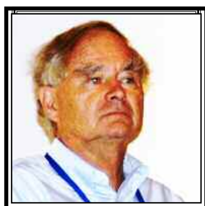
MICROFINANCE
AND THE PRESERVATION OF POVERTY

MALCOM HARPER



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→ | CHALLENGES

"He gives the poor man twice as much good who gives quickly."

PUBLIUS SYRUS

THE COMPARTAMOS IPO: TRIUMPH OR TRAGEDY ?

On April twentieth 2007, microfinance came of age. Compartamos, a medium sized Mexican microfinance bank with some 750,000 clients, had its initial public offering on the stock exchange. About one third of the shares were put on the market, and the institutions and individuals which were selling them cleared some 450 million dollars, valuing the whole institution at around one and a half billion dollars. Two young men had started the institution seventeen years before, with assistance from the United States Agency for International Development and other agencies. They had adopted the following mission statement:

"We are a social company committed to the people. We generate development opportunities within the lower economic segments, based on innovative and efficient models on a wide scale as well as transcending values that create external and internal culture, fulfiling permanent trusting relationships and contributing to a better world."

They each made over fifty million dollars from the flotation, and the rate of return on the six million dollars which they and others had earlier invested in the institution was around 100% per year. Compartamos was charging an annual interest rate of about 96% on its mainly very small loans to Mexican women, who had previously had no access to credit from formal financial institutions. There was a certain amount of competition from other institutions, but Compartamos had successfully maintained this high rate of interest in order to accumulate profits to finance its growth, and to attract equity shareholders as a basis for further borrowings from banks.

The extraordinarily high valuation was in part the result of global stock market euphoria, and the attractions of a new form of investment, with perceived social as well as profitable gains. Between the flotation and July 2010 the Dow Jones index fell by around 20%; in the same period the Compartamos share price had risen by about 30%. It had not, however, been a bad investment by the standards of stock market performance during that rather turbulent period.

The Compartamos IPO has been widely documented elsewhere, and there is still a fierce debate as to whether it was an unfortunate and isolated example of excessive profiteering, or a triumphant vindication of the argument that the poor were as credit-worthy customers as anyone else. My purpose, however, is to suggest that this incident was no more than a rather dramatic illustration of the exploitative everyday reality of microfinance, and that it is an indicator that that this aspect is rapidly taking over from the more benign face which the movement once had.

The trends which I shall identify are not, I hope, irreversible, and I do not want to suggest that microfinance has been wholly taken over by exploitative interests. Microfinance has brought formal financial services to many millions of disadvantaged households which previously had no access to such services. It continues to expand, and to bring these services to ever more people, for good and for ill. I would not suggest that the damaging and dependency-creating features of microfinance, which are the subject of this paper, are the result of a conspiracy to keep the poor poor, even though this does maintain the customer base of the institutions. They are an unfortunate by-product of the way the movement has evolved, which follows the normal but now accelerated centralising effect of global capitalism. They can, however, be resisted.

This short paper will point out some of the ways by which microfinance may be contributing to the perpetuation of poverty, rather than to its alleviation (or even to its elimination, as some of its more enthusiastic proponents claim that it can do). And, it will suggest ways in which these trends may be resisted, or even reversed.

These tendencies are covered under the following five broad headings:

- the types of clients reached by microfinance;
- the features of the financial products that are provided;
- the means through which they are delivered;
- the cost and the uses of micro-loans;
- the sources of funds and ownership of the microfinance institutions.

CLIENTS

One of the defining features of microfinance, which has caught the imagination of the general public more than any other, is that its clients, who today number is well over one hundred million people, are overwhelmingly women. Microfinance is not at all a women's business in the sense that the founders, owners or staff of the institutions are women; they are predominantly male, as are the leaders, owners and staff of most businesses, particularly in poorer countries, but their customers are mainly women. The Micro-credit Summit Campaign estimates that 84% of all microfinance clients are women, and Grameen Bank states that 97% of its customers, or 'members', are women. Many institutions, indeed, refuse even to accept male clients, although it is unlikely that many apply.

