This is the first of three MBP Technical Briefs focused on natural disaster preparedness. This brief discusses techniques to prepare the microfinance institution and staff for a natural disaster; Brief No. 7 discusses client preparedness; and Brief No. 8 discusses donor preparedness.

Pre-Disaster Planning to Protect Microfinance Institutions[1]

WHY PLAN FOR UNEXPECTED DISASTERS?

The evidence is unambiguous: as microfinance institutions (MFIs) increase their capacity to plan for and respond to unexpected disasters, their vulnerability to these disasters goes down. MFIs operating in chronic natural disaster environments have put ever-greater resources into disaster preparedness and mitigation activities, and they have shown a significant improvement in the quality and speed of their response to natural disasters, greater ability to deal with clients' post-disaster needs, and smaller financial losses.

IS DISASTER PLANNING ONLY FOR CHRONIC DISASTER AREAS?

With increasing environmental degradation and climate change, areas that faced infrequent natural disasters in the past may experience more frequent floods, droughts, and hurricanes. Unprotected clients and MFIs devastated by a single crisis can be progressively undermined by subsequent crises. After a first crisis strikes, an MFI is at a critical juncture where staff can reflect—even briefly—on lessons learned and take initial steps to prepare for future crises. This brief identifies nine steps to prepare and protect MFIs before disaster strikes.

NINE STEPS TO PROTECT AN MFI AGAINST NATURAL DISASTER

The nine steps outlined below are designed to achieve two purposes: first, to reduce the impact of a sudden natural disaster on the MFI's portfolio and solvency, and second, to allow the MFI to respond rapidly and effectively when disaster strikes.

STEPS TO PROTECT THE MFI'S PORTFOLIO AND SOLVENCY

1. Identify the Potential Population at Risk and Undertake Financial Projections

In areas at risk for repeat disasters, loan officers can help MFI management create a "risk map" that identifies which clients (by location, type of activity, or type of shelter) are at extreme, moderate, or minimal risk in the event of a natural disaster. Once collected across all clients, the MFI can conduct a risk assessment, identifying where the vulnerability is greatest, and what percentage of the current loan portfolio is held by at-risk clients. This allows the MFI to estimate the potential effect of a natural disaster on cash flow and financial returns, should the at-risk clients temporarily halt repayments or request emergency loans. On the savings side, the MFI should identify the amount of liquidity required to provide the at-risk population access to voluntary or compulsory savings, assuming that loan repayment inflows in a disaster situation will slow to zero. These figures will help the MFI's management decide whether to increase liquidity reserves, to provision more for losses, or to change lending policies. One form of lending policy change, for example, is to aim for greater portfolio diversification, both in terms of geographic coverage and types of activity.

2. Update and Store Duplicate Client Records out of the Disaster Zone

Disaster response and post-disaster MFI recovery is often crippled by loss of client records. After the 2000 floods in Mozambique, for example, one MFI's records were displayed on CNN—as huge bricks of soggy, useless paper. In disaster-prone areas, records should be regularly updated, duplicated, and stored as far away from disaster zones as possible. At a minimum, MFI files can be stored in air-tight, durable, fire and water-resistant containers.

3. Create a Disaster Fund

The greatest problem facing an MFI after a sudden disaster is liquidity: loan repayments slow or cease, while clients request withdrawals of savings and emergency loans. (See Brief No. 5: "MFI Liquidity Problems after a Natural Disaster.") MFIs can easily be caught unprepared for the cash demands of these events, which can emerge over the course of only a few days. Donors are rarely able to move quickly enough to meet the immediate need of MFIs for cash. Therefore, some experienced MFIs have developed internal disaster funds that can be quickly accessed to solve (or at least reduce) a short-term liquidity crisis. Regardless of the structure, the key characteristic of these funds is immediate accessibility.

Internal disaster funds take several forms. Some funds are directly built into the clients' cost of borrowing: either through a fee, a set-aside of a percent of the loan amount, or a higher interest rate. These client-financed funds can be divided into those managed within the "group" structure and those managed by MFI staff.

A few more established MFIs have created central disaster funds as part of their operating budget. In Bangladesh, a country hit repeatedly by natural disasters, ASA has decided to set aside 10 percent of total income from 1999 onwards for emergencies, while Grameen Bank has held a disaster reserve fund of US$100 million. In addition, several Bangladeshi institutions have created disaster loan funds using external grants as seed capital. In some cases, these funds serve only one large institution (such as BRAC); in other cases, the funds serve a range of smaller MFIs (such as the 22 MFIs included in the CARE DLF).[2]

These three measures—assessing vulnerability, protecting records, and establishing disaster funds—all protect the MFI's portfolio from the unexpected.

PREPARATORY STEPS TO RESPOND QUICKLY AND EFFECTIVELY WHEN DISASTER STRIKES

In general, MFIs "muddle through" disaster response, with the result being slow response and poor results. Bangladesh's 20 years of experience—which have led from a shift from "muddling through" to rapid and efficient response—yields the six recommendations below.

