thus, undertaking this depends on the size of the MFI, its financial position and the regularity of disasters.	• Obtaining grants • Having standby line of credits or overdraft facilities. • Negotiating late payments or interest waiver with existing lenders. • Gaining access to "Disaster Fund Facilities" sometimes available from donors or the government. • Factoring – Selling the loan portfolio to other lenders with a "discount"

[4] World Bank. Surviving Disasters and Supporting Recovery: Guidebook for Microfinance Institutions. Disaster Risk Management Working Paper Series No.10. February 2005.

3.8 EXTERNAL COORDINATION


Photo Credit: ebolaresponse.un.org

During disasters, Your MFI is not alone in overcoming the challenges. There can also be a hand full or a multitude of groups or organizations that your MFI can turn to for advice or support. Thus, be open to coordinating with others.

- Meet with other MFIs in your area of operations.
- Talk with first responders, emergency managers, community organizations and utility providers.
- Plan with your suppliers and other business associates.
- Share your plans with other organizations and encourage comments/suggestions to your plan.
- Offer your help when you can.


Photo Credit: ebolaresponse.un.org

4. EMERGENCY RESPONSE PHASE

MFIs, without compromising staff safety and security and given the crisis level, should undertake rapid portfolio reviews. A rapid portfolio review may include the following activities:

- Visiting clients
  - assessing their situations and ability to repay
  - assessing the level of cooperation by client

- Assessing the functioning of local markets
  - Interviewing local authorities
  - Interviewing emergency responders, NGOs, or relief agencies
  - Interviewing non-clients of various sizes (micro, small, medium and large scale enterprises)
  - Investigating with value chain / supply chain actors
  - Comparing findings with other financial institutions

This review lays the basis for the MFI's response and developing a strategy for each borrower or for the management of the portfolio as a whole. Staff needs to be trained or given thorough and clear guidance how to undertake these visits, interviews and assessments with high level of sensitivity to the psychological and emotional state of clients and the nature of crisis at hand.

Regardless, business interruption must be expected. The level of disaster preparedness however will determine how quick an MFI can resume operations and recover.


Photo Credit: A Call to Business Microfinance

5. RECOVERY PHASE

Portfolio management strategies and liquidity management strategies described in the earlier sections normally form part of an MFI's recovery strategies.

MFI's need to be prepared to allow for the restructuring of many loans in its portfolio after a disaster. *However, blanket restructuring is to be avoided as much as possible. Each client's individual situation must be assessed by the loan officer and the new payment arrangement tailored to each client's capacity to repay.* Write-off is a last resort and only done after a period of time has been given to client to recover and yet collection is still a remote possibility. Under normal MFI practice, a write-off is only an internal accounting process and does not remove the client's obligation to repay.

Refinancing or providing an additional loan is much riskier than restructuring. It must only be done after a careful analysis and structuring such that client will have the capacity to pay for both loans and at the same time continuously meet the client's family or household needs. *Refinancing must be avoided if it will result to client over-indebtedness and this is usually apparent when client will have to make sacrifices that are detrimental to his/her own well-being and that of the family or household.* For example, children will be stopped from attending school.

Loan disbursements must also be immediately resumed to existing clients that have fully repaid. Disbursements to new clients may not be advisable when the MFI still has a liquidity crunch as it would be best to prioritize current clients that may have higher demand for loans.

Monitoring of affected clients and more frequent visits to them is necessary but with high sensitivity so as not to create unnecessary pressure to pay but rather to express that the MFI cares, to provide positive motivation and analyzing together with client to find realistic repayment solutions.


Photo Credit: ebolaresponse.un.org

6. LESSONS FROM THE EBOLA CRISIS

Ensuring Staff Safety and Security

MFIs extensively raised awareness amongst staff on infection prevention and encourage them to also educate their families on the disease. MFIs approved special funding to buy and provide staff with a package of protective supplies such as water buckets, chlorine, hand sanitizers, and gloves.

External Communication

Continuous communication and engagement of clients by MFIs during the crisis period provided some level of comfort that the lending relationship will be sustained at recovery or after the crisis period. One MFI acknowledged that branches shouldn't have been closed as it created a rumor that the MFI has permanently left. Instead, branches could remain open with a few staff present to continuously engage clients. Another MFI actively sought donorfunds to be able to provide clients with a packageof food and protective supplies as part of continuously engaging clients.

Photo Credit: ebolaresponse.un.org

Communication was also of utmost importance during the recovery phase.When Ebola restrictions were gradually eased, MFIs held small group client meetings, meetings with group leaders,or branch council meetings[5] to survey clients and understand their perspectives and views towards recovery.

Loan Portfolio Management

- *Having diversified Market segments and products allow MFIs to alleviate overall negative impact. MFIs that have SME loans, salary and consumption loan portfolios had better overall portfolio quality as compared to just offering the group loan product. In addition to diversified clientele,diversification of geographical outreach and economic sectors being served also reduced the risks.*
- *One MFI tested one branch to resume loan disbursements whilst the crisis is still ongoing. It observed that loan repayments increased and clients were eager to get new loans. The MFI then resumed disbursements in other branches after the positive results from the test branch and repayment did improve across all the branches.*

Photo Credit: ebolaresponse.un.org

Liquidity Management

Due to the expected decline in operating revenues from suspension of loan disbursements and slowdown of collections,MFIs decided to tighten operating expenses where it is possible.

[5] MFI, LAPO Sierra Leone, normally establishes a branch council wherein clients in a specific branch select a group of leaders to represent them in various matters with the MFI and also serves as a communication channel.