This strong gender bias is widely publicised as one of the main strengths of microfinance, in that it puts financial resources into the hands of women who have traditionally been deprived of influence over the use or even of legal ownership of money or other assets, world-wide. This form of discrimination is still strong, even in the so-called developed countries, and is even stronger in poorer societies. Microfinance has been widely and reasonably applauded as an important reversal of this almost universal aspect of society, everywhere, since it 'empowers' women in the most direct possible way, by putting money into their hands.

It is important, however, to examine all the reasons why women are the preferred clients for microfinance. The intention is to empower women, to enable them to play an equal role in economic decision-making, and this is right and proper. Women clients, however, play an important part in enabling microfinance institutions to achieve both aspects of the 'double bottom line', to do well as well as to do good. There are many reasons why they are more profitable customers than men: Women are physically, economically and socially weaker than men; they find it more difficult to resist pressure for repayment, they have fewer alternative sources of financial services than men and are thus less likely to risk damage to their credit rating with the only institution that will serve them, and they are less likely to have powerful social and political networks which will help them to avoid repayment obligations.

Additionally, women are more likely than men to accept routine standardised conditions of borrowing, and repayment. They have less opportunities to break away from the traditional activities and constraints of their local communities, and child bearing and child rearing, as well as the 'household duties' which are traditionally ascribed to them, make it less likely that they will be able or wish to invest in different types of activities, to borrow larger sums, or repay over longer or more irregular periods, than their peers. They fit more closely to a standard predictable pattern of customer behaviour, and this makes them less expensive and less risky to serve. They are better business.

This may be regarded as exploitation of women's disadvantaged condition, or as natural business sense, depending on the viewpoint of the observer, but the predominance of women as microfinance customers is not only an expression of micro-financiers' concern to redress social injustice. For whatever reasons, the operating methods of the industry have evolved in such a way that it is good business to work mainly with women.

Women are generally poorer than men, so that working predominantly with women presumably lowers the income profile of microfinance clients. It is now generally accepted by most well-informed authorities, however, that microfinance does not reach the very poorest people, the so-called 'poorest of the poor', and that when it does, it often does them more harm than good[1].

Many microfinance institutions, such as BRAC in Bangladesh, recognise this and have introduced a whole range of remarkable programmes which are specifically designed to reach out to destitute people.

These programmes, however, are not microfinance; they are poverty alleviation programmes. They may involve grants, in kind or in cash, or they may be based on paying poor people for their labour on civil works. They are not 'sustainable', still less profitable, and they must be heavily subsidised. Some are highly successful, and have enabled many thousands of women and men to escape from extreme poverty and to join the ranks of the 'economically active poor', the main clientele of microfinance.

The rhetoric of many other institutions, however, particularly but not only some of those in the Grameen 'family', suggests otherwise. Microfinance is still said to reach and benefit the poorest people, and, it is still widely touted as a panacea for poverty. The Grameen Bank has itself introduced a programme for beggars, with very small no-interest loans with flexible repayment, to enable them to add micro-vending to their traditional begging activity, but this is unique. Microfinance generally does of course reach many very poor people, if not the very poorest, but the claim that it reaches 'the poorest of the poor', and can on its own eliminate poverty, contributes to what is perhaps the major problem affecting microfinance: gross exaggeration of what it can achieve.

This in turn leads both 'social' and for-profit investors, as well as donors, politicians such as the President of the United States, and the general public, to believe that if they or their governments support microfinance they are addressing the root causes of extreme poverty. This is obviously an attractive proposition, since microfinance is popular in the City of London and on Wall Street as well as in Mexico and India. It amounts to an 'easy way out' the belief that poverty can be alleviated painlessly, and even profitably. This can only 'crowd' out' genuine attempts to deal with absolute poverty.

A great deal has been written about the people who are and continue to be clients for microfinance, and the literature is replete with heart-warming stories about women who have successfully started little businesses and sent their children to school. Less is known, however, about the people who are not clients, and about those who were, but have 'dropped out'. Microfinance is said to 'reach the unreached', but it can also further marginalize those most in need.

Many institutions do not know or are reluctant to reveal the numbers who drop-out from their groups, but in East Africa they are said to amount to between 25% and as much as 60% per year[2] while figures from India show an annual dropout rate of some 10% from self-help groups[3]. There is sadly little evidence to suggest that the people who drop out from microfinance groups are 'flying out', because they have graduated to an economic level where they want, and can access, a more individualised type of financial service, such as the readers of this paper, and the managers and staff of MFIs themselves enjoy. Grameen Bank, again, has introduced student loans to enable young men and women from client families to go on to higher education, but this is not a common practice; most microfinance clients either remain as microfinance clients, or drop out because they fall below the modest level of well-being that is needed to remain a group member in good standing.

