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Small Change

Is Microfinance capable of eliminating poverty and empowering women?

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Glossary

ADB	Asian Development Bank
BDB	Bank Dagan Bali
BDS	Business Development Services
BRAC	Bangladesh Rural Advancement Committee
BRI	Bank Rakyat Indonesia
CGAP	Consultative Group to Assist the Poor
IPO	Initial Public (Stock) Offering
JLG	Joint Liability Group
MFI	Microfinance Institution
MDG	Millennium Development Goals
MYRADA	Mysore Resettlement and Development Agency
NABARD	National Bank for Agriculture and Rural Development
NBFC	Non-Banking Finance Company
NGO	Non-Governmental Organization
PACs	Primary Agricultural Credit Societies
SBPL	Self-Help Group Bank Linkage Program
SEWA	Self Employed Women's Association
SHG	Self-Help Group
RBI	Reserve Bank of India
RFAS-2003	Rural Finance Access Survey 2003
RRB	Regional Rural Bank
UN	United Nations
US	United States of America

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Abstract

This paper begins with an introduction to the concept of microfinance and its historical provenance. The substantive part of this thesis revolves around the oft-made claim that microfinance is a panacea for poverty and the empowerment of women. The body of the text analyses this claim using theoretical insights and comparisons with other development tools as well as case-studies from India. By way of conclusion it is asserted that although microfinance has proven effective in providing financial services to a hitherto excluded population, it has been successful in effecting only a 'small change'. As of now, and by itself, microfinance remains incapable of providing a solution to global poverty and the emancipation of women.

Am Beginn dieser Arbeit steht eine Einführung in das Konzept der Mikrofinanzierung und ihres historischen Ursprungs. Der Hauptteil dieser Masterarbeit dreht sich um die oft geäußerte Behauptung, dass Mikrofinanzierung ein Allheilmittel gegen Armut und eine Stärkung von Frauen sei. Im Inhalt wird diese Behauptung anhand von theoretischen Einsichten und Vergleichen mit anderen Instrumenten der Entwicklungspolitik sowie in indischen Fallstudien analysiert. Zusammenfassend lässt sich festhalten, dass sich Mikrofinanzierung zwar als wirksam in der Bereitstellung von Finanzdienstleistungen für bisher davon ausgeschlossene Bevölkerungsgruppen erwiesen hat, aber nur in „kleinem Ausmaß" erfolgreich war. Unmittelbar und für sich genommen bietet Mikrofinanzierung keine Lösung für die globale Armut und die Emanzipation von Frauen.

Chapter 1. An Introduction to Microfinance

I. Introduction

Microfinance – the provision of loans and other financial services to those who have traditionally been denied access to the formal financial sector, has grown from an idea into an industry. Brought to the world's attention in 2006, when Muhammad Yunus and the Grameen Bank won the Nobel Peace Prize for "their efforts to create economic and social development from below"[1], the rapid growth of the microfinance movement across the developing world has spurred both accolades and accusations. Those who promote microfinance, consider it a powerful tool in poverty alleviation and women's empowerment.

In 1997, then United Nations (UN) Secretary General, Kofi Annan, declared that, *"Microcredit is a critical anti-poverty tool - a wise investment in human capital. When the poorest, especially women, receive credit, they become economic actors with power. Power to improve not only their own lives but, in a widening circle of impact, the lives of their families, their communities, and their nations."*[2]

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[1] Press Release – Nobel Peace Prize 2006. Available at: http://nobelprize.org/nobel_prizes/peace/laureates/2006/press.html. Last accessed: March 30, 2010

[2] The Global Development Research Centre website. Available at: http://www.gdrc.org/icm/iym2005/index.html. Last accessed: March 30, 2010

This thesis adds a question-mark behind Annan's declaration. On the basis of research and field work, using India as a case example, I will seek to explore the often inflated claims that microfinance is the most promising solution to global poverty and to raising the status of women in society.

II. Methodology and Structure

The microfinance industry currently finds itself at crossroads – delicately balanced between social intention and commercialism. It is my assertion that those who proclaim microfinance to be the solution to the world's problems give it too much credit. However, I do not question that microfinance and the resultant financial inclusion it encourages does bring about a largely positive change in the lives of the poor, provided it is employed in a socially responsible way.

To begin with, the thesis delves into a detailed literature review in order to establish the state of the art. The sources that inform the text include policy papers commissioned by the World Bank and the United Nations, personal interviews with microfinance personnel and clients, as well as full fledged publications on various aspects of microfinance. The substantive part of this thesis is buoyed by theoretical insights and empirical research.

Most of the literary sources that inform this thesis were available at the libraries of the London School of Economics and Political Science (LSE), the School of Oriental and African Studies (SOAS), the Economics University (Vienna) and the University of Vienna. Many of the articles and journals were sourced online. I was awarded a grant from the University of Vienna to

travel to London to work at the library archives there for one month. The grant also allowed me to make a field trip to India where I attended the Microfinance India Summit (October 26- 28, 2009) and then interned at PlaNet Finance India, a not-for-profit microfinance consultancy (Nov – Dec 2009). In the course of my visit to India I was also able to visit microfinance operations in villages across Karnataka, Kerala and Delhi. The details of these visits are chronicled in the fourth chapter of this thesis.

The text commences with a brief exploration into the history and origins of microfinance. Chapter two focuses on the 'state of the sector' and traces the development of microfinance in India. This is followed by an attempt to understand whether microfinance is in fact the surest stratagem to expedite the end of poverty and the empowerment of women, in chapter three. Further on, chapter four offers insights from field work and empirical research undertaken in India. And finally, the last chapter concludes the thesis, with a reflection on the brickbats and bouquets.

III. A Brief History of Microfinance

A. Tracing the Origins

Informal financial institutions catering to the poorer sections of society are documented as far back as the 15th century in Nigerian history.[3] In Europe they were first developed in the 18th century in response to the immense poverty engendered by the 30 years' war (1618-48).[4] The term microfinance was formally employed in academic literature in the 1980s.[5]

[3] Hans Dieter Seibel, *History matters in microfinance,* Working Paper in Small Enterprise Development – An International Journal of Microfinance and Business Development, Vol. 14, No. 2, 2003, 12

[4] Dirk Steinwand, *The Alchemy of Microfinance: The Evolution of the Indonesian People's Credit Banks to 1999 and a Contemporary Analysis,* Berlin, 2001:51. Cited in: *The Microfinance Revolution: Vol. 2 Lessons From Indonesia,* Marguerite S. Robinson, The International Bank for Reconstruction and Development/ World Bank Publications, Washington, DC, 2002: 96

The well known author Jonathan Swift began the first loan fund for the poor in Ireland, in 1720.[6] In 1823 a special law legalized the operation of such charitable institutions as formal financial intermediaries. The loan funds created under the auspices of charitable work began to return rich profits and served over 20 percent of Irish households as per conservative estimates[7], until the government reigned in these booming businesses by regulating the permissible interest rates.

The Raiffeisen credit cooperatives started in Germany by Friedrich Wilhelm Raiffeisen, in 1847, were famously meant to "control the use made of money for economic improvements, and to improve the moral and physical values of people and also, their will to act by themselves"[8]. By the year 1910, the cooperatives were servicing 1.4 million people.[9] The British introduced this German model in the Indian city of Madras in the 1880s and consequently more than 9 million Indians were part of a vast credit-cooperative movement by the mid-20th century.[10] Simultaneously, the Dutch colonial administration designed a rural cooperative banking system (the Badan Kredit Desas) in Indonesia, based on the Raiffeisen model, which later spawned the Bank Rakyat Indonesia, which is today one of the worlds largest microfinance institutions (MFIs).[11]

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[5] Marguerite S. Robinson, *Microfinance Revolution: Sustainable Finance for the Poor,* World Bank Publications, Washington, DC, 2001: XXX
[6] Robinson 2002: 96
[7] Seibel 2003a: 10, cited in: Ibid
[8] Freidrich W. Raiffeisen, *The Credit Unions, 8th edition*, Neuwied, 1966. Cited in: David C.Richardson. *Unorthodox Microfinance: The Seven Doctrines of Success*. Cited in: The MicroBanking Bulletin, Issue No. 4, 2000: 3-7
[9] Jonathan Morduch, *The Microfinance Promise*, Journal of Economic Literature, Vol. XXXVII , pp. 1569–1614, 1999: 1573
[10] Ibid: 1574
[11] Robinson 2002: 97

B. The Rise of Microfinance since the 1970s

Well into the 21st century, development has been driven either by governments or donor-financed credit programs. It is widely recognised that in spite of the high costs of administering aid driven initiatives, they have failed to make a significant impact on poverty reduction. Some critics also believe that charity has ruined the credit culture of the poor. From the 1950s, international aid donors and governments alike subsidized credit delivery to small farmers. The 1960s and 70s saw major efforts to expand rural finance in developing countries and Agricultural Development Banks were responsible for the delivery of this cheap credit.[12]

In much of the developing world after the colonial era, governments were misguided into implementing development strategies premised on 'supply-leading finance theory'[13]. This entailed the provision of loans in advance of the demand for credit, for the purpose of fostering economic growth.[14] These loans were heavily subsidized and suffered alarmingly high default rates, between 50 to 90 percent.[15] Often these loans were used as hand-outs by corrupt politicians to strengthen their vote-banks, while the credit-institutions continued to suffer financial losses due to the unsustainably low interest rates charged by them.

The provision of this subsidized credit was subject to the whims of governments and donors and the credibility and financial viability of these programs was often jeopardized when public funds were used to waive off outstanding loans at election time.[16] At any rate, access by the poor to these programs tended to be low due to the misappropriation of loan funds despite the subsidies, and the costs of borrowing high, because of widespread inefficiency and corruption.

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[12] Susan Johnson and Ben Rogaly, *Microfinance and Poverty Reduction,* Oxfam: London, 1997: 5
[13] Morduch 1999: 1570
[14] Robinson 2001: 140
[15] Ibid: 145
[16] Johnson and Rogaly 1997: 5

The mid-1970s saw trenchant criticism of this model with the consequence that donors and governments alike shifted focus from interventionist to market-based solutions.[17] The failure of the earlier attempts resulted in concerted interest in alternate development tools such as microfinance. The microfinance revolution of today is essentially a financial and technological revolution, which began in the 1970s, developed in the 1980s and took off in the 1990s.[18]

The Bank Dagan Bali (BDB) in Indonesia was started in September 1970 and is one of the earliest commercial microfinance institutions to serve a low-income clientele, without any subsidies.[19] In 1973 ACCION International, a United States based non governmental organization (NGO) disbursed its first loan in Brazil[20] and famously in 1974 Professor Muhammad Yunus started what later became known as the Grameen Bank by lending the modest sum of $27 from his own pocket to 42 people in Bangladesh. A year later the Self-Employed Women's Association (SEWA) started to provide loans of about $1.5 to poor women in India.[21] These institutions proved beyond doubt that poor people made good creditors, with repayment rates exceeding 95%, even when the interest rates charged were higher than those of traditional banks.

To begin with, microfinance was the exclusive domain of state driven and charitable aid.[22] Microfinance today is based on the principle of free markets, where resources are meant to be capitalized on. However, while on the one hand the Indian microfinance giant, SKS Microfinance is

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[17] More recently, economists from Ohio State University, such as Dale Adams and J. D. Von Pischke, have been vocal advocates of the view that provision of credit should be left almost entirely to the private sector. Ibid: 6

[18] Robinson 2001: 59

[19] Ali Wardhana, Introduction, pp. XVII-XXVII, in: Ibid: XXVII

[20] Avaliable at: http://www.accion.org/Page.aspx?pid=797 . Last accessed: March 31, 2010

[21] Ela R. Bhatt, *We Are Poor but So Many: The Story of Self Employed Women in India,* USA 2005

[22] Manfred Zeller and Richard L. Meyer (ed.), *The Triangle of Microfinance: Financial Sustainability, Outreach, and Impact,* London, 2002: 4

aspiring to an initial public stock offering (IPO), entirely self-sustaining MFIs are still far from the norm. It is generally agreed that while microfinance aims to become self-sustaining, governments still have an important role to play in terms of providing the opportune policy environment in which these institutions can flourish and be regulated. It is my contention that it would be presumptuous to assume that microfinance and free markets are a panacea for poverty.

At the Microcredit Summit (1996), held in Washington, US$20 billion was raised to provide micro-credit to 100 million of the poorest households of the world, in the next ten years. Writing at the time, Buckley[23] and Rogaly[24] questioned whether micro-credit was the best form of aid for the poorest. Critics argued that it constituted a large part of the aid budget and had diverted funds from other initiatives aimed at better healthcare, food aid or monetary aid, as the case may be, without having proven its success.

Often public subsidization of microfinance is justified on the grounds that it may be the most cost-efficient means of reducing poverty.[25] There are those that argue, and among them Yaron and Benjamin, that public works, rural infrastructure and human resource development are more viable alternatives to reducing poverty than targeted credit schemes for the poor.[26] Furthermore, it cannot be denied that among the very poorest lie the destitute, feeble, sick, elderly and orphans, who cannot benefit from microfinance and must be supported by governments and donor driven aid. Microfinance cannot effectively help all of the people, all of the time, and the crux of this thesis is to explore who lies within the gamut of microfinance clientele and who lies outside.

[23] Graeme Buckley, *Microfinance in Africa: Is it either the problem or the solution?,* World Development 25, 1997: 1081-1093. Cited in Ibid: 152
[24] Ben Rogaly, *Microfinance Evangelism, "destitute women," and the hard selling of a new anti-poverty formula,* Development in Practice 6, 1996: 110-112
[25] Zeller and Meyer, 2002: 13
[26] Ibid

IV. Literature Review

The 'microfinance revolution' has progressed steadily since the 1970s but there is a severe dearth of empirical academic literature on microfinance. Much of the writing is theoretical, anecdotal, or at worst, promotional. Of the three policy objectives of microfinance, namely financial sustainability, outreach to the poor and welfare impact, the last one particularly gets short shrift in the literature. "The period of consolidation and the move towards the perpetuation of MFIs has focused attention on issues of financial and institutional viability"[27], the evaluation of the roles of microfinance in poverty reduction is less elaborate. Loan size is often used as a proxy for evaluating the scale and impact of microfinance. However, it is universally agreed that at best, this is an imperfect substitute for judging impact. Presently most monitoring activities use simple but crude descriptions of project beneficiaries[28], although more comprehensive methods and indicators of assessment are being developed.