4. Develop Disaster Policies and Procedures

A disaster response plan is an essential part of rapid response when disaster hits. Relying on the experience of the Bangladeshi MFIs, a good disaster plan addresses the following policy and product issues:

- Based on what criteria should loan officers decide whether clients' outstanding loans be rescheduled? Who is authorized to determine the repayment schedule? Should rescheduling take place on a branch-wide or case-by-case basis? Will interest continue to accrue on rescheduled loans? (See Brief No. 1: "Loan Rescheduling after a Natural Disaster.")

- Will clients in good standing be allowed to take emergency loans? With what restrictions and up to what level? Where will the MFI procure cash for emergency loans, and how will it be physically distributed to the clients? (See Brief No. 2: "New Loans after a Natural Disaster.")

- For MFIs that take compulsory savings, will clients be allowed to withdraw compulsory savings? If so, up to what level and with what restrictions for replenishing this account? Where will the MFI procure cash for savings withdrawals, and how will it be physically distributed to the clients? (See Brief No. 3: "Using Compulsory Savings for Natural Disaster Response.")

- Will the MFI provide any emergency relief activities to affected communities? If so, for what time period, with what precautions, and using what staff? If not, to what organizations can the MFI refer clients for emergency food, shelter, clean water, or medicines? (See Brief No. 4: "Non-Financial Emergency Services to MFI Clients.")

- If hurricanes or flooding are predicted, should the MFI make agricultural or livestock loans during that season? And if it does, should the MFI provide insurance for these higher risk loans?

Each policy should include some flexibility in its parameters: different types and sizes of disasters will require different levels of response, and even for a specific disaster, the effect on individual branches will vary. These differences may lead to dissimilar policies by area: for example, severely affected branches may have a longer rescheduling period than those that are only moderately affected. When developing the parameters for response, the MFI should undertake a "what-if" analysis to ensure that the MFI has sufficient resources to carry out the chosen policy for different levels of disaster, and to identify the effects of these policies on the MFI's financial standing.

5. Create a Disaster Mitigation Team

For small MFIs, all staff need to be prepared and alerted to respond in case of disasters. Larger MFIs may establish a disaster mitigation task force[3] made up of 8 to 10 mid-level and senior managers from across the staff. During normal times, the task force is responsible for the following tasks: (1) develop a comprehensive plan for disaster response;[4] (2) undertake pre-disaster projections for financial planning; (3) assign disaster response responsibilities by department; and (4) identify preventative measures to make the MFI less vulnerable to a sudden disaster. Once disaster strikes, the task force serves as a forum for the smooth flow of activities and information. Each task force member is assigned a disaster response task, such as communicating with branch offices to assess damages, liaising with donors and commercial banks, providing post-disaster accounting information, providing emergency services for staff or clients, and identifying and coordinating with emergency service providers.

6. Develop an Internal and External Disaster Communication Strategy

Between headquarters and field offices, communication systems based on traditional telephones, faxes, and modems may be damaged by disasters, while cell phones are more resistant to disasters. The MFI should invest in communication technologies that allow the head office and branch offices to communicate during and immediately following a disaster.[5] Within days of the disaster, the head office should collect information from each branch on the level of damage sustained by clients. This information will allow the MFI to determine what percent of clients are severely affected, moderately affected, unaffected, or still unreachable. This information will be critical for mobilizing emergency assistance and donor financial support, as well as for making accurate assessments of the impact of the disaster on the MFI's financial situation. Field staff should attempt to report on the loss of life to clients or family members; the incidence of injuries and disease; and the loss of homes, household assets, business assets, livestock, and business inventories. Based on these figures, the MFI can identify the percent of its branches that are severely, moderately, or lightly affected by the disaster, and plan an appropriate response.

Continuous field staff communication with clients is equally critical and plays a central role in assessing damages and keeping clients motivated, repaying, and working together for crisis recovery. In Bangladesh, MFI staff use boats to move clients to shelters, to visit clients surrounded by floodwaters, and even to maintain weekly meetings throughout the crisis. When roads are destroyed, staff may need to track down clients by foot. In less affected areas, all-terrain vehicles may be useful. Proper staff incentives should be developed to reward staff who make extra efforts to contact clients and keep the program intact, even when their own families may be affected by the crisis. Different programs have developed different types of incentives, such as special field allowances or additional salary or vacation time after the crisis.

7. Train Staff

Despite the best-laid plans, natural disasters frequently destroy communication and transportation links, leaving field staff cut off from the head office. These staff members must often make critical crisis-response decisions without input from the head office. Not surprisingly, those MFIs that have already communicated disaster policy guidelines to field staff, that have clearly defined chains of command, and that have created flexibility in management and decision making show the greatest effectiveness in responding to crises.[6] Therefore, the task force must not only create policies and procedures for crisis periods but also must train field staff for operating in a crisis environment. If immediate training is not possible, staff should at least be provided with clear written guidelines to follow if crisis strikes.