Some may leave because they leave the area, or because they change to a competing supplier of microfinancial services, but most drop out, because they cannot maintain the regular savings, they cannot repay their loans or they lack the skills, the confidence and the opportunities they would need to invest in their own micro-business. The 'sustainability', or profits, of microfinance institutions depend on all their clients being in debt. Some allow clients to remain in their groups while they 'rest' for a few weeks at most between loan cycles, but if they stop borrowing for any longer they are 'balanced out', that is, their outstanding loans are set against their accumulated savings, they are given the balance, often without any interest, and they have to leave. Clients who want only to save are unprofitable, and such people tend to be the poorest; they are too poor for micro-debt.

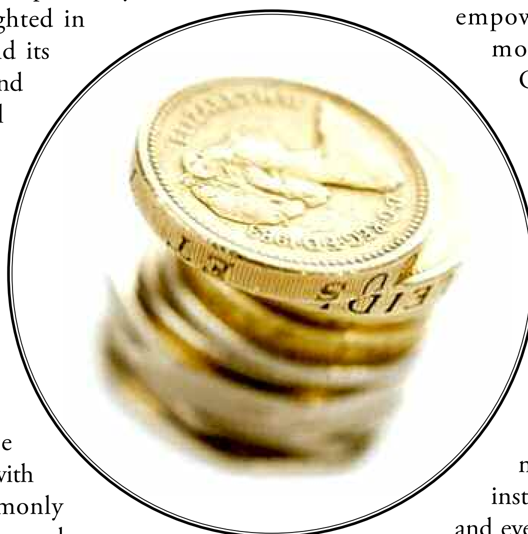
In my own experience I have found that members of the groups themselves also want to avoid the topic of dropouts; those who have dropped out are of course unhappy to talk about their own failure, which has pushed them still further to the margins of their communities.

FINANCIAL PRODUCTS

Traditional retail banking, worldwide, has been based on clients' savings. These savings are used not mainly as a form of security for loans, or to develop and test client's ability to take small regular amounts from their day-to-day spending as 'practice' for

repaying a loan. Secure, accessible and if possible remunerative savings, for their own sake, are the most important service which the institutions offer to their members. Loans come second, and are funded from the accumulated savings of those who want mainly to save.

Institutions of this type depend on the trust of their clients for their survival. They may or may not be owned in a legal sense by them, but the institutions depend on the clients, rather than the clients depending on the institutions. Microfinance institutions, which started by being called micro-credit institutions and still offer loans as their main product, depend on their clients to borrow and repay their loans, but the dependency relationship is heavily weighted in favour of the institution and its owners. The clients are bound to repay by legal and social sanctions, and the group systems strongly motivate continued indebtedness. Savings constitute independence, loans create dependence.



The size and terms of microfinance loans further strengthen the dependence of their clients. Loans are small, and for short terms, with frequent repayments, commonly spread over twelve months or less. Clients must remain in continuous contact with the institution, and the size, and the cost and terms of their loans mean that it is very difficult for them ever to become independent of their source of microfinance services. Their economic and even social survival comes to depend on remaining in the group and always being able to borrow and be in debt. There is no escape, except to fall to an even lower level.

DELIVERY CHANNELS

Most microfinance clients receive their financial services through some kind of group intermediation. The groups may, like self-help groups in India, act as financial intermediaries themselves, borrowing from a bank or MFI, or taking members' savings and on-lending themselves, or they may perform a social intermediation role, approving and guaranteeing members' loans, and facilitating transactions between members and the institution, but not actually taking title to the funds themselves.

These groups perform a valuable service to their members, under the broad heading of 'empowerment'. The services they provide to the microfinance institution, including guaranteeing or securing members' loans as well as extensive transaction assistance, are one important means which makes it possible to provide formal financial services to people who lack any collateral security and whose financial needs are not sufficient to justify the total cost of an individual account. Microfinance institutions outsource to their groups many of the normal functions performed by bankers: this assistance is unremunerated, but it can be reasonably be argued that it is the only way through which the institution can provide services to the members at all.