Debates on whether microfinance programs meet their goal of poverty reduction continue. "More recently these debates have been extended to the possible implications of such programs for women's empowerment, with some evaluations claiming positive results while others suggesting that microcredit leaves women worse off than before."[29]

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[27] Cécile Lapenu, Carla Henry, Manfred Zeller, and Manohar Sharma, *Un outil d' évaluation du niveau de vie des clients des institutions de microfinance,* 2004. Cited in: Bernd Balkenhol (ed.), *Microfinance and Public Policy: Outreach, Performance and Efficiency*, Basingstoke, England, 2007: 39
[28] Zeller and Meyer, 2002 : 11
[29] Naila Kabeer, Chapter 8. Conflicts over Credit: Re-Evaluating the Empowerment Potential of Loans to Women in Rural Bangladesh, in David Hulme and Thankom Arun (ed.), Microfinance, A Reader, London 2009: 108

Goetz and Sen Gupta use the five point index of 'managerial control' over loans as indicative of women's empowerment and find that most women do not fare well based on this criteria. Ackerly[30] notes that underpinning most credit interventions is an implicit assumption of the empowered woman. She substantiates, "Empowered, the borrower wisely invests money in a successful enterprise, her husband stops beating her, she sends her children to school, she improves the health and nutrition of her family, and she participates in major family decisions."[31] Her criterion of choice is 'accounting knowledge'. Women who could list input-costs for their loan-funded enterprise, its yield and profitability, were considered empowered in her study. Montgomery et al[32] considered 'management of loan funds' as a signifier for empowerment. Therefore, among their sample, the 9 per cent first time borrowers who were primary managers of loan-funded activities were more empowered, as compared to the 87 per cent who described their role in terms of 'family partnerships'. The authors reached the conclusion that joint management served to mask male-dominance in decision-making and therefore loans had done little to empower the women.

Naila Kabeer also elaborates on the examples of positive outcomes illustrated in the research of Rahman (1986), Pitt and Khandekar (1995) and Hashemi et al (1996). In each case, the studies conclude that women who participate in credit programs are better off than women who do not.[33] Dreze and Sen (1995) also found that women members of credit programs were less likely to be the victims of domestic violence.

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[30] Ackerly 1995: 56, Cited in Ibid: 109

[31] Ibid

[32] Montgomery, Richard, Debapriya Bhattacharya, and David Hulme. *Credit for the Poor in Bangladesh: The BRAC Rural Development and Employment Programme*, 1996. Cited in: Mark M. Pitt, Shahidar R. Khandekar and Jennifer Cartwright, *Does Micro-Credit Empower Women? Evidence from Bangladesh*, Policy Research Working Paper 2998, The World Bank Development Research Group on Rural Development 2003

[33] Kabeer 2009: 110

Contradictions in the literature are a result of using different methods, questions, interpretations and models, leading to conflicting conclusions about the empowerment potential or the poverty-alleviation potential of a certain program. Kabeer points out that some studies rely on statistical data and significance tests, while other rely on qualitative and anecdotal evidence. She also highlights the difference between 'average' and 'non-average' outcomes, concluding that Hashemi *et. al.*'s finding that access to credit leads to a reduction in domestic violence is perfectly compatible with Goetz and Sen Gupta's empirical observations that sometimes it exacerbates the same.[34]

It is also important to question the indicators used in empirical studies, which are often 'causality implicit'[35]. For instance, Ackerly's criterion of 'possessing accounting knowledge' does not automatically translate into empowerment as the author seems to imply. The terms in which empowerment outcomes are measured also offer limited frames of reference. For instance, while some studies highlight increase in household living standards or children's nutrition or the gender gap in education, others focus on women's political participation and bargaining power vis-à-vis men. While each of these outcomes registers a significant positive or negative effect, none of them present a holistic picture of the outcome of microfinance programs.

Finally, the differing interpretations of empirical findings often lead to wildly divergent conclusions on impact. For instance, Pitt and Khandekar interpret women's increased forays into market-oriented work as a positive step towards their empowerment, while Goetz and Sen Gupta and Montgomery *et al.* warn against the intensification of women's workload and fatigue, and interpret this as negatively affecting their empowerment. Kabeer observes that "Pitt and Khandekar interpret the higher level of household consumption expenditure associated with loans to women as

[34] Ibid: 112
[35] Ibid: 113

evidence of the greater weight given to women's preferences in household decision-making, while Montogmery *et al.* suggest that such findings demonstrate that loans to women are 'heavily compromised by the persisting responsibilities of women to cover the consumption needs of the family'"[36].

What is most conspicuous in the literature is the absence of women's testimonies and their own evaluation of the impact of microfinance programs o their lives. "Participatory impact assessment can help to enrich academic theorizations … be providing important insights into inequality as a 'lived experience'."[37] Of course, it is important to treat personal accounts with caution as the beneficiaries may have strong incentives to present the program in a positive or negative light.

[36] Ibid: 114
[37] Ibid: 115

Chapter 2. State of the Sector in India

I. Introduction

This chapter will explore the central tenets of microfinance in order to understand why it has emerged as the preferred development tool of our time. The focus remains on the microfinance industry in India, which will be discussed in some detail in this section.

Development strategies, the world over, have long suffered under the weight of institutionalism, bureaucracy and red-tapism and have manifested as misinformed, misused or misguided charity. Past policies to address poverty were based on the faulty premise that the poor are neither creditworthy nor able to save. The emphasis was largely on "giving and forgiving" loans.[38] These development initiatives involved credit transfers and have had a history of "doubtful coverage of the poor, with a never-ending need for injections of public resources to keep rural state-driven, top-down banks and cooperatives from collapsing"[39].

Much has been written about the fossilized nature of government banks in rural India and the failure of aid and charity worldwide. It is in this context that the UN, World Bank and thousands of NGOs and banks across the world are waking up to the potential of microfinance to address the malaise of poverty and inequality, realizing that easy access to credit is more important than cheap

[38] Manfred Zeller and Manohar Sharma, *Part I – Access to and Demand for Financial Services by the poor. Ch. 2. Demand for and Access to Financial Services by the Rural Poor : A Multi-country Synthesis*, in: Zeller and Meyer (ed.) 2002: 19
[39] Ibid

subsidized credit.[40] The solution to poverty and underdevelopment proffered by microfinance has therefore become accepted wisdom.

In the past fifteen years poverty-reduction has become an integral part of development paradigms: it has emerged as a World Bank objective in the 1990s and was adopted as one of the UN Millennium Development Goals in 2000. Just as poverty is not restricted to developing nations, neither is microfinance. Although it is most entrenched in parts of South Asia and Latin America, it is also being promoted in Canada, France, Germany, Ireland, United Kingdom and the United States.

"Microfinance has generated enthusiasm in the development community as well as politically – with the predictable result that some of its merits have been oversold".[41] In the following chapters this claim will be explored further, while trying to understand whether microfinance has made good on its social development objectives.

II. The Need for Microfinance?

The Reserve Bank of India (RBI) defines microfinance as "the provision of thrift, credit and other financial services and products of very small amounts to the poor in rural, semi-urban and urban areas for enabling them to raise their income levels and improve their living standards."[42] It also serves as an umbrella term for the provision of financial access, through focused financial

[40] I. Satya Sundaram, Microfinance in India, Delhi, 2007
[41] Ibid
[42] Avaliable at: http://www.rbi.org.in/SCRIPTS/FAQView.aspx?Id=7. Last accessed: March 31, 2010

intermediaries, to those parts of the population that are not being served by mainstream financial services providers.[43]

Today microfinance is not limited to the provision of micro-credit[44], it denotes short-term financial products for those who do not have access to these from traditional formal sources. These products include individual and group loans, savings services, facilities to encash cheques, payment orders, micro-insurance, loan-guarantees and the transfer of remittances from abroad. Marguerite Robinson contends that about 80 per cent of the world's 4.5 billion people living in low and lower middle income economies do not have access to formal financial sector services[45]. In another set of statistics, the Census of India 2001 states that only 35.5% of all Indian families own and operate bank accounts[46], thereby necessitating interventions such as microfinance.

A. Harnessing the Extant Bank Network in India

In the Indian context, especially in rural areas, there remains a vast lacunae in the availability of formal finance, and informal finance often comes tagged with extortionary terms or conditions of servitude. Following the bank nationalization drive started by Indira Gandhi in 1969, where commercial banks were required to open rural branches, India's banking network grew exponentially. Today India boasts of over 32,000 rural branches of commercial banks and regional rural banks (RRBs), around 14,000 cooperative bank branches, 98,000 primary agricultural credit

[43] Pramod Marar, Balaji S. Iyer, Unmesh Brahme, *HSBC brings a business model of banking to the doorsteps of the poor*, Journal of Organisational Excellence, Volume 28, Issue 2, 2008: 15-26

[44] Malcolm Harper (ed.), Microfinance: Evolution, Achievement and Challenges, London, 1999

[45] Robinson 2001

[46] With strong disparities between states – 24.2% in Orissa vs 72.8% in Goa

societies (PACS), 154,000 outlets of the post office network[47], as well as several other non-bank finance companies (NBFCs) and mutual fund sellers.[48] While the numbers seem impressive, it has been estimated that 70% of the marginal and landless farmers do not have a bank account and 87% have no access to credit from a formal source[49], leading to the conclusion that rural banks primarily serve the interests of the richer rural populace. From among the households surveyed under the RFAS-2003 (Rural Finance Access Survey 2003), over 90% reported that they funded unexpected expenses from cash at home, and the second most significant source was informal borrowing from friends, relatives and moneylenders. These statistics gave microfinance a vast playing-field, and taking heed of this potential, the industry has grown to serve over 70 million clients in India alone[50].

B. Why the Bank Network has Failed to Deliver

In order to understand why most Indians are unable to borrow from formal financial institutions, Basu and Srivastava[51] cite a combination of factors involving the banks and the clients themselves. They argue that the banks are wary of the repayment capacity of poor borrowers, their volatile income streams and incapability to provide collateral. The clients also make bad-borrowers as they typically avail of loans for consumption smoothing rather than investment in business and when the loans are for entrepreneurial purposes the poor borrowers often lack the technical/business skills and market information to make their businesses viable. Further, the transaction costs of rural loans are significantly higher since the loan size is usually small, there is widespread illiteracy among poorer clients and they are spread over a large geographical area.

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[47] Which facilitate deposit mobilization and money transfers.
[48] Priya Basu and Pradeep Srivastava, Scaling-Up Microfinance for India's Rural Poor, Research Working Paper 3646, The World Bank South Asia Region, Finance and Private Sector Development Unit 2005: 3
[49] RFAS-2003 survey, which covered 6000 rural households in Andhra Pradesh and Uttar Pradesh. Cited in: Basu and Srivastava, 2005
[50] N. Srinivasan, Microfinance India. State of the Sector Report 2009, New Delhi, 2010
[51] Basu and Srivastava 2005: 7

From the perspective of the borrowers, rural banks are unattractive for multiple reasons as well. As noted previously, the services offered by banks are not well suited to the non-uniform income patterns of the poor, compounded with the transaction costs and in some cases bribes to bank officials, banks begin to seem as tedious an option as usurious moneylenders. Borrowers also usually have to travel long distances from their villages to reach the bank, and alongside paying for the transportation cost, lose close to a day's wages due to the time spent travelling. Finally, bank loans take, on average, about 33 weeks to process[52], and are made out against collateral, making them unviable for poorer rural borrowers.

C. Drawbacks of Informal Finance

The RFAS-2003 report indicates that informal finance remains the mainstay of rural borrowers, where 44% of the households surveyed had borrowed from informal sources at least once over the past year and the interest charged on these loans averaged 48% per annum. Interestingly, while nearly half the loans were used to finance "family emergencies" and "social expenditures" (related to births, deaths, marriages etc.) and only 13% were used for investment related purposes.[53] The attractions of informal finance range from flexible repayment schedules to ease of access to the loans and less reliance on collateral. However, it was noted that in most cases where collateral was involved, landless and marginal farmers tended to pledge self-labour in lieu of other assets, thereby leaving them vulnerable to exploitation as bonded labour.

[52] Ibid: 9
[53] Ibid: 10

D. Harnessing Latent Potential from the Informal Economy

Until the 1980s, credit for agriculture was accorded high priority and the presence of informal micro-enterprises – street vendors, home workshops, market stalls, providers of informal transportation services etc. were perceived by policymakers and economists to be a result of economic dysfunction.[54] The typical profile of those operating in the informal economy include a scarcity of capital, non-legal status, operation in unregulated markets, labour intensive production modes, non-formal education and low skill levels, irregular work hours and small inventories[55]. While these traits formerly led to their exclusion from access to formal finance, commercial microfinance recognizes the profit-potential of the informal sector, which not only provides employment to millions in India, but is also an important contributor to the economy.

III. The Microfinance Agenda

To begin with, microfinance set out to address income and gender inequality by empowering poor women. In the course of time, the emphasis shifted to sustainability and outreach and lately, the core emphasis seems to have become profit generation.

Institutional microfinance started as a means of alleviating poverty and helping the poor to create sustainable livelihoods for themselves. Optimists argue that "microfinance seems to have squared the circle; this was an intervention that could not only alleviate poverty, but that could and should also pay for itself, be 'sustainable' and even make profits. Only in that way, it is argued, can it reach the millions who need it."[56] Against the backdrop of the global financial/liquidity crisis, the

[54] Robinson 2001
[55] Ibid
[56] Jackelen, Henry and Elisabeth Rhyne, *Towards a More Market-Oriented Approach toCredit and Savings for the Poor,* 1991. Cited in Harper 1999: 3

microfinance sector has stood firm and continually shown higher profits and weathered the global financial crisis better than many of the trusted institutions of mainstream finance.[57] The perception that catering to the poor is risky business seems to have firmly been proved wrong by microfinance.

Writing about the limitations of the post-Independence development initiatives in India, Uday Kumar rightly points out that "The experts and technocrats, who tailored development programs for such a vast country (India), failed to provide the necessary space for the involvement of the local community in the design, implementation and monitoring of such programmes."[58] Microfinance is poised well to infuse some democratic spirit into development initiatives, seeing as client satisfaction is the premise for its financial sustainability.

