

Reserve Bank of Malawi on Pricing Disclosure

The Reserve Bank of Malawi (RBM) is leading an effort to require pricing disclosure for all microfinance institutions (MFIs) in Malawi. This directive of the new Malawi Microfinance Bill¹ will help ensure that microfinance institutions clearly communicate their pricing to clients prior to disbursing loans. *MFTransparency* interviewed Lanjes Sinoya, Principal Examiner at the Reserve Bank of Malawi, about the pricing disclosure and client protection aspects of the bill. The following excerpts from the interview will provide insights into the process and motivation for developing this policy.

Introduction

The RBM's new pricing disclosure policy is part of the Malawi Microfinance Bill of 2010. Section II, Subsection 1 of the bill states that "All microfinance institutions, including approved financial institutions, shall display in a conspicuous place on the premises of every branch where they conduct business a notice containing [among other things] terms under which microfinance products and services are offered." Concerning pricing disclosure specifically, the directives state in Section 1, No. 3 "Micro Credit Agencies shall, at all times, carryout fair lending practices. The contract between the lender and the borrower must state the nominal rate of interest as well as commissions and fees either on an annual or monthly basis."

The Malawi Microfinance Bill was enacted on September 1, 2010 but at the time this case study was published it had not yet been implemented and was in the review stages. In the following interview, Lanjes Sinoya, Principal Examiner, outlines the process that the RBM is taking to develop this new policy, as well as the intended impact for the Malawian microfinance industry.

Developing the Policy

The Malawi Microfinance Bill contains two specific directives: the 'Microcredit Agencies Directive' and the 'Non-Deposit MFI Directive'. These directives aim to establish requirements for registering and supervising MFIs to ensure adherence to best practices and corporate governance standards. According to Mr. Sinoya, the persistent occurrence of complaints from MFI clients reported to the Reserve Bank, Consumers Association of Malawi, and Office of the Ombudsman about unfair lending and loan collection practices was a major motivation for the development of these directives. Most of the complaints were in reference to non-transparent pricing and unfair market practices.

MFTransparency: Why did the Reserve Bank of Malawi decide to prioritize the issue of client protection and pricing disclosure?

Malawi Microfinance Industry at a Glance

Loans: **US\$62 million**

Active borrowers: **312,768**

Institutions reporting to MFTransparency: **10**

Source: **MFTransparency**

Deposits: **US\$31.5 million**

Depositors: **307,043**

Institutions reporting to the MIX Market: **9**

Source: **MIX Market**

¹ The Microfinance Bill was published on July 30, 2010 by the Reserve Bank of Malawi. The full text is available here: <http://www.rbm.mw/documents/mcsu/Microfinance%20Act%202010.pdf>

Mr. Lanjes Sinoya: Having received numerous complaints from the microfinance industry, the Reserve Bank noted that the most worrisome aspect of microfinance is failure on the part of the service providers to effectively disclose the cost of borrowing. It was therefore determined that the microfinance regulation will not be adequate if transparent pricing is not mandatory. In this regard, the need for microfinance service providers to provide borrowers with accurate, comparable and transparent information about the products/services on offer and the cost of their loans is perceived as one of critical elements for the development of the industry.

MFTransparency: What has been the process of developing these directives? How were different stakeholders involved in the process?

Mr. Lanjes Sinoya: The Reserve Bank, with technical assistance from a World Bank consultant, drafted the directives taking into consideration best practices and local operating conditions. The draft directives were then circulated to all stakeholders including microfinance service providers, the umbrella body Malawi Microfinance Network (MAMN), commercial banks, insurers, Malawi Law Society, UNDP/UNCDF, CGAP, Ministry of Industry and Trade, development partners and other interested stakeholders for their views and comments. We incorporated the preliminary comments into the draft directives prior to calling for a local stakeholders workshop for a face-to-face discussion. The comments which were considered valuable were again taken on board.

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MFTransparency: Has Malawi looked to any other countries for ideas in terms of regulating pricing disclosure in microfinance?