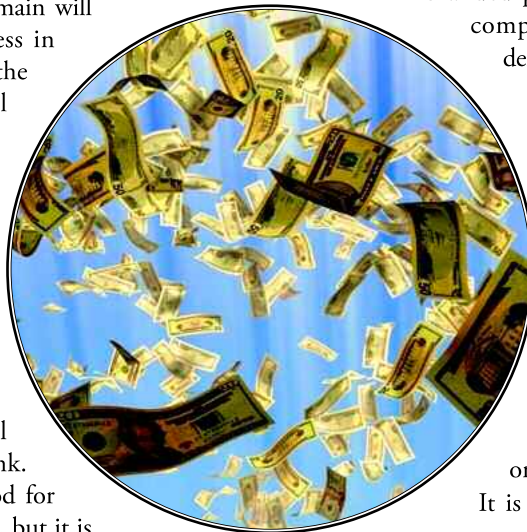
Group lending systems, however, can contain inherent contradictions. They do enable lenders to reduce their costs, and the financial services which are provided can be empowering for individual borrowers. But the processes of enforcing loan repayment in particular can be disempowering, particularly for the most poor and vulnerable. Group based systems, through their informal financial and risk sharing mechanisms, can reduce information asymmetries and secure high recoveries. These advantages, however, are often offset by the unequal and dependent power relations which such systems support. By building on existing informal mechanisms, microfinance institutions may be perpetuating and even reinforcing power asymmetries in a way that is completely contrary to their stated objectives of poverty alleviation and providing opportunities for the poorest and most vulnerable[4].

Like many other features of microfinance which have been introduced for good reasons, however, groups also have their downsides from the day-to-day point of view of their clients. It is unlikely that anyone who is reading this paper would be interested in a financial service which demanded attendance at a meeting for an hour or more every week, as well as open discussion of all their household's financial affairs, or where they were required to guarantee loans to other customers. Group microfinance is a second rate product, which is justified because the customers are poor.

In addition to the risk of loss and the burdens placed on members' time and their privacy, groups also have a number of other less obvious but potentially worrisome effects, which can contribute further to client dependence. Most businesses, particularly those which have the potential to grow and employ people in addition to their founders, are started by one person, or sometimes by a small team. There are of course many successful co-operative businesses, and other enterprises started, owned and managed by larger groups or even whole communities, but these are exceptional.

Entrepreneurship is primarily an individual phenomenon.

Group microfinance is successful because all the members of a given group, indeed of all the groups serviced by a given institution, have approximately similar financial needs. If one person wants to save larger but less regular sums than her peers, or to borrow for very different periods, it is difficult for the system to accommodate her needs. Groups can empower their members to demand and receive more than they could expect as individuals, but they also reduce all their members to the lowest common denominator: all can advance, but only at the pace of the slower. The slowest and least successful members may of course be forced to drop out, but those who remain will still have to act more or less in concert, in order to avoid the imbalances which will inevitably occur if one or a small number of members have much larger savings or loan balances than their peers.



This need not be a problem if microfinance institutions try to help their more ambitious clients to 'graduate' to individual accounts with a regular bank. Such altruism might be good for local economic development, but it is not good business for any institution to assist its best customers to close their accounts and take their business elsewhere. It makes sense to retain them, to maximize the profits to be made from their business, but not to distort the whole business model on their behalf.

Groups are also grateful, whereas individuals all too often turn and bite the hand that fed them. NGOs and other institutions which want to help the poor thrive on gratitude; it helps to raise more money from supporters, it reinforces their confidence in the merit of what they are trying to do, and if the institution's sponsors have political connections, client gratitude can be turned into votes.

Women work better in groups than men. Those microfinance institutions which admit men invariably find that male groups' repayment records are worse than women's. Men's relative inability to work effectively in groups may in part be because they are physically stronger and more able to resist group pressure, such as for repayment. Whatever may be the reasons for it, however, group delivery methods reinforce the predominance of women as microfinance clients. As we have seen, this has valuable social and business benefits, but it also reinforces the unequal power relations between microfinance institutions and their members.