However, it is still debatable whether microfinance can make profits and pursue the social welfare agenda at the same time. Christopher Dunford of 'Freedom from Hunger' believes that these are irreconcilable aims. He argues that "profitability and growth are more likely to be achieved by offering more services to the same clients, rather than reaching out to new ones" and if this is achieved "the client profile will inevitably drift upwards and away from the poor, and what started like a businesslike activity with charitable goals will become no more than another profit seeking business."[59] The next chapter explores these themes in an effort to understand whether poverty alleviation, women's empowerment and profit-making are compatible aims for microfinance.

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[57] Hume and Arun 2009: 225

[58] Uday Kumar, *Ch. 23. From passive participation to effective leadership: a study on empowerment of women in Dakshin Kannada, Inida.* Cited in: Isabelle Guérin, and Jane Palier (ed.), *Microfinance challenges: empowerment or disempowerment of the poor?*, Institut Francais de Pondichéry, India, 2005: 325

[59] Harper 1999: 8

IV. The Two Models in the Indian Context

As of March 2009, over 1.716 million Self-help Groups (SHGs) active in India, represented over 54 million microfinance clients, while the MFI model, growing at a staggering 60 percent, served another 22.6 million. These two main models of microfinance in India are briefly introduced below.

A. Self-help Group- Bank-linkage

The SHG model, in the form of the SHG-Bank Linkage Programme (SBPL) was initiated in the early 1990s by the National Bank for Agriculture and Rural Development (NABARD). Self-help group linkage is based on the principle of 'savings first'[60]. These savings are not only a way of creating group solidarity and testing people's willingness regularly to keep some cash aside, but they also create a loan fund from which the group can borrow. Groups normally comprise of 15-20 women. Their savings and the accumulated interest the members charge themselves on loans may even make it unnecessary for the group to borrow from outside at all. Peer-pressure replaces traditional guarantees, such as references and assets or collateral. The existing network of government banks was harnessed to link the SHGs to credit channels, and having demonstrated the financial success of this endeavour, private banks are increasingly venturing into the field.

To obtain loans from banks, the SHG members must first establish their credit-worthiness, by maintaining scrupulous records of savings and mutual lending, usually for a period of six months. Further, the mechanism guards against defaults on loan payments, as no new member may receive a

[60] Ibid: 2

fresh loan until the previous arrears have been cleared. Another repayment incentive is the ability to access larger repeat loans upon on-time repayment. The loans proffered to the SHGs are usually a multiple (2-4 times) of their savings, and are granted to the SHG as a whole, which then decides autonomously on the disbursement among the members. It is argued that the meetings reinforce a culture of discipline, routine payments and staff accountability, while others counter the claim arguing that daily or weekly congregation compounds the workload of the borrowers and at times discourages new entrants.[61] There is also the assertion that the 'group leader' may wield undue control over loans issued to the other members.

While ideally, once members have managed to build up their assets, they should be able to operate individual accounts, this is not always the case. Critics of the SHG movement argue that poor people, given the choice, prefer an individual service and the simplicity of a reliable retailer managing the bookkeeping, rather than taking on the added responsibilities and risks of running their own mini-financial institution (SHG).[62]

Among the other drawbacks, SHGs entail a process of mutual self-selection, which may lead to the exclusion of the economically weakest members in a community. Further, it has been noted that repayment does not depend solely on peer pressure, there also needs to be management, transparency and accountability, which require a costly apparatus of training and supervision.

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[61] Johnson and Rogaly 1997: 8

[62] Jonathan Morduch and Stuart Rutherford, *Microfinance: Analytical Issues for India*, Cited in: Basu and Srivastava 2005: 26-27

B. The Microfinance Institutions (MFIs) - Join Liability Groups or Individual Liability

MFIs serve as 'lending intermediaries' between investors (banks/private equity firms) and the micro-credit borrowers. In India, they exist either as NGOs or as Non-Banking Finance Companies (NBFCs). The Joint Liability Group method was made famous by Grameen Bank in Bangladesh and has been replicated by MFIs across the world.

Under the JLG model, MFIs organize members into groups with the understanding that even though members will be given individual loans, the group as a whole will be liable for repayment. As in the case of the SHGs, social pressure ensures that repayment levels remains over 98 per cent in India. The size of the group is much smaller than an SHG with each group comprising of 5 women. Certain MFIs also lend to individuals with individual liability. In order to qualify for a bigger individual loan, members must have demonstrated good credit history over one to two years.

NGO MFIs often turn into NBFCs in India as this allows them to tap into commercial capital and expand at a much greater scale. However, the biggest drawback of NBFCs is that RBI regulations do not allow them to offer the much needed voluntary savings facilities. The advantage of the JLG model over the SHG model lies in the former's ability to scale. It is highly replicable and allows MFIs to rapidly expand their client base and become more profitable. In fact 30 percent of the 70 million microfinance clients in India are members of the top 10 MFIs.[63] Critics of the MFI/JLG model argue that high growth rate experienced by MFIs in India has translated into a mission drift with the focus shifting from client satisfaction to profit making. Some argue that this

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[63] Srinivas 2009

shift is inevitable, as social investors have been replaced by private equity and venture capitalist players.

V. Financial Systems vs. Poverty Lending

While commercial microfinance was coming into its own in the 1990s, there was a big debate between those that favoured the financial systems approach and others that espoused poverty lending. The financial systems approach emphasized large scale outreach among those capable of repaying loans and institutional self-sufficiency. The poverty lending approach tended toward reducing poverty through credit, coupled with other complementary services such as encouraging savings, skills training, literacy, numeracy, health and nutrition workshops, family planning advice etc. While clients were required to save in order to be eligible for loans, the system relied on government and donor financed credit, which was then on-lent to the poor at below-market rates. Elisabeth Rhyne points out that regardless of their affiliations, everyone involved in microfinance shares a common goal – "to provide credit and savings services to thousands or millions of poor people in a sustainable way"[64].

While the goal of poverty-lending is certainly laudable, there are some obvious drawbacks to it. First of all, governments and donors cannot indeterminately keep funding lending activity at less than market rates. Second, there is a higher demand for voluntary savings among the poor, than there is for incurring loans. While the Grameen bank of Bangladesh started out practicing poverty lending, they shifted to the more sustainable financial systems approach in 2001. Other pioneers of

[64] Elisabeth Rhyne, The Yin and Yan of Microfinance: Reaching the Poor and Sustainability, Micro-banking Bulletin, Vol. 2, No. 1, 1998: 6

this approach are the Bank Rakayat Indonesia (BRI), BancoSol Bolivia, MYRADA in India and the Association for Social Advancement (ASA) in Bangladesh.

As Robinson points out "Food is a universal need, credit is not. Not all poor people want or need credit." Viewed in this manner, it may be argued that donor funds can be utilized more fruitfully to tackle starvation, illness and unemployment, rather than provide loans to the poor. The balance, therefore, has tilted firmly in favour of the financial systems approach.

VI. Matters of Concern

A. Mission Drift

It would be foolhardy to believe that the involvement of banks and other financial institutions is simply altruistic. After all, microfinance has been recognised as an astute business opportunity, and herein lies another potential negative turn of events. There is an apparent shift in the focus of MFIs, from the philanthropic bent and missionary zeal to alleviate poverty, towards the hard-nosed business ethic of calculating success based on the financial bottom line. In an environment where the measure for success often-times remains the number of loans disbursed or the number of clients acquired, the poor often become casualties rather than beneficiaries. Malcolm Harper points out that poor people have always been prey to unscrupulous and recalcitrant moneylenders or other bogus savings institutions. Therefore, there is a very real risk that in the guise of genuine MFIs, swindlers or worse incompetent people may injure them even further.[65]

[65] Harper 1999: 4

B. Use of Loans

There is a latent assumption that micro-loans will lead to entrepreneurial and profit-generating activity, thereby perpetuating a virtuous cycle of poverty reduction. However, the reality is that a large portion of loans are taken for non-productive activities, such as weddings, funerals, dowries, roof-repair, subsistence etc. This is not to say that such activities do no merit loans, in fact, one of the primary merits of microfinance is that it makes the poor less vulnerable to destitution by making available these small loans. It may also be argued that by smoothing over the expenditure on food consumption of a farmer for instance, a micro-loan may allow him/her to work better in the fields, and is therefore eventually remunerative.

"The clients of microfinance institutions have always used some of their loans for purposes other than micro-enterprise investment. This may still be known as 'misuse' by some agencies but most providers of microfinance services are coming to realize that money is fungible, and that their customers probably know better than they do how to best use their money."[66]

However, a cautionary note must be added that when micro-loans are made available of for non-remunerative purposes, by an over-zealous loan officer to a financially-uneducated client, they may engender a spiral of further poverty. The State of the Sector (SOS) Report 2009 explicitly warns against such loans and recommends that the ability of the client to repay the loan amount must be established prior to the disbursement of the loan.

[66] Ibid: 2

C. Multiple-borrowing

Often when a borrower is unable to repay a micro-loan within the stipulated time, she may be forced to take another loan, from a different MFI in order to meet her commitment. The problem of multiple-lending has permeated most regions in southern India, where there is a high concentration of MFIs, and intense competition to woo the maximum number of clients. In such a scenario, it would be appropriate to cite Pischke's dictum that 'micro-credit is also micro-debt'.[67]

As MFIs expand and loan officer incentives are tied to client repayment, there may be a clash between profitability and sensitivity to client needs and circumstances. The most heinous consequence of taking a micro-loan and being unable to repay it was evident in the much publicized Krishna district debacle of 2006 where some farmers committed suicide due to the debt-burden. However, to the credit of the microfinance community, there is a concerted effort towards sensitizing field officers and higher management towards the needs of the microfinance clientele[68]. In fact, Indian NBFC MFIs have come together to initiate the formation of a 'credit-bureau' in order to avoid the cataclysmic consequences being repeated elsewhere. Most MFIs have some sort of procedure in place to re-schedule loan repayments in the face of genuine circumstances.

D. Quality Issues

There have also been allegations against the quality of MFIs in India, many of which suffer from weak governance and management structures, the absence of internal controls and the lack of financial discipline. This is particularly true of the many opportunistic start-up enterprises that are keen on cashing-in on the current microfinance boom. Attracted by the high returns that established MFIs have yielded for their investors, these start-ups are able to break even in a mere 18 months of

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[67] D.W. Adams, D.H. Graham and J.D. Von Pischke (eds), Undermining rural development with cheap credit, Colorado, USA, 1984

[68] Prabhu Ghate, Indian Microfinance: The Challenges of Rapid Growth, New Delhi, 2007

operation, at the risk of providing poor quality services and charging high rates of interest to clients[69].

E. Beyond Micro-loans

"Most business owners and managers, whatever the scale of their businesses, spend only quite a small amount of their time thinking about how to raise finance, or dealing with bankers, moneylenders, family members or others who may be able to provide it. On a day-to-day basis they are more concerned with making or buying things, and then marketing and selling them."

This observation leads us to two important conclusions, namely that microfinance clients need not just the financial input, but often-times more importantly they require business development services (BDS), skills-training, information about market conditions and access to markets. The second import is that besides simply procuring loans, clients also require other financial services, most significant among them insurance and savings.

After two decades of focusing on providing banking services to the poor, practitioners are now working towards 'livelihoods training', and teaching marketable skills and/or providing avenues for employment or marketing produce. The Microfinance India Summit 2009 was dedicated in part to re-conceptualizing the role of microfinance to tailor it to sustainable livelihood generation. There is definitely an awareness of these requirements among the leaders in the industry, but as of now, micro-insurance and savings constitute a meagre part of the microfinance efforts. It is important to point out that most MFIs at the helm of affairs lack the financial and administrative expertise to

[69] Personal interview with the Progam Officer at PlaNet Finance, November 23, 2009

execute these services properly. It is in order to fill this void that banks and insurance companies/agencies are required to enter into partnerships with MFIs.

F. Over-empowerment

Shahin Yaqub of BRAC[70] offers another interesting perspective when he writes that "poor people save and repay as instructed and work within the often inconvenient group mechanisms. When microfinance helps them to become less poor, they become empowered." He writes that, "Empowerment and virtue are not the same thing"[71] suggesting that in their empowered position, poor people are better able to resist not just unjust socio-political conditions, but also the legitimate claims of microfinance and are no longer willing to be subservient to the MFIs various procedural demands.

VII. Regulation of Indian MFIs

The Indian government mandates a policy where banks are required to direct 40% of their lending to the "priority sector" segment (including agriculturalists and other rural borrowers) of the economy. Banks have the option of subscribing to government issued bonds to fulfil this requirement, but more and more commercial banks are now financing microfinance loans, as these are more lucrative.

Two separate incidents, in recent years, that greatly embarrassed the Indian microfinance community have reinforced the need to put regulatory mechanisms in place. In the Krishna district of Andhra Pradesh the government shut down certain MFI branches after farmers committed

[70] Cited in Harper 1999: 9
[71] Ibid

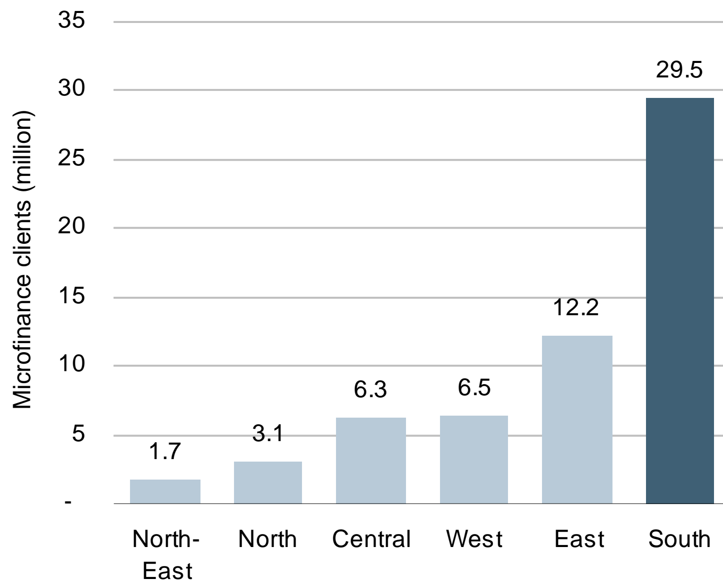
suicide due to indebtedness, while in Kolar district of Karnataka, the local Muslim leadership forbid Muslim women from repaying MFI loans, leading to large scale default with the crisis, spreading to non-Muslim communities as well. Interestingly, after the debacles in the Krishna and Kolar, the microfinance industry has become increasingly keen on establishing a regulatory framework, and a microfinance bill, pending in the parliament is eagerly anticipated.