Field staff training should also include: (1) how to provide pre-disaster information to clients, including safe shelter locations to minimize injuries and to protect moveable assets and livestock; (2) techniques for working with clients during the crisis without damaging the MFI's "business" reputation; (3) techniques on managing and accounting for relief funds; and (4) ways to coordinate effectively with relief and emergency workers. In well-functioning disaster preparedness programs, field staff in disaster-prone areas are regularly briefed on disaster-response methods and the likelihood of forthcoming disasters, which they then communicate to clients.[7]

8. Open Discussions with Donors and Commercial Banks for Emergency Capital

Another obvious sources of emergency liquidity is the commercial bank sector. However, tapping into this source of funds requires a pre-existing relationship between the MFI and a bank, based upon the MFI's demonstrated financial responsibility. Donors also may have disaster response funds, but unless negotiated as part of a disaster loan fund relationship, they are likely to be inaccessible immediately after a disaster strikes. Again, accessing these funds is likely to require a pre-existing relationship with the donor. Overall, some combination of bank and donor arrangements may best match the MFI's disaster-response capital plan.[8]

9. Liaise with Early Warning Systems and Relief Organizations

Maintaining a disaster early warning system within an MFI is cost-prohibitive. Therefore, the MFI should identify which institutions track weather patterns and predict storms or floods. One member of the task force should be responsible for regular communication with early warning institutions so that the MFI is not taken by surprise. Access to e-mail and the worldwide web makes this task ever easier.

Second, the MFI should identify which organizations provide emergency services such as food grants, medical supplies and services, clean water, and temporary shelters and pinpoint their areas of operation. These relief services may be provided by private or charitable organizations, or by government units. If organizations are available to provide these emergency services, MFIs should not become involved in relief activities. By staying in regular contact with clients, MFI staff can then serve as liaisons to relief organizations. However, if no relief organizations can reach the MFI's clientele within days of a disaster (as may be the case in remote rural areas), then the MFI should identify where basic emergency supplies can be located—such as oral rehydration salts or water purification tablets[9]—and how they can be transported to affected areas. (See Brief No. 4: "Non-Financial Emergency Services to MFI Clients.") Although the MFI may need to have cash on hand to purchase these supplies, donors are often willing to subsidize the bulk of these relief activities.

Taken as a whole, the six steps above ensure that the MFI is forewarned about impending disasters and has the necessary elements—including a plan, trained staff, and sufficient financial resources—to respond quickly and efficiently.

CONCLUSIONS

These nine steps cannot fully prepare or protect an MFI from a natural disaster. But they can lessen the shock of the disaster on the institution and its staff, and hasten the return to normal MFI operations. This brief has not discussed specific steps MFIs can take to prepare and protect clients, which is an equally important issue for MFIs preparing for disaster. Client protection and preparedness are examined in Brief No. 7.

ENDNOTES

[1] This document draws on information presented in MBP papers, "Microfinance in the Wake of Natural Disasters: Challenges and Opportunities," by Geetha Nagarajan, 1998; "Bangladeshi Experience in Adapting Financial Services to Cope with Floods: Implications for the Microfinance Industry," by Warren Brown and Geetha Nagarajan, 2000; and "Disaster Loan Funds for Microfinance Institutions: A Look at Emerging Experience," by Warren Brown and Geetha Nagarajan, 2000 (all available at www.mip.org/pubs/mbp-def.htm under "Managing Risk").

[2] See Brown and Nagarajan, "Disaster Loan Funds for Microfinance Institutions: A Look at Emerging Experience," 2000, available at www.mip.org/pubs/mbp-def.htm.

[3] This terminology and approach comes from Grameen Bank's emergency operations approach, which is one of the most effective disaster response systems now in place within MFIs.

[4] The plan includes a set of disaster protocols—including special staff incentives, crisis communication, and chain of command during disaster situations. It also includes developing relationships with institutions that provide timely early warning.

[5] On a fee basis, MFIs can allow clients the use of cell phones to phone relatives after a disaster strikes. For small MFIs, this may provide sufficient financial incentive for them to invest in cell phones.

[6] Hasan, M. Emrul, "Effects and Implications of High Impact Emergencies on Microfinance: Experiences from the 1998 Floods in Bangladesh," South Asian Network of Microfinance Initiatives (SANMFI), Dhaka, 1998.

[7] Nagarajan, Geetha, "Microfinance in the Wake of Natural Disasters: Challenges and Opportunities," Microenterprise Best Practices Project, March 1998, http://www.mip.org.

[8] When disasters strike, local commercial banks may face capital and liquidity constraints similar to those of MFIs. In these cases, they are likely to be ineffective sources of emergency capital.

[9] During and after floods, access to clean drinking water is a major problem, and diarrhea is second only to drowning as a cause of death. Packets of oral rehydration salts and water purification tablets can keep microfinance clients and their families alive and healthy, avoiding a further slide into poverty. In addition, a healthy client can repay more quickly and will have greater loyalty to the institution.