THE COST AND THE USES OF LOANS

The cost of microfinance loans further strengthens clients' dependence. Microfinance interest rates are rarely as high as that charged by Compartamos, but the average annual yields on the loan portfolio are in the region of 30%. Such high rates are of little significance for an investment such as one dollar for a packet of ten cigarettes which will be sold for fifteen cents each, or a total of one and a half dollars, in half a day or less, or even for a hundred dollars worth of goods which will be sold in a week days for a profit of perhaps twenty dollars. It is possible to earn returns such as these, of fifty per cent a day, or twenty per cent a week, on petty trade, often by selling branded products from multinational companies. The nexus of dependence is neatly preserved.

More 'productive' enterprises, however, such as growing crops on a small farm or manufacturing simple items in a village workshop, require larger investments, they earn much lower rates of return, often around thirty per cent per year or less, and they may take half a year or more to realise their profits[5]. It is unprofitable to finance such ventures with microfinance loans, and this further marginalizes the borrowers, keeping them and the regions and countries from which they come in a state of continuing dependence, both on microdebt, and on foreign sources for goods to sell. The returns to capital from marketing branded consumer goods and from microfinance are generous, and the microfinance client remains dependent on whatever value she can add by her labour alone.

Most microfinance borrowers improve their financial position through their loans. They may, at the most elementary level, replace a moneylender loan which that cost perhaps ten per cent a month (similar as it happens to the rate charged by Compartamos) with a microfinance loan costing three per cent a month. The gain of seven per cent a month, even on a loan as small as one hundred dollars, is very significant for a household whose total earnings may be as low as two dollars a day or even less. The switch may involve some intangible gains, and losses. Some moneylenders demand free labour as well as interest, and their loans may be informally linked to the preservation of traditional repressive hierarchies. Many poor families, on the other hand, also rely on their local moneylender for urgent needs, such as an immediate loan to cover the cost of emergency medical care. Microfinance institutions cannot usually

match immediate services of this kind, and many clients prefer to keep their informal credit lines open at the same time as they obtain access to formal financial services for the first time.

Refinancing a moneylender loan usually involves no new skills; apart from the intangible aspects mentioned above, there is usually a straight gain. Similarly, relatively low cost micro-debt for what are oddly called 'consumption' purposes such as school fees, medical care, or house repairs (as opposed to somehow more worthy 'productive' investments in stocks of goods for resale for petty trade, such as bottles of Coca-Cola or sachets of Sunsilk shampoo), can offers an immediate saving over the higher interest rate that might otherwise have been paid to an informal moneylender.

Microfinance is associated with self-employment, and although many loans are used mainly for 'consumption' (as above) most institutions expect their clients to invest their loans in micro-enterprises which can be expected to yield a high monetary return and thus to cover the interest charged on the loan, as well as to generate enough surplus in due course to pay off the principal. The rhetoric of microfinance is about promoting enterprise, empowering the poor to help themselves, 'a hand-up and not a handout'.

As we have seen, however, the scale and cost and terms of micro-loans makes them unsuitable for investment in anything but the smallest petty trading businesses, vending, small-scale service businesses and so on. This would not be too serious if there were alternative sources of finance that were more suitable for longer-term investments in job-creating businesses such as manufacturing or farming. In too many places, however, microfinance has become the dominant paradigm. The long-established commercial banks have often been drastically 'down-sized', privatized or closed, and the institutional space which they occupied has been taken over by microfinance institutions, such as the National Microfinance bank in Tanzania or Centenary Bank in Uganda.

Similarly, in some parts of the ex-Communist states of Eastern Europe and Central Asia, where there is no recent history of full-service commercial banking, the dominant banking approach is now micro-banking. These new institutions have been vigorously promoted by Western donors, with the result that long-established community or state-owned industries, or their privately owned successors, have been unable to access the type of banking services that they need to run their businesses. Whole economies are moving towards becoming micro-trading economies, dependent for finance on highly profitable microfinance institutions owned by Western European, American or Japanese interests, and similarly dependent on profitable multinational consumer goods, plantation and resource companies for the goods which they trade. These 'emerging economies' risk becoming economic satellites of the West, in the same way as they used to be political satellites of the East.

SOURCES OF FUNDS AND OWNERSHIP.