Mr. Lanjes Sinoya: When formulating the legal framework, tours to Uganda, Tanzania and Kenya were conducted. In addition, regulations for other countries like Namibia, Bangladesh, Bolivia, Peru, just but a few, were critically considered to tap on their experiences and best practices. All these formed basis for the laws and directives.

MFTransparency: What challenges did the RBM face in developing this bill?

Mr. Lanjes Sinoya: Some of the most substantial challenges we faced included how to customize the best practices of other jurisdictions to fit within our operating environment.

Implementation

Developing sound implementation strategies is equally important as the quality of the policy itself. MFTransparency spoke to Mr. Sinoya about the RBM’s strategy for addressing implementation challenges, including industry stakeholders and enforcing new requirements.

MFTransparency: What challenges do you anticipate for the implementation process?

Mr. Lanjes Sinoya: The main challenges that the RBM has identified relate to capacity. For some MFIs it will be difficult to acquire the necessary infrastructure for reporting on financials and

pricing. The bill will also impose a new regulatory burden on the part of the Reserve Bank – the need to regulate and supervise the industry is imperative. The Reserve Bank remains challenged in terms of staffing and skills to adequately supervise the numerous service providers in the industry. The mitigating strategy is to involve MAMN in enhancing best practices among its members. All MFIs will become affiliates to MAMN.

MFTransparency: The directives state in Section 1, No. 3 “Micro Credit Agencies shall, at all times, carryout fair lending practices. The contract between the lender and the borrower must state the nominal rate of interest as well as commissions and fees either on an annual or monthly basis.” How will this statement be enforced?

Mr. Lanjes Sinoya: The law requires that interest rate and all charges be displayed in the business premises. It also requires periodic reporting to the Reserve Bank of all charges levied on loan products. These will both be verified during on-site examinations.

The RBM has also established a consumer education unit to educate the masses on financial services and the need for clients to know full terms and conditions of financial services and products. The consumer education unit will also receive and resolve complaints between service providers and customers.

MFTransparency: What role will industry support organizations have in ensuring that this new policy is implemented?

Mr. Lanjes Sinoya: To expand upon the new responsibilities for MAMN mentioned above, the network will play the role of a self-regulatory organization (SRO) and monitor compliance to market conduct practices among its members. In order to do this MAMN will need to strengthen its code of conduct for its members. They will need to administer adherence to this code of conduct. MAMN will report any non-compliance to best practices to the Reserve Bank for enforcement.

Intended Outcomes

Moving forward, there are several areas in which the RBM hopes the Microfinance Bill will help institutionalize standards for best practices in terms of transparency, client protection and sustainability. The RBM also recognizes the need to adapt to feedback from industry players.

MFTransparency: What are the main intended outcomes of Malawi’s new microfinance policy framework?

Mr. Lanjes Sinoya: The intended outcomes of the new microfinance policy framework are as follows:

Microloan Products in Malawi

- 93% of loan products are for **business purposes**
- **Village banking** is the lending methodology used for nearly half of all products
- 80% of products have a **flat interest rate**
- 70% of products include **fees** and **compulsory savings**, and 91% of these charges are not disclosed on the repayment schedule
- **APRs vary** most among **NGOs**, with a minimum APR of 11.31% and maximum of 260.96%

Source: MFTransparency

- Promote best practices in the operations of the institutions so as to ensure safety and soundness of MFIs as well as market-based development
- Protect consumers from abusive, exploitative lending and other unfair market practices
- Instill governance and market conduct structures that promote confidence of the general public in the financial sector as a whole
- Create a competitive environment and level playing field that ensures market efficiency and fairness

MFTransparency: What best practices will the new policy framework institutionalize?

Mr. Lanjes Sinoya: With respect to pricing disclosure, the new bill stipulates requirements for full disclosure of information in a standardized format and on a regular basis, including interest rates and other charges.

MFTransparency: How do you perceive the reaction of the microfinance industry concerning these directives? Are there any particular areas that the MFIs might find difficult to follow?

“Striking a balance between what is ideal and what is realistic and appropriate within the specific market context is essential to success.”

