Finding the balance: The role of mashonisas in the lending sector

By Brett van Aswegen

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Since the National Credit Act was tightened up a few years ago to lessen the level of over indebtedness in the country, the number of unsecured credit agreements opened per annum has reduced.

Brett van Aswegen, Wonga CEO

So this begs the questions. Has the need for credit diminished in line with the tightening in credit extensions and, if not, where are consumers going when they couldn't access the formal market?

What is a mashonisa?

To shed some light on these concerns, Wonga recently commissioned an investigation into the informal lending in South Africa. We wanted to understand the role mashonisas play in the credit market, how they operate, why people choose to use them and whether there are opportunities for formal lenders to compete with their informal counterparts.

Mashonisa is the colloquial term used to describe a community-based informal lender (loan shark) and, unsurprisingly, our research confirmed a number of negative stereotypes associated with these lenders. Interest rates, for example, are extremely high with between 30% and 50% charged regardless of the loan term. And, when non-payment is an issue, collection practices are sometimes severe and include intimidation, social shaming and the seizure of assets.

In light of these harsh practices, it's easy to imagine that these lenders are a last resort for borrowers who cannot access formal credit. However, our study found that this is often not the case. In fact, many borrowers claimed to be using both formal and informal credit at the same time. This is evidenced by the prevalence of mashonisas, who appear to be a widespread and socially embedded aspect of community life rather than a criminal underclass, preying on the weak and vulnerable. Based on our findings, there are as many as one mashonisa to every 100 households.

Speed and convenience

Rather than being unable to access formal credit, the reason customers choose mashonisas is linked to speed and convenience. They provide easy access to credit when cash is needed urgently, without having to go through the lengthy application and verification process undertaken by formal lenders. They often live on the same street as their customers, so quick cash is just a short walk away. The money is used to manage cash flow between paydays and relied on to fund essential immediate expenses, such as buying dinner for the family and paying for transport to work.

As a result of mashonisa's social embeddedness and their customer's reliance on them for access to emergency cash, it's naïve to assume that they can be regulated in a similar way to the formal market. Compounding this, we must also consider the significant economic impact of trying to shut down 40,000 jobs and the knock-on effect this would have on customers who rely on these cash loans to get by every month.

However, our investigation has made it clear that trying to reconcile the operations of formal and informal lenders would be almost impossible. For formal lenders, as a result of credit bureau enquiries, affordability assessments and cash disbursement fees, the costs associated with granting credit are high and pricing is capped well below what the informal market is charging. Informal lenders, on the other hand, lend to people in their communities who are known to them either personally or by reputation and compensate for any additional risk by charging very high interest rates.

Middle ground

We cannot ignore the impact the informal lending market has on customers' level of over indebtedness. However, further tightening of credit legislation for the formal lending market is not going to protect customers or solve the social debt burden. Rather, we may reach a tipping point where customers are pushed into the informal market compounding the issue of over indebtedness.

Instead, I believe there is a middle ground. We tend to take a very binary view of formal vs informal lending, but I believe there might be a business model that uses a shared economy approach to challenge this thinking. Think of it as an Uber of lending, where perhaps formal lenders can take advantage of the socially embedded nature of mashonisas to alleviate the hassle associated with disseminating loans, while allowing customers to benefit from the regulatory protections of the formal market and alleviating some of the financial risks these informal lenders face as a result of non-payment.

Although the parameters of this relationship are difficult to define, it's clear that mashonisas are here to stay. They are born out of a social need that regulation has not accounted for and therefore, rather than supressing or ignoring their existence, there needs to be a way of bringing them into the regulatory space. Encouraging relationships between informal and formal lenders could provide a valuable opportunity for them to combine knowledge, draw on each other's strength and formulate a more balanced model that serves all interests.

ABOUT THE AUTHOR

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