Currently, non-profit MFIs in the form of trusts or societies are unregulated, while NBFC MFIs are regulated by the reserve bank. However, the reserve bank includes them under the broad spectrum of *all* Non-Banking Finance Companies. There are therefore no special regulations for the microfinance industry, an oversight which will hopefully be corrected by the microfinance bill.

VIII. The North-South Skew in India

There is a distinct regional imbalance in the access to financial services, whereby the most heavily populated and poverty stricken regions of eastern, central and north-eastern India have a disproportionately lower level of financial access. While these states account for 54 percent of the country's population and 40.5 percent of the total bank branches, they have only a 20 percent share in outstanding bank credit and 29 percent share of deposits.[72] The growth and spread of MFIs has reflected a similarly skewered trend, where the more prosperous southern states are nearly saturated, and the poorer states show a rather sparse presence of MFIs.

[72] RBI, Basic Statistical Returns,2002; RBI Handbook of Statistics, 2003; Census 2001, Cited in: Basu and Srivastava 2005: 6



Microfinance Clients by Region [Source: State of the Sector Report, 2009]

It must be noted therefore, that MFIs tend to operate in area of relative prosperity, leaving the poorest among the poor with limited options of access to finance. "It is no coincidence that successful, poverty oriented MFIs have flourished better in urban or high-potential rural areas with above-average infrastructure and market-access and where borrowers benefit from complementary public and private services that enhance the profitability of their loan-financed investment."[73] While topography and population distribution would seem to favour high efficiency among northern Indian MFIs, other factors seem to have an adverse impact, such as the relatively poor education quality of north Indian staff[74], scepticism of north Indian bankers regarding development agency motivations and differences in MFI management in the two regions.

[73] Zeller and Meyer 2002: 371
[74] South Indian States have among the highest literacy rates in the country.

The underlying causes for this include "the general malaise in the economy of the central, eastern and north-eastern states, with very little resultant demand for credit among the subsistence poor, and the absence (for historical reasons) of good quality NGOs that are willing to initiate microfinance programs in these states."[75] "This regional inequality may be matched by a 'quality gap'[76] where clients in low microfinance density areas may receive lower quality services at a higher price."[77]

The Asian Development Bank (ADB) 2007 report states that the impact of the region as a contributing factor to the southern MFIs' success is apparent. High level of literacy, high population density, efficient means of transportation and communication, the potential for marketing products, high percentage of migrants bringing in outside revenue, positive developments in old credit structures and forms of government intervention have led to the saturation of the southern states with MFIs. Another major reason why the south enjoys more leverage is that Karnataka was the breeding ground of MYRADA's experiment with SHG-Bank-linkage, a success story that was quickly replicated in the region.

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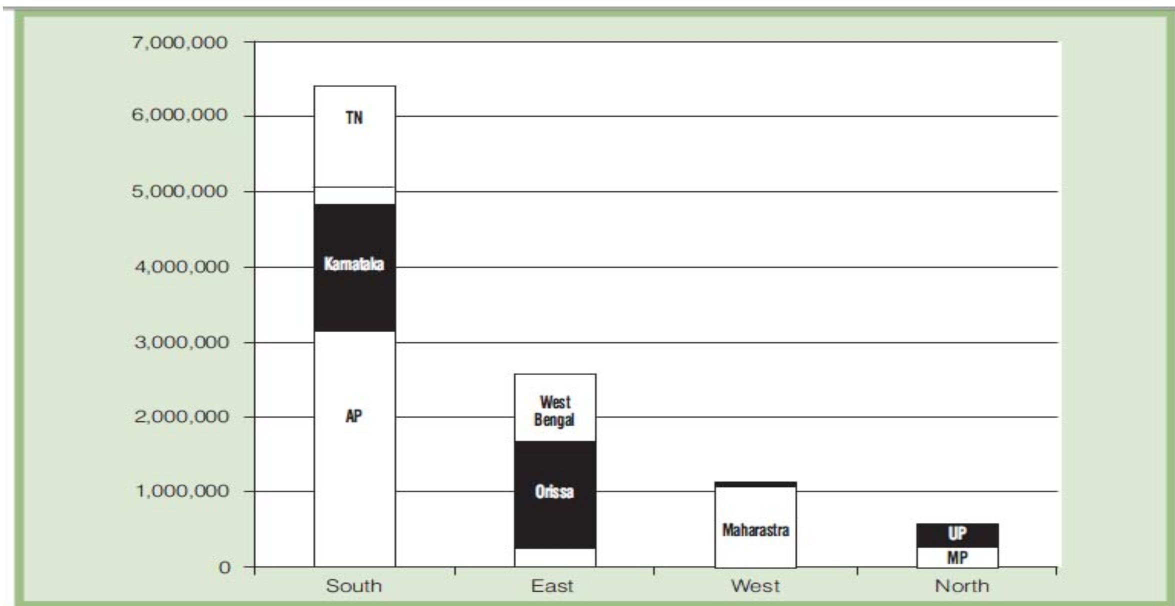
[75] Vijay Mahajan and Bharati Ramola, *Microfinance in India: Banyan Tree and Bonsai,* World Bank Research Paper 2003. Cited in Basu and Srivastava 2005: 26

[76] Elisabeth Rhyne and Maria Otero, *Microfinance through the next decade: Visioning the who, what, when, where and how,* Paper commissioned by the Global Microcredit Summit 2006, ACCION International, Boston, 2006

[77] Hulme and Arun 2009: 230

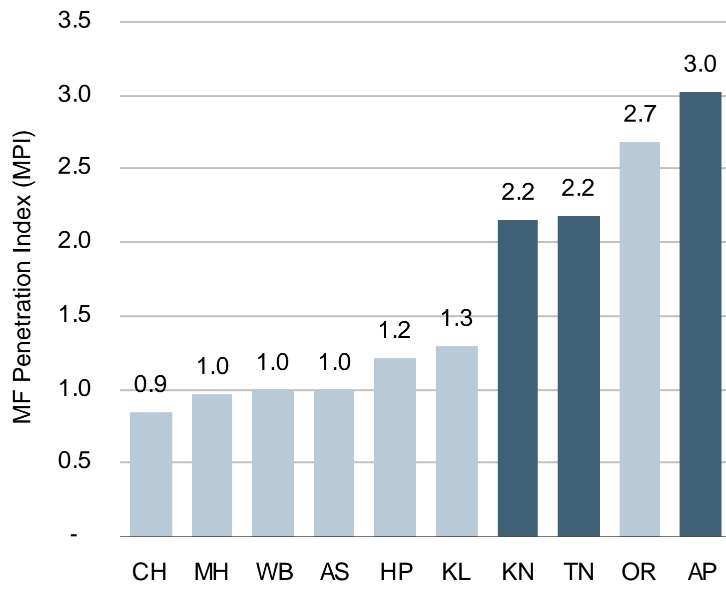


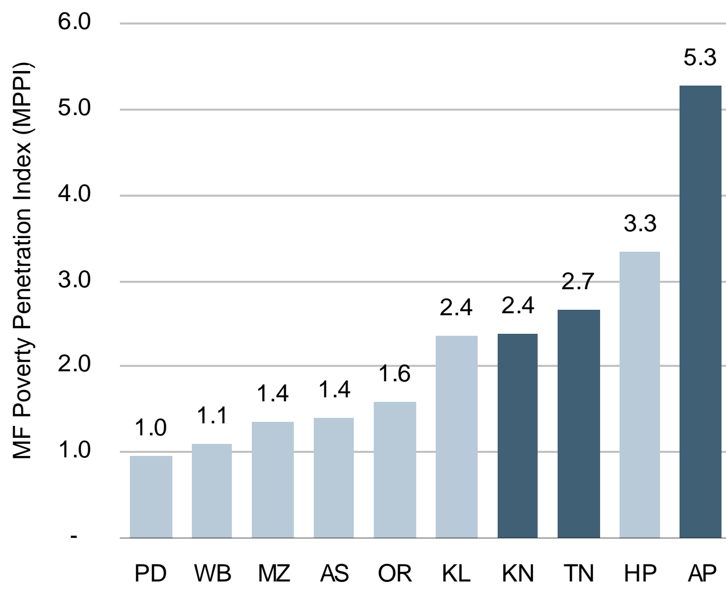
States (from bottom to top): South: Andrah Pradesh, Karnataka, Kerala, Pondicherry, Tamil Nadu, Tripura; East: Assam, Bihar, Chattisgarh, Jharkand, Orissa, West Bengal; West: Gujarat, Maharahstra, Rajasthan; North: Delhi Madhya Pradesh, Uttaranchal, Uttar Pradesh.

Source: Sa-Dhan Quick-Survey 2008.

State-wise Distribution of Clients, 2007/08 [Source: Dakshin Report, 2008]

The Dakshin Bharat Microfinance Report, 2008 (above) highlights the distorted regional distribution of clients according to the major states in India. As is apparent, the southern states of Tamil Nadu, Karnataka and Andhra Pradesh have the highest number of clients. The irony of the situation is depicted clearly in the following two charts reflecting the microfinance penetration index (MPI) and the microfinance poverty penetration index (MPPI), whereby the poorest Indian states are the ones that are least targeted by MFIs.





MPI and MPPI, in top ten Indian states [Source: State of the Sector Report, 2009]

Meyer and Zeller[78] suggest that in order to foster economic development "sequencing of investments is important and microfinance may better follow rather than precede investments in other critical areas, such as infrastructure, technology, human capital investments, agriculture research, and extension." Economic regeneration in these regions will require major development initiatives from the government, which would then stimulate livelihood opportunities and spur the demand for credit and other microfinance services.[79]

[78] Zeller and Meyer 2002: 373
[79] Basu and Srivastava 2005: 26

Chapter 3. Great Expectations

I. Introduction

The aim of this chapter is to analyze whether Indian microfinance makes good on its promise to address women's empowerment and poverty. Conservative estimates show that in India more than eighty percent of the microfinance clients are women, alerting us to the operation of a deliberate trend. It is within the scope of this chapter to examine why women are being exclusively pursued by MFIs, and whether participation indubitably leads to their empowerment? Pertaining to the second question, this chapter will examine whether microfinance has been (and indeed can be) successful in targeting poverty. In order to accomplish this I will first delineate the highly ambiguous category of the 'poor', and subsequently examine whether microfinance is the appropriate means for alleviating poverty.

II. Microfinance and the Poorest of the Poor: Shall the twain meet?

A. Identifying the Poorest

"Like many other development tools, microfinance has insufficiently penetrated the poorer strata of society. The poorest form the vast majority of those without access to primary health care and basic education; similarly, they are the majority of those without access to microfinance."[80] "Most authorities seem to agree that microfinance generally does not, and probably should not, directly reach the very poorest people. Practioners use phrases such as 'the economically active poor'

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[80] Jonathan Morduch and Barbara Haley, *Analysis of the Effects of Microfinance on Poverty Reduction,* RESULTS Canada for CIDA, 2001. Cited in Sam Daley-Harris (ed.), *Pathways Out of Poverty: Innovations in Microfinance for the Poorest Families*, Conneticut, USA, 2002: 5

to describe the clients whom their institutions actually do reach, and perhaps also to excuse their failure to match the exaggerated expectations that some enthusiasts and publicists for 'micro-credit'…have created."[81]

There are myriad ways of defining poverty, Johnson and Rogaly, among others, have come to acknowledge that 'vulnerability' to crises and income fluctuations and powerlessness, whether in an absolute sense or in relation to others, are important indicators of poverty. Sebstad and Cohen employ the most commonly used concept of the national poverty line to distinguish between the poor and non-poor. "The poverty lines of one and two dollars per day (in international 1985 prices converted to local currencies to ensure purchasing power parity) defined by the World Bank… have been established as yardsticks for measuring poverty internationally."[82]

"People living in extreme poverty exist below the minimum subsistence level; they include those who are unemployed or severely underemployed, as well as those whose work is so poorly remunerated that their purchasing power does not permit the minimum caloric intake required to overcome malnutrition. Also included are those people who live in regions severely deprived of resources; those who are too young, too old, or too disabled to work; those who for reasons of environment, ethnic identity, politics, gender and the like have little or no earning opportunities – and who have no assets or household members to support them; and those who are escaping from natural and manmade catastrophes." [83]

[81] Harper 1999: 7
[82] 1990 World Development Report in World Bank 2005: 68. In: Balkenhol 2007: 31
[83] Robinson 2001: 51

Those within the category of ‘poor’ may further be distinguished as ‘destitute’ (the bottom ten percent households below the poverty line – BPL), ‘extreme poor’ (bottom 10 to 50 percent households BPL), and ‘moderate poor’ (top 50 percent households in the BPL category). There is also a further category of the ‘vulnerable non-poor’, who are precariously placed above the poverty line, and may fall back under at the slightest instigation. Besides, it may be noted that often within the same poor households, there are degrees of vulnerability, and it is often the women and girls who bear the most hardships, and forego the most luxuries.

Poverty is multidimensional, it is relative and it is closely linked with vulnerability. “A dynamic analysis of poverty reveals that the most underprivileged are also those who are most exposed to the various risks of life and have the fewest means of coping.”[84] Balkenhol writes that chronic poverty increased due to the neo-liberal policies of the 1980s and that the related concept of ‘vulnerability’ should be understood as part of a larger social dynamic where it is recognised that “people facing mounting burdens are those who are the victims of determinism”[85] and that it is these people who should benefit from social policies such as microfinance etc.

Marguerite Robinson suggests that MF is not the ideal tool for those belonging to the lower brackets of poverty. In the following graphic she elaborates that micro-loans are only appropriate for those just above or below the poverty line, while the poorest of the poor still require welfare assistance and livelihood development training.