Mr. Lanjes Sinoya: Overall, the industry has reacted positively to the directives while expressing reservations on provisions to do with pricing and disclosure. We hence anticipate MFIs will face challenges in terms of reporting. The directives require that MFIs provide periodic reports on their operations to the registrar, which requires an institution to have good management information systems in place. Currently most microfinance institutions have poor record keeping and management information systems, hence reporting and transparency may be a challenge. The Reserve Bank will, on its part, conduct training to all MFIs on call report completion.

The Reserve Bank, however, anticipates the need for some technical assistance in building the capacity of the MFIs, especially in the area of information communication. Above all, the initiative on transparent pricing needs a coordinated effort in terms of developing a framework for the industry that clearly stipulates how to keep all charges transparent. The Reserve Bank will make such a framework mandatory under the law.

MFTransparency: Do you have any advice for other countries who are considering implementing a similar act?

Mr. Lanjes Sinoya: Implementation of a law should go with concessions. However, the industry needs to adhere to good corporate governance, operate on a sustainable basis and follow best practices. Striking a balance between what is ideal and what is realistic and appropriate within the specific market context is essential to success.

Takeaways

The new pricing disclosure policy in the Malawi Microfinance Bill is a very ambitious step for a nascent market. The RBM has focused on many of the most important aspects for achieving the desired outcomes. There are several important areas of the RBM’s new policy framework to highlight as particularly innovative.

Engaging all stakeholder groups. The Reserve Bank of Malawi has made a concerted effort to involve a range of different stakeholder groups in the process of developing this new policy. We believe this is an essential component to implementing new policy. The needs and perspectives of different actors must be taken into account if the policy is to have a positive impact on the market overall.

Partnering with the network. RBM's decision to partner with the network MAMN will be a critical factor in the success of this policy. The local MFI network in a given country tends to have the most detailed knowledge of the day to day operations of the market and understanding of the needs and capabilities of their members. It is crucial for any policymaker to engage their local network for the purpose of preparing and training MFIs to adhere to new policy, in addition to consulting them in the policy development phase.

Disclosure requirements paired with education and training. One of MF*Transparency's* core beliefs is that pricing information must be delivered along with education and training. Transparency is only valuable if market players are informed, understand the information presented to them and therefore able to make effective use of the data available. The RBM also recognizes this, making appropriate provisions for education and training of MFIs as well as financial literacy programs for clients.

Learn from others but customize to your own market. The regulators of microfinance markets around the world face many of the same challenges, and do not have the opportunity to exchange experiences frequently enough. The RBM took into account the experiences of other countries in developing their own policy, yet ultimately tailored it to the unique characteristics of the Malawi microfinance industry. Finding this balance is essential for successful policy.

Specificity of disclosure requirements. The Malawi Microfinance Bill states that the loan contract must include the nominal interest rate, commissions and fees either on an annual or monthly basis. To enhance the value of this information, MF*Transparency* would recommend that the RBM require:

- Disclosure of both annual and monthly rates
- Disclosure of an effective rather than nominal rate
- A formula for calculating this effective rate
- Disclosure of security deposit requirements and insurance charges.

This additional level of disclosure would enhance the ability to make comparisons between loan products and to fully understand all the charges paid by borrowers. The RBM might also consider requiring a standard template for repayment schedules and loan contracts so that this information is easy to find and compare.

One of the main challenges we anticipate that the RBM will face in implementing this policy is resource and capacity constraints on the part of MFIs in terms of ability to comply. The Malawian microfinance market is still in a relatively early stage of development. Extensive technical assistance and training are needed not only to ensure effective implementation of the new Microfinance Bill but also the sustainable growth of the industry in general. MF*Transparency* recommends a phased approach to implementing this new policy, allowing for a thorough capacity building process on the path to pricing disclosure. In Malawi and elsewhere, this is an essential component of the long term institutionalization of standards for pricing transparency.

MF*Transparency* is promoting price transparency by educating stakeholders, promoting standards for disclosure and by publishing the true costs of microfinance products in a clear, consistent fashion. To learn more please visit www.mftransparency.org or contact us at resources@mftransparency.org.