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Timeline
2019

Sample Size
1102 mystery shopping visits

Research Implemented by IPA
Yes

Mystery Shopping Assessment of Credit Cost Disclosures in Uganda

Abstract

Uganda has made substantial advancements in financial consumer protection policy in recent years but understanding whether and how the financial sector complies with these new regulations can be a challenge. Working with Financial Sector Deepening (FSD) Africa and Financial Sector Deepening Uganda (FSDU), an IPA research team conducted an audit study of over 1,000 financial institutions in three districts of Uganda to understand current practices and compliance with existing consumer credit disclosure and transparency requirements from the Bank of Uganda and the Uganda Microfinance Regulatory Authority. Overall, the study found that information on product cost was not consistently provided by loan officers, that inexperienced borrowers received less information than experienced shoppers, and that printed materials were conspicuously absent during sales visits and did not comply with guidelines. Additional analysis of loan charges reported by commercial banks over a 15-year period also points to an increase in the use of non-interest fees on loan contracts, which aligns with the wide range of non-interest fees encountered by mystery shoppers.

Policy Issue

Financial products have the potential to help the poor, however in some cases financial institutions' commercial goals may not align with consumers' best interests, and their staff may not be incentivized to offer products most suitable to low-income clients. A lack of transparency and low-quality information provided by financial institutions might have negative consequences for low-income consumers. Previous research has found that financial institutions routinely fail to voluntarily provide information to clients about avoidable fees, especially to people lacking financial knowledge, and clients are almost never offered the cheapest product. Many clients, meanwhile, lack the necessary understanding of financial products to engage in sound financial decision-making. Less informed customers may not be able to navigate this territory to find products that best suit their needs. This research in Uganda contributes to a growing body of research on current practices in transparency of consumer finance products.

Context of the Evaluation

In 2011, the Bank of Uganda (BoU) introduced the Financial Consumer Protection Guidelines, which include obligations of financial institutions (including banks, finance companies, and other deposit-taking institutions) to be fair, reliable, and transparent. These guidelines require that financial service providers share information about products with consumers, including the total cost of credit; that they display prominently standard fees and charges at all its branches, in promotional materials, and any other communication channels which it uses; and that consumers are shown a Key Facts Document prior to taking a loan, among other guidelines.

In many countries, setting rules has been insufficient to ensure financial institutions comply with such regulations. Supervision of sales visits is considered critical to ensuring that the rules established are upheld in practice.

Details of the Intervention

Between July and August 2019, IPA conducted 1102 mystery shopping visits to lenders in Kampala, Mbarara, and Gulu to document loan officer conduct related to credit product disclosure and pricing transparency. Institutions visited were supervised by either the Bank of Uganda (BoU) or the Uganda Microfinance Regulatory Authority (UMRA).

For the exercise, mystery shoppers posed as regular customers and visited lenders unannounced in order to discover information about the loan application process without the credit officer knowing they were being observed, and thus avoiding impacting their normal behavior or practices. IPA recruited and trained shoppers fitting profiles reflecting typical Ugandan borrowers. Shoppers portrayed a range of personas and scenarios—limited versus advanced borrowing knowledge, business versus personal borrowing need, male versus female, and varying loan amount requests—to measure how such differences would impact the products shoppers were offered and the information disclosed by loan officers. The research team also analyzed publicly available data on cost of credit published by the BoU in order to complement its understanding of the findings.

Results and Policy Lessons

Preliminary Results:

Information on product cost, including interest rate and total cost of credit, was not consistently provided by loan officers

- Only 69 percent of loan officers provided information about interest rates without being prompted (98 percent provided it to shoppers who asked)
- Of those loan officers to who did provide the interest rate, 67 percent failed to explain it in detail to shoppers, including how it is calculated
- Only half of eligible mystery shoppers were informed of the total cost of credit

Inexperienced borrowers received less information than experienced shoppers, suggesting particular challenges for protecting consumers with limited formal financial sector experience, or less education.

- On average, loan officers disclosed 3.58 non-interest fees to experienced shoppers, compared to 2.97 non-interest fees to inexperienced shoppers
- 68 percent of experienced shoppers were given information on total cost of credit, compared to 12 percent of inexperienced shoppers

Printed materials were conspicuously absent during sales visits and did not comply with guidelines. All shoppers asked for a payment plan, and experienced shoppers asked for a key facts document using the term “summary document” to avoid suspicion. Shoppers were also directed to collect any printed materials they could find in the branch.

- Loan officers showed shoppers a payment plan in only 12 percent of visits, and mostly to experienced shoppers and small loan applicants.
- A key facts document was rarely (6 percent) shown in the first visit, even if asked for or hinted at by the shopper.
- Among institutions that had any leaflets available, less than 40 percent stated interest rates on their written materials.
- Contrary to BoU’s Financial Consumer Protection Guidelines, only a handful of printed materials which included interest rates were accompanied by the total cost of credit. In no case was the total cost of credit printed more prominently than the interest rate.

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