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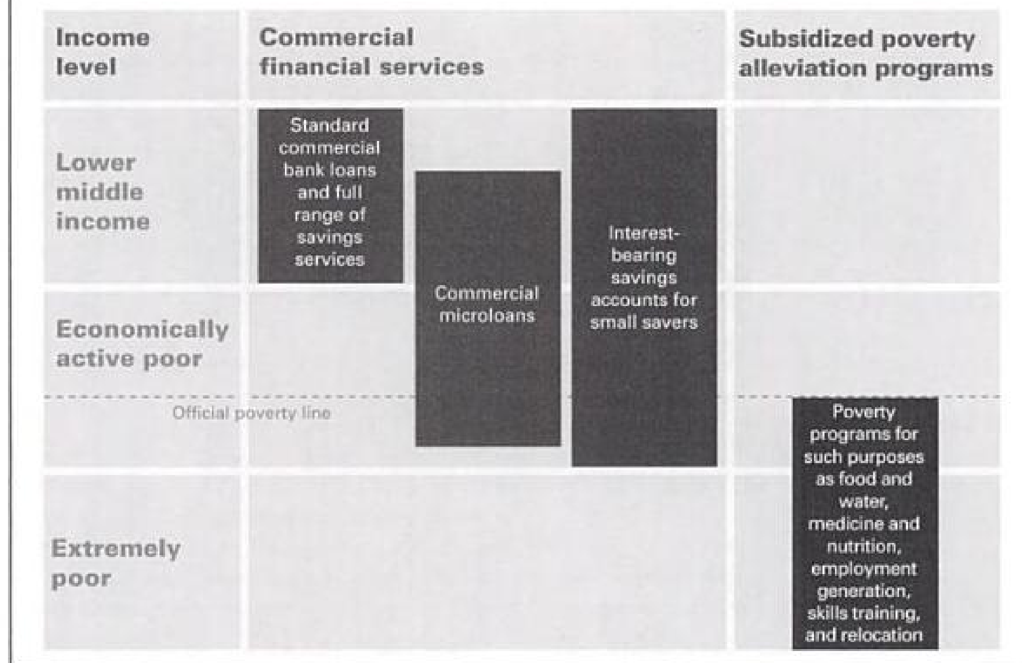
[84] Balkenhol 2007:30
[85] Ibid: 31



Financial services in the poverty alleviation toolbox [Source: Marguerite Robinson, page 54]

It is important to note that the fundamental cause behind insufficient income, the lack of access to education, health care, housing etc. may just as often be discrimination and marginalization. Diop, Hillenkamp and Servet[86] warn that even within a poor population there exists discrimination and pecking orders. They go so far as to suggest that by enabling some segments to improve their lot, microfinance initiative may be instrumental in reinforcing the domination and exploitation of those who are even poorer than them, reinforcing existing local hierarchies and inequality.

[86] Balkenhol 2007: 32

B. Terms of Engagement

Admittedly, to date there has been inadequate exploration of financial products and low-cost service delivery mechanisms that would allow MFIs to include extremely poor households without compromising their sustainability objectives.[87] However, it is my contention that the lack of access to financial services is just one defining aspect of the poor, among others such as illiteracy, poor health and nutrition, higher mortality, lack of political participation etc. It cannot be mandated as the root cause of poverty, and so by addressing this lacuna, microfinance cannot hope to achieve the alleviation of poverty. It is important therefore to understand how exactly microfinance *can* address the issue of poverty alleviation.

The Consultative Group to Assist the Poor (CGAP) contends that, "For micro-credit to be appropriate, a pre-existing level of ongoing economic activity, entrepreneurial capacity and managerial talent is needed. If not, then clients may not be able to benefit from credit, and will simply be pushed into debt". [88] There exists the latent supposition that borrowers must have an existing micro-enterprise to be able to absorb and repay a loan. However, this distinction between the 'economically-active' and 'non-active' poor is an artificial divide, since all sections of society are perforce economically active, i.e. involved in the relations of buying, selling, producing etc, thus exposing the weakness of this argument. An EPW Research Foundation report[89] iterates that not only do the poor indulge in the necessary activities of sale, purchase, exchange and production, they also save. In fact 74% of the poor in India save, as opposed to 83% of the non-poor, revealing that the difference is not so vast. [90]

[87] Daley-Harris 2002: 16
[88] Ibid: 45
[89] Economic and Political Weekly Research Foundation Report, 1994-95. Cited in: Guérin, and Jane Palier 2005: 349
[90] Ibid : 350

Simanowitz and Walter write that poverty reduction is in part a process of increasing income and economic stability, which leads to improved fulfillment of basic needs and access to services, as well as the development of a range of assets that will reduce household vulnerability to physical, economic, and social shocks.[91] Sebstad and Cohen delineate these assets as: "financial (income size, regularity and security, savings, loans or gifts), human (skills and knowledge, ability to labour, good health, self esteem, bargaining power, autonomy, and control over decisions), physical (housing, land, productive and non-productive possessions, and so on), and social (networks, group membership, relations of trust, access to wider institutions of society, and freedom from violence).[92] Microfinance may be instrumental in accumulating many of these assets - however, in the instances where an individual or community has been politically and socially marginalized or historically persecuted, (such as the caste system or the ostracisation of lepers in India) financial services by themselves are a rather blunt weapon.

Therefore, financial independence is simply one step. Other traditional constraints continue to operate upon the poor– such as traditional beliefs, matrimonial systems, caste membership etc. Realistically, microfinance alone cannot eliminate poverty, or transform social relations and the structural causes of poverty. What access to microfinance can do is target economic poverty and enable clients to seize opportunities for investment in business or other gains, smooth or increase consumption, meet life-cycle needs (birth, marriage, death, school-fees, retirement etc), and tide over crises and emergencies (illness, death, accident, fire, crime, weather etc).[93] Action is needed on many other fronts, including social safety nets, education, health services, social inclusion and sound macro-economic policies. There is "evidence of strong synergies between microfinance and other

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[91] Daley-Harris 2002: 20
[92] Sebstad and Cohen, *Ch.15. 'Microfinance'*, in Daley-Harris 2002
[93] Ibid: 22

poverty reduction interventions"[94], Daley-Harris contends that "the impact of each can increase when they are delivered together"[95]

There are those that argue that the very poor should be recipients of government or donor-funded development services, not micro-credit. I am inclined to agree with the view that business-oriented microfinance institutions cannot by themselves shoulder the task of poverty alleviation.[96] Market-led approaches tend to serve the profit-motive before any social goals, and therefore MFIs would likely target clients that demand larger loan sizes, in geographies that are better developed and offer more business opportunities. This process can be noted in the North-South skew of Indian microfinance, where the more prosperous southern states are better served by MFIs. The argument therefore, must be tweaked to say that "it is not good enough to wait for the market to serve the poor and very poor"[97]. As more and more commercial financial institutions, banks etc. get involved in microfinance, the pressure for making profits escalates. "This can dilute or even totally eliminate the original welfare objectives that prompted the founders and funders of the institutions."[98]

Hulme and Mosley demonstrated in their research that "the better-off the borrower, the greater the income from a micro-enterprise loan." Accepted wisdom in the microfinance community is that borrowers who already have assets and skills are able to make better use of credit, while the poorest borrowers leave themselves vulnerable to higher risks where business failure would likely provoke a livelihood crises due to the absence of a secure asset base. In their research, Hulme and

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[94] Jonathan Morduch and Barbara Haley, *Analysis of the effects of microfinance on poverty reduction*, New York University, Wagner Working Paper, No. 1040, 2002
[95] Daley-Harris, 2002: 29
[96] Robinson 2001
[97] Daley-Harris 2002: 18
[98] Harper, page 6

Mosley[99] found incidents of bankruptcy, forced seizure of assets, unofficial pledging of assets to other members of a borrowing group, and even reports of suicide due to peer pressure to repay failed loans. Marguerite Robinson nails the argument when she writes that, "Starving borrowers will use their loans to buy food for themselves and their children. Such people do not need debt. For these people, microfinance is the next step – after they are able to work."[100]

In recognition of these factors, microfinance theorists increasingly view improvements in economic security (implying income protection rather than income generation) as the first step in poverty reduction.[101] "Access to reliable, monetized savings facilities can help the poor smooth consumption over periods of cyclical or unexpected crises, thus greatly improving their economic security"[102] and once this is achieved, access to credit may help these people out of poverty by improving the productivity of their enterprises or creating new sources of livelihood. However, on the ground, MFIs are often guilty of forcing loans upon unwitting borrowers, and gradually increasing loans at that – which lead the poorest clientele to either avoid joining these programs, or forces them to withdraw.

Simanowitz and Walker suggest, rather mordantly, that "there are norms in society that lead to the poorest being regarded as inadequate and incapable of achieving", and by not adopting a specific poverty-focus MFIs tend to reflect these patterns of marginalization, which are also reflected in the self-perceptions of the poorest, and the perceptions of the wider community, including the MFI staff and management and the microfinance industry.[103] While I would be loathe

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[99] David Hulme and Paul Mosley, *Finance Against Poverty, Vol. 2,* London, 1996: 120-122
[100] Robinson 2001: 46
[101] Jean Dreze and Amartya Sen (ed.), *Hunger and Public Action,* Oxford, England, 1989
[102] Lynn Bennet and Carlos E. Cuevas, *Sustainable Banking with the Poor,* Journal of International Development, Vol. 8, Issue. 2, 1996: 145-152. Cited In: Johnson and Rogaly, 1997: 12
[103] Daley-Harris 2002: 39

to fully endorse this view, it is important to note that this could be one consideration that drives MFIs away from serving the poorest among the poor.

Simanowitz and Walker have identified that MFIs with a focus on poverty-targeting may incur higher costs. To begin with, developing and initiating such a program by understanding the demands of the very poor would cost staff time and money. Since poorer people often live in more remote and inaccessible locations this results in added operational costs. Once these clients have taken loans they are likely to generate less income and at the same time require more support. Also, creating more flexible products and adding allied non-financial services, as business development services (BDS) or skills-training, are essential for poverty outreach, however at the same time these services are costly and complicated to implement. Ana Marr concludes that "the task of harnessing local information and reducing poverty is an intrinsically intractable and complex issue; it does not appear that it can be safely entrusted to organizations run entirely on a commercial basis"[104].

C. Modes of Exclusion

There are other ways in which the poorest among the poor may be excluded by MFIs, formally or informally. Formal exclusion is the result of a scenario where the MFI narrowly defines the target focus, formally excluding all those below a certain income-level, or those lacking certain skills.

Informal exclusion, on the other hand, may occur in the form of self-exclusion, where the extremely poor are reluctant to join MF operations due to an aversion to risk or lack of self-confidence or in the form of exclusion by other members. Since the poorest are likely to be the least

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[104] Ana Marr, *Microfinance and Poverty Reduction: The Problematic Experience of Commnal Banking in Peru,* SOAS Working Papers 122, London, UK, 2002

vocal and least likely to express their needs within the program structure or through market research. Informal exclusion may also be practiced by the MFI staff, who are mostly only concerned with credit discipline and ensuring repayment and for this reason may target wealthier clientele or those with more stable occupations.

MFIs may also insist on compulsory borrowing or an increase in the size of repeat loan, as part of their program design, while not taking into consideration the borrowers' ability to repay. In such cases clients may be forced to exit the program. Clients may also voluntary-exclude themselves from participation if they are uncertain of their ability to take on debt. In other cases, clients may lack access to business opportunities due to a lack of skills, input, market and demand. In such cases the 'worse off' become more worse off as a result of failed businesses, leading to a livelihood crisis, and eventually exit from the microfinance program.

There has been much speculation about the negative impacts of microfinance, among them accumulated indebtedness, business failure, conflicts in the family arising from women's newly found economic independence and increasing work-load for women clients. However, most assessments of microfinance projects, including the AIMS[105] assessment reports and the World Development Report[106], detail generally positive or neutral impacts. Simanowitz and Walker point out that impact assessment is carried out only among existing clients and "where there is a high rate of exit, there are large numbers of former clients who are eliminated from the impact assessment."[107] A study conducted by SHARE[108] indicated that the MFI had a 17 percent rate of client exit. Among

[105] Assessing the Impact of Microenterprise
[106] Cited in: Anton Simanowitz, Client Exit Surveys: A Tool for Understanding Client 'Drop-Out, Journal of Microfinance 2, No. 1, 2000
[107] Daley-Harris 2002: 31
[108] One of the leading Indian MFIs

those who left, most cited failed business ventures as the reason (41%), many others felt that their incomes had remained the same or actually decreased after joining SHARE (33%), and a small percentage reported that they had perceived no benefits of their participation in the program (6%).

An internal study conducted by one of the largest MFIs in India, in regions with the highest percentage of client exits, found that the main reason for borrowers dropping out of the system was a perceived lack of need. This may seem counterintuitive since microfinance is based on the premise that as businesses growth, there is a greater need for working capital and so loan sizes increase over time. However, it was found that the vast majority of borrowers who exit do so because they do not use the loan for income generating purposes but to fulfill a temporary need such as expenses for a wedding, sickness in the family, roof repair etc. and once that need is fulfilled, they choose not to continue to borrow from the MFI.

D. Ground Realities

The microfinance industry takes a lot of credit for what it is doing, and yet, despite all these years of microfinance activity, we are yet to see any measurable form of impact. Many view access to financial services as an end itself, when in reality, microfinance is supposed to be a means to an end – with the end being affecting positive change in the lives of clients.

"From the beginning of this century, MFIs have moved beyond 'minimalist lending' to the poor to microfinance quality enhancement and risk diversification through the development of micro-insurance schemes to protect clients against the risks that can lead them further into

poverty."[109] This shift of focus means that the challenge of reaching out to the poorest still remains unmet due to high risks and costs. There is scattered evidence to suggest that sustainable microfinance can reach and have an impact on the poorest clientele, however there are challenges and limitations to the realization of this goal.

Stanton, based on her research of rural Mexican lending institutions concludes that be it state owned, private commercial finance, or informal private lenders, the clientele served excludes the very poorest[110]. Such a situation is not only borne out of the institutions concern for profits. Rather, the clients themselves weigh the perception of costs and benefits of taking a loan, including the transaction costs, time spent and the eventual probability of the loan being sanctioned, and decide against participating in a lending program. It is important to note that in this regard, faulty program design, as well as the perception of inaccessibility are together responsible for the poorest excluding themselves. However, Sharma and Buchenrieder conclude that microfinance may benefit the poor largely by smoothing their consumption through borrowing or improved management of their savings.[111] Harper argues against the conventional wisdom, that MFIs must realize that the poorest may be the most profitable clients since they are willing to work in groups, rather than deal with extortionary moneylenders and less empowered, therefore less likely to default on repayments.

E. Group Dynamics

Simanowitz argues that while "groups have the potential to facilitate skills development, building of confidence, and social networks, group liability conditions often serve to undermine this

[109] Tara Sinha and Lionel Siriwardena, Ch. 19. Poverty Reduction that Works, The VimoSEWA Self Employed Women's Association Microinsurance Programme, India, In: Paul Steele, Neil Fernando and Maneka Weddikkara (ed.), Poverty Reduction That Works: Experience of Scaling Up Development Success, London, 2008: 319

[110] Julie Stanton, *Ch.4. Wealth and rural credit among farmers in Mexico : is market participation consistent with targeting?,* In: Zeller and Meyer 2002

[111] Ibid: 6

positive potential of groups and lead to a more coercive and conflictual environment that discourages the participation of the very poor". Further, Fisher and Sriram (2002) iterate that just because a group of poor women together run a 'saving-and-loan club', they do not become immune to the corrosive effects of poor management, confused accounting, capture of assets by the leadership and other kinds of abuse.[112]

III. Microfinance and Women: Is microfinance synonymous with empowerment?

There are multiple reasons for targeting a primarily female clientele, depending on whom the question is addressed to the answers will range from 'they make better debtors', 'they are more compliant, reliable and easier to reach', to 'they have persistently remained the most vulnerable among the poorer sections of society.' In India this second dimension has a major significance, and the evidence is that women are poorer, more disadvantaged and marginalized than men. The last census demonstrates that the sex ratio continues to worsen to the detriment of women.[113] The Second National Family Health Service conducted in 1998-99 "finds that the average woman in India is disempowered absolutely as well as relatively to men, and there has been little change in her disempowerment over time."[114] Most significantly, these disempowered women are conditioned into believing that men are superior to them and often they have little or no agency, even with regards to their own health or mobility. Guerin and Palier have found that only one in three women can go to the market without their husband's permission and only one in four may visit relatives or friends without permission.[115]

[112] Basu and Srivastava 2005: 23
[113] Guérin, and Palier 2005:347
[114] Ibid
[115] Ibid

Most microfinance programs are aimed at women clientele since studies showed that they make better, more reliable borrowers. Other concerns such as the view that women are more likely than men to be credit constrained, have restricted access to the wage labour market, and have an inequitable share of power in household decision-making are legitimate reasons for targeting women[116], but it is evident that these are not the main considerations for most MFIs.

A. Feminization of poverty

Empowerment has become a key word in the discourse on development. The universality of the concept has repeatedly been criticized in development and feminist literature, because empowerment is an inherently dynamic, malleable and relative term.

Since the 1990s, Amartya Sen's seminal article on inequalities[117] has shaped the trajectory of development strategies. In 1995, the UNDP introduced two new 'gender-related indices' of measuring development – Gender-related Development Index (GDI) and Gender Empowerment Measure (GEM). The indicators highlighted that women are poorer and indeed, much more vulnerable to poverty then men, leading therefore to the feminization of poverty and the focusing attention on the need to target development schemes towards women. Microfinance, in this regard, is one more in a repertoire of such efforts. However, this interest in the gender-dimension of poverty is not sufficient to explain why MFIs prioritize or even exclusively focus on women.

[116] Mark M. Pitt, Shahidar R. Khandekar and Jennifer Cartwright, Does Micro-Credit Empower Women? Evidence from Bangladesh, Policy Research Working Paper 2998, The World Bank Development Research Group on Rural Development 2003: 1

[117] Amartya Sen, *More than 100 million women are missing,* Feature in New York Review of Books, Vol. 37, No. 20, 1990

B. The Feminist Argument

It may also be argued, by extension that since historically, women have been oppressed and marginalized, efforts such as microfinance are ideally poised to assist them in the fight for their rights. This is certainly true of initiatives such as the Friends of Women's World Banking (FWWB) and Self-employed Women's Association (SEWA) that actively promote women's rights and freedoms. Jacquline Brown however, remains skeptical of the motives of profit-oriented MFIs. She writes that "it is not always certain that an improvement in the living conditions of women would be actively sought were others not also to benefit"[118].

C. Contribution to Socio-Economic growth

Significantly, many independent studies show that women, more so than men, tend to use their resources for the wellbeing of the family, such as on food, education or health. While women are more likely to share their loans or the profits from their loans with male household members than vice versa and the entire family is more likely to benefit economically, and women are more likely to benefit personally and socially. "Loans to men do little to challenge the internal gender inequalities of the households, and indeed appear to reinforce them by giving men an affordable base from which to prevent their wives from engaging in their own income-earning activities"[119]. A UN report entitled 'The World's Women 1995: Trends and Statistics' spoke explicitly of this phenomenon and stated that women's development tends to have a multiplier effect and lead to greater overall economic development within the family and for the community. This is one of the oft-cited rationales for targeting women, used by microfinance practitioners.

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[118] Jacqueline M. Brown, *Microcredit, Feminisms and Empowerment: A discursive analysis of subject-object approaches to development,* San Fransisco State University, Master or Arts Thesis in International Relations, 2002: 38

[119] Kabeer 2001: 140

D. Women are More Pliable Clientele

This, in a nutshell is the rhetoric most often cited by microfinance practitioners that women are better, more reliable borrowers, and indeed records testify that women have loan repayment rates of over 90 percent in India. Palier writes that "The objective of financial viability of the MFIs goes hand in hand with the valourisation of empowerment of the economic type that involves broadening of possibilities of individual choice and a greater financial independence. To strive for financial viability leads one to target women as the most reliable borrowers"[120]. The majority of the MFIs are content to target women, assuming that their empowerment is an automatic consequence. Guerin and Palier conclude that there are ultimately very few MFIs which really have a gender policy worth of the name.

Naila Kabeer also raises an important issue when she writes that, "Women's higher repayment records do not merely reflect their socialized compliance in the face of the instrumentalist authority of NGOs or government officials, as the more negative evaluations tend to suggest, but also the compliance which comes with having few choices."[121]

E. Ground Realities: Economic Empowerment - An End in Itself?

The World Bank offers the following definition of empowerment: "Empowerment is the process of increasing the capacity of individuals or groups to make choices and to transform those choices into desired actions and outcomes. Central to this process are actions which both build individual and collective assets, and improve the efficiency and fairness of the organizational and institutional context which govern the use of these assets"[122]. However, by now it has been well established that access to financial services cannot alone foster empowerment. While the

[120] Guérin, and Palier 2005: 41
[121] Kabeer 2001: 140
[122] Guérin, and Palier 2005: 44

microfinance lobby is extremely vocal about the positive strides made towards empowering and emancipating women, it is to their credit that some practitioners also recognize that female clients may also suffer overwork, fatigue and the reinforcement of traditional roles as a result of participation in the microfinance programs.[123] One of the main contentions of the Anjuman Committee Report that studied the Kolar debacle was that the center meetings kept women from their "household duties". This was especially an issue if they were taking multiple MFI loans and therefore had to attend multiple meetings during the week.

Goetz and Sen Gupta (1996) attempted a study on women's managerial control over loan use in Bangladesh, and based on their results concluded that most women have a minimal level of control over their loans.[124] Traditional roles establish women's subservience to men, who may usurp the loan in its entirety or dictate the terms of its use. The authors point out that in such situations women's credit participation may worsen the degree of domestic abuse suffered by them.[125]

Significantly, the study found that single, divorced, and widowed women were more likely than other to retain control over the loans, indicating that normative traditional roles were not really being challenged under normal circumstances. It was also noted that women retained control more often when the loan size was small, and when the loan was used for activities that did not challenge the notions of appropriate work for women and men. Albeit the study pertains to social realities in Bangladesh, but the subservient position of women vis-à-vis men is a reality across the subcontinent, and the results have a significant resonance among women microfinance-clients in India.

[123] Personal Notes from the Microfinance India Summit, 2009
[124] According to their criteria, less than 18% women in the sample had full control over their loans, and 39% participants had very little or no control over the loans they took from credit programs.
[125] Anne Marie Goetz and Rina Sen Gupta, *Who takes the credit?: Gender, Power and Control over Loan Use in Rural Credit Programmes in Bangladesh,* World Development 24:1, 1996: 45-63

Johnson and Rogaly[126] question the conclusions reached by the Goetz and Sen Gupta study. They argue that 'control', or the lack thereof, over the loan is not a sufficient indicator of whether the women clients were empowered or not. One possible explanation may be that credit is fungible within the household, and while the women did not directly control the terms of use of the loan, they may have used their position as receivers of the loans as a bargaining counter to strengthen their status and position within the household. Further, Goetz and Sen Gupta allege an illusory notion of individuality in the household, whereas in reality household work as more organic units of collaboration and partnership. Therefore, while the women may not retain control of the loan per se, their contribution in bringing in the loan most likely does not go unnoticed. On a related note, Guerin and Palier write that, "Even if one aims only at the empowerment of women, to ignore the men is dangerous because then one incurs the risk of increasing tension in the household, in the neighbourhood and/or in the village."[127]

Simanowitz and Walker write that "participation in a microfinance program …may lead to changes in poor peoples' self-perception and ability to interact with other people within the household (such as having an impact on gender relations), within the community, or within wider political and social structures."[128] This may also strengthen their social networks. Viewed in these terms it may be argued that financial services have the potential to affect many aspects of a client's life, besides enabling a micro-enterprise. In another study by Hashemi et al. (1996), the authors

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[126] Johnson and Rogaly 1997: 13
[127] Kabeer 2001: 140
[128] Daley-Harris 2002: 26

conclude that whether or not the participants' husbands appropriate their loan funds, just the experience of being a member of a microfinance program is beneficial for empowerment.[129]

It would be very naïve to suggest that female clients derive no ostensible benefits from microfinance. The economic benefits that accrue to women often translate into greater participation in the household economy and economic decision making and may also extend to greater participation in the community as a whole or engagement with authorities within and outside the community.

Interestingly, Pitt and Khandekar[130] in a landmark study conducted in Bangladesh found that the flow of consumption expenditure increased 18 taka for every 100 taka borrowed by women, but only 11 taka for every 100 taka borrowed by men. Another study, using different parameters finds that credit provided to women improves measures of health and nutrition for children of both sexes, while credit provided to men has no significant effect.[131] Also, interestingly many Indian MFIs require women to have their husband's consent and signature on the loan document, before they disburse the loan to them. "Given this, if there is a serious disagreement between husband and wife in any family, such a member can neither join the MFI program nor can she get any new loans, and she would have to leave the program"[132]

In most of the literature on microfinance SHGs are projected as democratic and participatory bodies that inherently foster empowerment. However, issuing a word of caution, based

[129] Syed M. Hashemi, Sidney Ruth Schuler, Ann P. Riley, *Rural Credit Programs and Women's Empowerment in Bangladesh,* World Development 24:4, 1996: 635-654
[130] Pitt and Khandekar 1998. Cited in Pitt, Khandekar and Cartwright 2003
[131] Pitt, Khandekar, Choudhury and Millimet, 2003. Cited in: Ibid: 1
[132] BSS handout at the Microfinance India Summit, 2009

on the evidence of multiple case studies, Guerin and Palier warn that "to organize women's meetings is not synonymous with participation" and that "the collective approach, often put forth, does not only have the beneficial effects of emulation and cooperation; it can also lead to the reinforcement of gender and caste inequalities"[133], as corroborated by the Light and Shades study, conducted by the EDA, under the guidance of Frances Sinha[134].

F. Over-empowerment

This concept is employed by Suadnya et al. to emphasize that within the paradigm of a microfinance operation, where the power relation between the MFI staff and clients is presumed to promote empowerment, a relationship of domination of the 'patron-client' type may also be engendered. Similarly, within an SHG, a group leader often wields a lot of control over the other members' access to and use of the loans. Therefore, it is important to qualify that the top-down approach to empowerment that most MFIs seem to be employing is inherently flawed.

It is difficult to agree on a single, all-encompassing definition of women's empowerment. By its very nature, the concept is fluid and subjective and relative to its socio-cultural context. I would tend to agree with the statement that "The link between microfinance and empowerment is neither linear, nor unequivocal and even less systematic"[135].

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[133] Guérin, and Palier 2005: 345
[134] Frances Sinha and Kim Wilson, *Self Help Groups in India: A Study of the Lights and Shades,* EDA Rural Systems and Andhra Pradesh Mahila Abhivruddhi Society, 2006
[135] Guérin, and Palier 2005: 28

Chapter 4. Empirical Research

I. Lessons from the Microfinance Summit, New Delhi, 2009

My first interface with the microfinance sector was in 2006, when I attended the 3rd Microfinance India Summit. Last year, in 2009, I had the opportunity to attend the 6th Summit, which was held in New Delhi, from October 26 to 28. While the crux of the event was an opportunity for the industry to toast to its past successes and indulge in a three-day networking exercise, there were also clarion calls for the microfinance community to conform to its ideal of 'Doing Good and Doing Well'. The theme for the Microfinance India Summit 2009, 'Doing Good and Doing Well' is a recognition of the latent opportunity represented by microfinance, with the added disclaimer that in order to realize its full potential, microfinance must also be sustainable.

The various seminars focused on the state of the sector, goals for the future and long term prospects, and technological innovations that could potentially radicalize the future of microfinance. Here, I will focus on two of the issues on the agenda that I considered most pertinent.

A. Mission Drift

The terrifically rapid growth of the microfinance industry in India excited much applause, attention and speculation. Microfinance India made good on a prescient declaration by Michael Chu, a former Wall Street financial specialist and president of ACCION International, who said that "Microfinance today stands at the threshold of its next major stage, the connection with capital markets…if accomplished, it will make the outreach of microfinance to date […] a mere prologue for what will come. The millions reached today will increase a hundredfold. This is nothing short of

changing *the very nature of banking,* from servicing the top 25 or 30 percent (at the most) of the population of the developing world to meeting the demand of the rest. It is the reclaiming of finance for society at large – the true democratization of capital". What Chu did not allude to was the private fortunes of the CEOs and founders of these MFIs have amassed overnight while charging exorbitant rates of interest (between 20 to 60 percent) to their poor clients, nor the problems with scaling up too quickly, the watered down quality of services, the ruthless scramble for targets and the aggressive competition among MFIs to recruit more clients, that such rapid scaling-up entailed.

It takes careful dexterity for organizations to balance the social mission of microfinance with climbing the ladder of economic sustainability and profitability, and unfortunately most MFIs have thus far failed the test. Pushed by shareholders (mainly private equity players and venture capitalists) to maintain exorbitantly high growth rates, MFIs have witnessed a palpable shift of priorities. Loan officers, who used to pride themselves on the links that they maintained with the communities that they served, have become little more than collection agents. The chase for numbers makes it impossible for loan officers to be sensitive to client circumstances and many borrowers have complained about strong-arm collection tactics even in the face of genuine hardship such as a death in the family or severe loss incurred in the enterprise. In the name of standardization, MFIs have severely restricted their product offerings and stifled innovation.

The high growth rates also have more dangerous repercussions in the form of unsustainable growth. Most MFIs do not have the capacity or the processes in place to manage such a rapid scale-up and there is a very real danger of organizations imploding. The lack of adequate technological inputs, competent management and streamlined processes are all issues that have been put on the backburner, as MFIs continue to expand their outreach.

The State of the Sector report 2009, released on the occasion of the 6th Microfinance Summit in New Delhi states that as microfinance caters to more and more clients, loan sizes are also drifting upwards. Anton Simanowitz writes that the most commonly used, and much criticized proxy for depth of poverty outreach - loan size, is likely to give very misleading conclusions. Large loan size is certainly a good indicator that very poor clients are not being served, but it does not follow that small loan size implies very poor clients are being served. Simanowitz goes on to quote Dunford, "Loan size is often much more a reflection of the institution offering the loan than of the characteristics of the borrower".[136]

B. Sustainable Livelihood Creation

Another emphasis of the Summit was to encourage sustainable livelihood creation, alongside the provision of microfinance. The microfinance industry has awakened to the realization that it is imperative to give the poor a method of *earning* money and not just borrowing money.

"The support given to micro-enterprises in terms of businesses and skills training is often referred to as 'non-financial services'. An argument is now being put forward that such services should be demand-led and self-sustaining."[137] One of the core rationales behind this contention is that "services provided in the past by NGOs have not been particularly useful or appropriate to those trying to set up businesses. Therefore if users are not willing to pay for the service, this indicates it is of little real benefit to them."[138] It is important to note that a not all MFI borrowers are entrepreneurs. Many take loans to start an enterprise for the first time and do not have the

[136] http://www.microcreditsummit.org/pubs/reports/socr/2002/socr02_en.pdf
[137] Tanburn 1996, Cited in Johnson and Rogaly 1997: 55
[138] Ibid

requisite business management and accounting skills that are imperative to running a successful micro-enterprise. Similarly, financial management is often not the forte of NGOs and the non-financial services they do provide fall far short of fulfilling the needs of their borrowers. In recognition of these factors, some MFIs (mainly NGOs) have recognized that they lack the expertise to build requisite skills among their borrowers. They have therefore allowed and encouraged borrowers to attend training programs conducted by certified training providers, which the MFI then finances in the form of a loan.

II. Field Work

In the following section I will attempt to substantiate my thesis with empirical findings from my own fieldwork. As part of my research I had the opportunity to travel to various destinations across India, including Delhi, Karnataka and Kerala. The substance of my empirical findings is a combination of interviews and impressions that I have recorded in the course of my work.

While speaking with the interviewees, I was careful to establish that my research was independently motivated and that I would maintain full confidentiality. For this reason, the clients and MFIs shall not be identified directly[139]. The indicators that I used for my research were inspired by a study conducted by Hashemi et al.[140], where the researchers used eight criteria to measure women's empowerment, namely: mobility, economic security, ability to make small purchases, ability to make larger purchases, involvement in major household decisions, relative freedom from domination by the family, political and legal awareness, participation in public protests and political campaigning. I was careful not to ask leading questions, or to let my preconceptions and theoretical

[139] Names have been changed to protect the identities of the interviewees

[140] Johnson and Rogaly 1997: 13; Kabeer 2001: 111

understanding jeopardize the authenticity of their responses. Interviewees were often reluctant to speak ill of the MFIs, lest this negatively impact their loans. However, once I had established my impartiality, most interviewees were surprisingly forthcoming, and offered incisive comments and often trenchant critiques.

<u>The Interviews</u>

A. Bypanahalli, Karnataka

My first port of call was a small village, just outside of Bangalore, named Bypanahalli. The village has long been penetrated by MFIs, the first of which started operations in 2003 and is now one of four competitors in the region. The *panchayat*[141] that I visited comprises of 48 families, most of which, I was informed, are participating in MFI operations.

Vijaya, who was my first interviewee, was quick to tell me that the women in the village were very pleased with the MFI operations. She informed me that prior to joining the MFI, she and her husband worked as daily wage-labourers on farms in the agricultural season, and at other times on construction sites. Once she was inducted into an SHG, she began a regular cycle of savings, at Rs.10 per week. Originally, her group comprised of 22 women. Over the course of the third month, three of them had to drop out, one due to her inability to make regular payments, and two others due to some personal reasons. None of them was given back the money that they had accumulated. After 7 months of regular savings, the group had accumulated roughly Rs.4,000 and qualified for a cumulative loan of Rs.10,000 from the local cooperative bank. Of this amount, Vijaya was among the first four borrowers to receive Rs.2,500.

[141] Local unit of governance, also denoted the local governing body

Vijaya invested her first loan in buying poultry in order to harvest the eggs and sell them to a wholesale vendor. She was also able to save Rs.400 and spend it on new clothes and trinkets for her three daughters. She informed me that at first her husband was apprehensive about allowing her to start a new venture and sceptical about her business acumen. However soon enough the poultry business started earning regular profits and he began to show her unqualified support. Vijaya was careful to mention that her husband was among the relatively liberal men in the village; he had never raised a hand to her or her children and did not consume alcohol. She acknowledged that hers was an exceptional story in this regard. The positive potential of microfinance is epitomized by women such as Vijaya.

Next, I met Pujamma, another member of Vijaya's SHG. Her narrative was starkly different from her colleague's. Pujamma is the mother of three children, all under the age of ten. Her husband is an auto-rickshaw driver, who lives and works in Bangalore, leaving her to care for her children, her father-in-law and an unmarried sister-in-law. When she first decided to join the SHG there was severe opposition from her household. Upon the intervention of the MFI staff, she was allowed to attend the preliminary meetings and subsequently convinced her family of the benefits of participation. Initially it was very difficult for her to put aside a weekly savings amount from her meagre income as a seamstress and several times she contemplated dropping out of the program. However, she relented in anticipation of the loan amount.

When Pujamma took her first Rs.2,500 loan, she had planned to set up her own tailoring unit. Her plans were thwarted when her husband requisitioned most of the money, ostensibly to pay arrears on his rent in Bangalore. Left with no capital and no support from her in-laws, Pujamma decided to borrow some money from her maternal cousin to be able to repay the loan instalments.

Simultaneously, she began to work longer hours at the tailoring unit and often brought work home. This led to discord within the household and her husband threatened to leave Pujamma if she was not attentive to her duties at home. Meanwhile, the oldest of her children, 9 year old Mina has begun to assist her in sewing buttons and other simple tailoring tasks, while the younger two attend the village school. Mina's story exemplifies one of the worst fallouts of microfinance interventions, where on the one hand loans allow investment in new entrepreneurial ventures, but at the same time force women to expand their hours of labour or children to work instead of attending school.

Pujamma informed me that her husband eventually returned Rs.1,000 to her, after she explained to him that the SHG would slander her and her family if she failed to repay the loan. Two years on from her first loan, she has still not repaid her cousin. The stories of most of the other women in village Bypanahalli lie somewhere between these two versions.

While analyzing the testimonies of these women borrowers, it became clear that most textual accounts of women's empowerment conform to neo-liberal and feminist ideals, which are often very different from these women's own sense of accomplishment. For instance, it was evident from all the accounts that there was little evidence of radical changes in the gender division of labour as a result of women's access to loans. Access increased their levels of economic activity but not necessarily their economic freedom, which was circumscribed by familial control. It may be surmised then that by text-book standards, these women are not truly empowered. However, when asked, 'What difference did the loans/participation in the MFI make to their lives?', most women pointed out that for the first time in their lives they had some measure of access to finances, which was a matter of great pride and no mean achievement.

Taking my cue from Naila Kabeer's study, I probed further by asking 'What changes did the loans bring about and how do you assess these changes?' A few of the women cited an increased voice in household decision-making. While none of the women I interviewed retained sole control over their loans, in some cases women conceded control over their loans to male household heads in recognition of their responsibility for the collective welfare of the household, while in others appropriation of the loan by male members of the household was a manifestation of the pre-existing marginalization of their women kin. At the same time, these women were mindful of the new respect they commanded from their families by bringing in the loans, even if they lost all control over its actual use.

Chandra, a middle-aged, self-employed MFI client told me, "Why shall I be bothered with the decisions? I am a married woman, if I do not respect my husband, I will lose the respect of others". This prompted me to ask her whether her husband accords her similar respect, to which she answered blithely, "Men and women are not the same", without any further explanation. A similar response was noted across a large section of women interviewed by Naila Kabeer, one of whom stated, "Even if I die, my husband will continue to take responsibility for my children… I keep the money, but it is his responsibility to spend it so it does not stay too long with me."

Joint decision-making was taken for granted in most cases, and while this is often regarded by critics as undermining women's authority, it could also be viewed as reflecting collaboration over household interests. In fact, some clients saw it as irrelevant that the loan was formally granted in their name. Enhanced self-worth and perceived economic contribution were repeatedly testified to. Contrary to the starkly individualistic parameters used by critics of women's empowerment, most of the women in Bypanahalli were elated not only by their own sense of achievement but also the value

attached to the wellbeing and dignity of work engaged in by other household members. For instance, Kamla, one of the first members of an MFI in the village community told me that "Today my husband is able to do dignified work and has respect in society, and for me that is my biggest achievement". Interestingly, she runs a small nursery in her home and is not allowed to travel long distances without her husband's permission, but says vociferously that she does not feel oppressed or cheated of her rights.

B. Irulam, Wayanad, and Kuzhikandom, Idukki, Kerala

I travelled across the spice-growing villages in the interior of Kerala, where I was introduced to a radically different social reality from the one I had observed in Bypanahalli in Karnataka. At Irulam and Kuzhikandom, in the Wayanad and Idukki districts I interviewed small and marginal spice farmers, each of whom owned less than 5 acres of land, but were comfortably above the national poverty line. These families lived in well constructed houses, with modern bathrooms, 24-hour electricity and sometimes even cable television. Most of them owned two and four-wheeled vehicles, and nearly everyone had mobile-phones. Confessedly, I was not expecting to be confronted with the relative prosperity that I witnessed here.

Another visible trend in Kerala was the relative absence of chronic poverty, for which the 'Kerala Model' has been lauded by development experts around the world. However, the primarily agricultural economy, dependant on volatile harvests and international market prices, means that farmers are very vulnerable to the vagaries of weather and fluctuations in harvest-prices. In such an environment, loans may be necessary for consumption-smoothing or as much-needed capital in the harvest season, however the requirements of most farmers are easily furnished by banks, many of which are a legacy of the rich-cooperative movement in Kerala.

However, proverbially, there was more to the picture than met the eye. Mr. Mathew, a vociferous proponent of fairtrade in India and globally, first alerted me to the shaky foundations of the big marble houses that these so-called small farmers lived in. In years of prosperity many of them had taken out loans to construct these gargantuan dwellings and since then were trying to pay-off their loan instalments. Tragically, in this Wayanad village last year, four farmers committed suicide due to a debt-burden that they could no longer bear. Mr. Mathew rightly observed that in such an environment it seems almost irresponsible to introduce microfinance to these households, already suffering with over-indebtedness.

C. Dallupura, Delhi

The next phase of my research was conducted in village Dallupura, on the outskirts of the national capital. Microfinance has entered this region relatively recently and the stark underdevelopment and illiteracy are compounding its teething troubles. Here, my inquisitiveness was first met with hostility and suspicion. Dallupura was until recently a village unconnected by concrete roads and electricity. Today it is an amalgam of the relatively conservative village ethos of yore and the more liberal (some say permissive) modernity associated with urban India. The primarily Muslim population is still propagating 'purdah' and decorum for the women while urging the men to explore opportunities in nearby Delhi. Understandably, an intervention such as microfinance, which ascribes a pivotal role to women, does not go un-challenged in these quarters.

Among the first persons who agreed to talk to me was Rasul Mian, who runs a local *kirana*[142] store and a small flour mill. Recently, his wife was approached by one of the MFIs foraying into this

[142] Grocery store / Corner shop

region. He informed me triumphantly that she did not fall into their 'trap', and later rather vitriolically tried to convince me that I should not be working for 'these profiteering monsters' and should think about getting married at the earliest. Once I had convinced him that I am not working for an MFI, he allowed me to speak with his wife Shahda and daughter Nasreen.

Shahda seems to conform to Rasuls prejudices. She explained matter-of-factly that it is not her place as a woman to control the finances in the house and although the family could use the loans, the MFIs should target the men instead of 'badgering' the women. As an afterthought she also iterated that usury is forbidden in Islam. It is pertinent that notions of empowerment are closely interwoven with indigenous understandings of class, social status and gender propriety so that behaviour expressing gender norms was often simultaneously expressive of class hierarchy and social standing within the community.[143] Rasul did not wish for his wife to engage in activities that required her to interact with 'outsiders' and rather than question this restraint on her freedom, Shahda too felt this would undermine her social status.

The literature on microfinance often emphasizes that economic agency is often restricted by women's restrictions on mobility, however, "if empowerment entails the expanded capacity for making choices, for taking actions which express their own values and priorities, then it has to be recognised that these values and priorities are likely to be shaped by the values and priorities of the wider community."[144] Therefore, in the case of Shahda, and many others like her in Dallupura, remaining in *purdah* is regarded preferable to the 'mobility' that the literary advocates for women's empowerment seem to prescribe.

[143] Kabeer 2001: 117
[144] Kabeer 1999, Cited in Kabeer 2001: 120

Admittedly, Shahda and Rasul represent one point of view in Dallupura, where a growing number of women are in fact joining MFIs. Tasmeem, who is in her late 20s and the mother of three children, has been participating in microfinance operations for a little over a year now. So far she has taken a single loan of Rs.1,800, which she has used to invest in the joint embroidery business run by her and her husband Parvez. They are both satisfied with the MFI and hope to graduate to bigger loans in the near future. However, Parvez notes that some of the MFIs are overzealous in their search for clients and often force new recruits to take on loans unwittingly. Parvez's critique concurs with the accepted wisdom among critics of microfinance in India that the industry is growing too quickly and too brusquely, unmindful of the human cost of this rapid expansion.

The premise of this industry was to provide an avenue to access loans and services that would empower the poor to rise out of unmitigated poverty and social exclusion. Instead, the focus of most MFIs is shifting rapidly toward recruiting more clients and showing higher profits. Interestingly, a short film, which was screened at the Microfinance India Summit 2009, highlighted these issues and was duly acknowledged by the Indian microfinance community.

Johnson and Rogaly point to another major dynamic that operates in the town of Dallupura. They write that "A major concern in connection with the use of self-selecting solidarity groups for financial service provision is that, given the way in which members screen each other, it is the poorest who are least likely to be able to join the scheme."[145] This hypothesis is confirmed by the opinions of the MFI staff that I interacted with at Dallupura. Nadeem, who is a field officer with one of the three major MFIs in the region, also candidly agreed that those who dropped out due to repayment difficulties were the poorest members.

[145] Johnson and Rogaly 1997: 41

D. Srinivaspur, Karnataka

Back in one of the most MFI-saturated states in the country (second only to Andhra Pradesh), it was in the village of Srinivaspur that I confronted the dangers of multiple lending and unethical staff practices. One of the first women I spoke to here, Laxmi, had three loans from three different MFIs, of approximately Rs. 5,000 each. Laxmi candidly admitted that she needed the money primarily for her daughter's wedding and had simply stated to each MFI that the loan would be used to purchase a buffalo – a buffalo that the family already owned. No MFI staff ever bothered to check what the loan had been utilized for and since Laxmi's husband earned a steady wage from his bicycle repair shop, repaying the loans had not posed a difficulty. Laxmi, however, was in a minority in her village, which has been penetrated by as many as ten different MFIs. Lately, a number of borrowers had been having difficulty repaying their weekly instalments as they are primarily agricultural workers and this season had been a difficult one for them. Many had borrowed from multiple MFIs and were faced with hostile staff who demanded their weekly repayment, regardless of circumstances.

Laxmi told me that rather than incite sympathy from field staff, the plight of the borrowers made them even more stringent in their practices. Fearing mass defaults, each MFI's field officers told these women that unless they received repayments from each woman in the centre, they would not let anyone leave the centre meetings. Laxmi narrated one incident from a few weeks ago when the husband of one of the borrowers from their centre, Kamlesh Devi, passed away the day before the MFI center meeting was held. During the meeting, even though the field officer was informed about the incident, he demanded that the rest of the group pay Kamlesh's installment for that week.

The situation in Srinivaspur, unfortunately, is not an isolated incident. While high repayment rates, of over 98 percent, look good to investors and shareholders, the pressure of maintaining such low defaults often lead field staff to resort to strong-arm measures with borrowers. This begs the question whether the high repayment rates that the Indian microfinance industry is currently seeing is something that should unequivocally be lauded? "In addressing the question of impact, NGOs need to go beyond quantitative information detailing the number of users and volumes and sizes of loans disbursed, to an understanding of how and for whom these services support livelihoods."[146]

Through my research and field work, I have come realise that MFIs may be classified under three broad categories: those whose goal is simply to provide access to credit, those whose goal it is to provide access to credit in a responsible way, and those whose goal is to provide access to credit in a responsible way *and* create positive change in the lives of their borrowers. It is the last category that is best poised to cater to the needs of the world's poor and make good on the social development objectives of microfinance. Unfortunately, there are very few MFIs operating in the third realm and as long as such a state of affairs continues, microfinance cannot be expected to meet the expectations that it has raised.

[146] Ibid: 84

Chapter 5. Conclusions

"… Those who provide microfinancial services need to monitor carefully not only their positive impacts but also their negative effects, look to the future, and not rest on their laurels"[147].

This final section will amalgamate all the arguments put forth in the preceding chapters, and analyze the potentialities of microfinance for addressing its two main claims of poverty-alleviation and women's empowerment.

I. Microfinance as a Development Paradigm

It is evident that microfinance has made positive strides in enabling access to credit for those that were previously excluded. It may be concurred that development strategies that involve community-participation, such as the SHG movement, work because the beneficiaries themselves are incentivized to attain success, rather than remaining passive and dependant on government dole or donor aid. In these terms, microfinance is a crucial improvement over the credit-subsidies or charity of yore.

It is equally apparent that not all micro-credit/micro-debt produces effective results, especially for poor people working in low return activities, in saturated markets that are poorly developed and where environmental and economic shocks are common.[148] As the late British development economist Peter Bauer said, "To have money is the result of economic achievement,

[147] Harper 2003: 155
[148] Ibid

not its precondition". Therefore, it would be foolhardy to assume that simply disbursing a microfinance loan will generate economic and social development.

At the same time, the microfinance industry must remain wary of the pitfalls that have led to the failure of previous development interventions. Among them, the mad rush for scaling-up too quickly and reaching financial targets is a most dangerous trend. The Consultative Group to Assist the Poor (CGAP) mentioned in a recent report on microfinance initiatives that "a large proportion of the money they spend is not effective, either because it gets hung up in unsuccessful and often complicated funding mechanisms (for example, a government apex facility), or it goes to partners that are not held accountable for performance. In some cases, poorly conceived programs have retarded the development of inclusive financial systems by distorting markets and displacing domestic commercial initiatives with cheap or free money."[149]

Not only does this lead to insensitivity to the larger social welfare objectives, but as Arun and Hulme point out, "The entry of aggressive consumer lenders and their competition may encourage underwriting practices and poor loan screening which devalues portfolio quality"[150], eventually harming the financial bottom line of the MFI. "This anxiety to increase the number of users can undercut the very basis of the new model: the creation of sustainable financial institutions. Studies of credit schemes have consistently demonstrated that unless borrowers and savers believed they would benefit from the long term survival of the institution, and have a sense of ownership, repayment rates would decline."[151]

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[149] Brigit Helms, *Access for All: Building Inclusive Financial Systems.* CGAP/World Bank, Washington, 2006: 97
[150] Hulme and Arun 2009: 229
[151] Johnson and Rogaly 1997:15

As pointed out by Zeller and Meyer, there needn't be a contradiction between the aims of financial sustainability and welfare impact. In fact, they point to potential synergies, whereby if the MFI is economically sustainable, clients may be better convinced of the permanence of the institution and willing to entrust their time and savings to MFI, thereby furthering its success. Further, they argue that striving for financial sustainability would de facto force the MFI to be sensitive to client needs and therefore have the greatest impact. However, this would be an ideal to aspire to.

Guerin and Palier warn that "To be a banker, and above all a banker for the poor, cannot be improvised." Reflecting on the general weaknesses of the third sector in India, they note that many microfinance institutions are plagued by various dysfunctions, including a lack of clear direction, lack of professionalism, and weak relationships with public authorities and donors.[152] Also, many NGOs are latching on to the microfinance bandwagon, since donor agencies are convinced of its profitability. While this may be profitable in the near future, if MFIs provide below-par services, they will lose the trust and business of their clientele. For this reason, it is essential that NGOs should continuously and critically assess design features in the light of the results they produce in practice.[153]

And finally, it is critical that the microfinance industry develop comprehensive indicators to judge not only the economic, but also social impact. Since "the sector is now a big-enough player for its mistakes to be noticed and publicized"[154], the onus is on microfinance practitioners to honestly evaluate their efforts, and not rest on the laurels of their achievements.

[152] Guérin, and Palier 2005: 351
[153] Johnson and Rogaly 1997: 57
[154] Ghate 2007: 11

II. Best Practices

In recognition of the fundamental potential of microfinance for doing good, the Indian microfinance industry would do well to heed the following 'best practices'.

A. Client-Focus

While microfinance, and especially the SBPL model, shows great promise for successfully targeting poorer segments of clients, there are many voices of caution against mission drift to guard against the pressures to serve richer clients with larger loans, ensuring higher profits and lower transaction costs. Bechtel and Zander[155] emphasize the need for responsive structures that take into account client demand and beneficiary participation during project planning and implementation in order to protect clients' interests.

B. Transparency

While clients are made aware of their fixed weekly repayment due at the time of disbursing the loan, very few of them are actually aware of the true cost of the loan. A survey conducted by the Centre for Microfinance demonstrated that when asked about the total interest payment for their loan, only 11 percent of MFI clients knew the right answer[156]. MFIs often do not reveal hidden fees such as loan processing fee, loan cover insurance fee etc. to their clients with the result that

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[155] PKH Bechtel and R Zander, *Providing Financial Services to the Rural Poor: IFAD's Experience, Challenges and Evolving Approaches*, International Fund for Agricultural Development, 1994. Cited in: Hartmut Schneider (ed.), *Microfinance for the Poor? Development Centre of the Organisation for Economic Co-operation and Development*, 1997

[156] Personal interaction with Centre for Microfinance (Chennai) staff member at the Microcredit Summit 2009, Delhi

borrowers are unable to make informed decisions and discern between products offered by different MFIs.

When the issue of lack of transparency is wedded to the high interest rates charged by MFIs, it becomes a genuine cause of concern for those who fear that microfinance may be exploiting the very poor it seeks to empower. This has resulted in strong action being taken in certain countries. For example, Nicaragua recently passed a law which mandated the interest rate that MFIs are allowed to charge. Other countries have put a cap on interest rates and while interest rates in India are still unregulated, there is a fear that if MFIs do not encourage a process of conversion to transparent pricing, the state will intervene to address, what some see, as extortionist practices.

C. Accountability

By its very nature, microfinance is based on a principle of "relationship lending" which implies that MFIs have a certain level of responsibility/accountability towards their borrowers. This sense of accountability needs to be manifested through protection against over-indebtedness, ethical collection tactics, ethical staff practices, grievance redressal and protection of client data

D. Product Design

Product design is an important determinant of who is attracted to microfinance and who is turned away. Simanowitz and Walter write that "the boundaries of who microfinance can reach, and in what ways, have still to be explored. Many millions more can benefit. It is not the poverty level of potential clients that determines access and impact, but the design of the services provided. Not all people need microfinance, but most groups can benefit." [157]

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[157] Harper 2002: 1

For instance, when SHG promoters belong to the local community, they are better able to target the poorer households, however alternatively, their personal prejudices may also bias them toward a certain segment of the community, unless checks are put in place to address this. Lending in groups (SHG model) and doorstep disbursement of loans may encourage more clients to participate in a program. Similarly, charting flexible repayment schedule is an important factor that attracts poorer clients to microfinance. The high rates of interest and mandatory participation in monthly/weekly group meetings ensures that the microfinance programs are not hijacked by non-target or wealthier groups. However, the same conditions may be responsible for lack of participation by the very poor, who may be wary of incurring debt and reluctant to expend their valuable time on meetings.

The 'plain vanilla' income generating loan with its 50-week repayment schedule that still makes up the bulk of the portfolio of all MFIs is not a product that is suited to the needs of all borrowers. For example, many borrowers have businesses, or trade, that are highly seasonal or cyclic. The rigid weekly repayment schedule assumes that cash-flows for borrowers will remain the same throughout the year, or that they will have enough savings to tide over weeks when business is slow. However, with a vast majority of the poor still having no access to saving facilities, there is a real need for innovative products.

E. Inclusiveness and Collaboration in the Sector

The Indian microfinance industry would greatly benefit from increased collaboration within the sector. The immediate benefits of building on institutional potential would be to improve borrower screening and loan appraisal. Suggestions have been floated to create a nation-wide credit-

bureau, in order to prevent multiple-borrowings, which are a prime source for over-indebtedness among microfinance clients.

F. Technology

The 1990s were a watershed in the development of commercial microfinance, marked by expanding international and regional communication, growing focus on issues of regulation and governance, foundation of practitioner networks, introduction of internet discussion groups and websites, development of industry standards and rating agencies[158].

Technology is the future of microfinance; it has made it easier to address the two main obstacles in providing financial services to the poor – 'managing information' and 'service delivery costs'.[159] The challenge is to make products more convenient and cheaper for customers, and the provision and access to these services more secure for both clients and providers.

III. Mitigating Poverty and Empowering Women

Marguerite Robinson's recommendation that the microfinance sector should seek to meet the demand of low-income people for financial services largely informs microfinance practice today. The debate seems to have tilted firmly in favour of the financial systems approach, where MFIs are either trying to operate on commercial lines and systematically reducing their reliance on interest rate subsidies and donor support, and tending to look toward the markets for capital. The process is accentuated by formal established banks and financial institutions moving into microfinance.

[158] Robinson 2001: 63
[159] David Hulme and Thankom Arun, Microfinance – A Way Forward, Brooks World Povery Institute Working Paper 54, 2008

However, the commercialization of microfinance has led to the redistribution of assets in such a highly unequal way that by introducing private capital into the picture, overnight the directors and founders of MFIs have made fortunes, while their clients continue to labour under unjustifiably high rates of interest. Those concerned explicitly with poverty-reduction or targeting the extremely poor are taking recourse of 'graduation programs' that link microfinance to social protection and other services. "To save embarrassment, such MFIs can use token programs – such as Grameen's 'Beggars Program' to show that their heart remains with the poor even when their head (and financial portfolio) has moved to the market."[160]

It is widely agreed upon that anti-poverty resources should be allocated across sectors on the basis that "a concentration on a single intervention mechanism, say credit, is much less effective in poverty reduction than simultaneous credit, primary health, and education.[161] Microfinance has a gone a long way in extending financial services to the previously ignored lower-income groups, but it cannot and should not pretend to be a panacea for chronic poverty.

Finally, the much advertised claim of women's empowerment needs to be qualified with the disclaimer that empowerment is a complex and continually contested phenomenon with multiple dimensions. It is important to "ground the conceptualization of empowerment in an understanding of the relationships of dependence, interdependence and autonomy which characterize gender relations in different cultures, the structures of risks, incentives ad opportunities which they generate and therefore the particular trajectories which processes of empowerment are likely to take."[162]

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[160] Hulme and Arun 2009: 226
[161] Johnson and Rogaly 1997: 14
[162] Kabeer 2001: 136

Women cannot be judged to be empowered based on narrowly defined, often uni-dimensional indicators based on neo-liberal preconceptions. We need to look beyond the forms of development and change that have been valorised in development and feminist literature and instead shift focus to the priorities favoured by those whose lives these interventions are seeking to transform.

Microfinance has become the new development mantra, and not without reason. It is my contention that although this enthusiasm is warranted, it must be tempered with a hard look at the actual accomplishments of the sector. Microfinance has been successful in incurring small change, but as of now, and by itself, it is not a panacea for poverty alleviation or women's empowerment.

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Curriculum Vitae

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