There are about eighty specialised funds seeking to invest in the equity of microfinance institutions. Very few are based in what might be called 'destination countries', where there is a major need for microfinance. The majority are in wealthier countries, and the bulk of the invested funds come from the Netherlands, Germany and the United States.

These funds haveinvested several billion dollars in the shares of microfinance institutions. Foreign shareholders control a significant proportion of the world's microfinance institutions, and this proportion is probably increasing.

We live in a globalised world, but it nevertheless seems odd that there should be so much foreign interest in the ownership of microfinance institutions, which are not usually very large, and are quintessentially local in their clientele and their staffing. Many of the investors, including some of the largest ones, are of course social investors, who expect 'reasonable' economic returns from their investments as well as social returns. These investors are now being joined and to an extent supplanted, however, by institutions such as venture funds and the large multinational commercial banks which are more concerned with profit than society, particularly when profits are becoming harder to earn in their traditional markets.

There are very good commercial reasons why international capital is being drawn to microfinance. The institutions are generally not large, but they are growing very fast, and they offer high rates of return, with limited risks, at a time when such investments are in short supply. Commercial banks which deal with retail and corporate customers in the 'developed' world usually expect to earn a net return on their total assets of between one and two per cent; the returns from microfinance are much higher.

As one specialised fund management company puts it in an advertisement:

BlueOrchard's proven track record has convinced an ever-growing number of investors to choose the quality and profitability of a win-win investment : they earn a stable and competitive financial return on their investments while delivering effective social impact in emerging markets by encouraging entrepreneurship at the micro level.

And Accion, one of the pioneers in the promotion and financing of microfinance, organises regular investment road shows in New York, London, and other financial centres, under the label *Microfinance cracking the capital markets.*

Multinational banks, such as ABN-AMRO, HSBC and Citibank and others, lend large sums to microfinance institutions, sometimes in response to government or social pressure to be seen to being concerned for the poor. Such loans have so far proved to be good business, as well as good public relations, and commercial debt of this kind has substantially supplanted clients' own savings as a source of finance. In 1998, the institutions listed in the 'Mixmarket' had about seventeen dollars of client savings for every ten dollars of commercial bank loans. By 2010 this figure had gone down to less than a third of this amount (Mixmarket, *ibid.*). The institutions not unnaturally found it more profitable to borrow large sums at low cost from commercial sources than to incur the high transaction costs associated with providing on demand pass book savings accounts at multiple locations. Clients who are in perpetual debt are more profitable than those with their own savings, for microfinance institutions as well as for informal moneylenders.

Community-owned financial institutions generally rely on their members' savings as their main source of funds. This is partly because they may not have the financial strength to justify borrowing from banks, particularly in the early stages of their existence before they have built up share capital from members' contributions. It also, however, reflects their members' priorities: more people need to save, more, and more often, than need to borrow. The balance between the savings and the loans portfolios of retail banks, such as Bank Rakhyat Indonesia, reflect this reality. Most microfinance institutions start as NGOs or as non-bank finance companies, and are therefore, quite rightly, not permitted to mobilise demand deposits from the public. They, and their multinational capital supporters, have appreciated that it is more profitable to continue to focus on providing debt, and to treat savings products as a qualification or security for loans, not as a service to their customers in its own right.

Only a small number of the institutions listed by the MicroBanking Bulletin are community owned. This is to be expected, since such institutions offer no opportunities for equity shareholdings, and they have less need for bulk debt, since they can rely on their members' savings balances. They may serve their members' interest better than their commercially driven competitors, but, as with co-operative retail shops, co-operative farms and every other type of community enterprise, the tide is running against them.

A TENTATIVE NEO-MARXIST DIAGNOSIS

Marx proposed that modern society is based on a capitalist mode of production, whereby those who have control over capital can dominate and exploit those who have to sell their labour to those who control the means of production, through their capital. He came to this view in the context of large manufacturing industries, owned by capitalists and employing vast numbers of workers. He believed that these workers would in time unite to throw off the yoke of capital, and would usher in a new form of society which was ruled by labour.

This belief was not unreasonable, and modern labour movements, which have done so much to improve the conditions of workers, have indeed had their origins in factories where large numbers of workers have to be assembled together in order to use capital efficiently. They have to work together, but they can also protest, strike or even rebel together.

Microfinance offers a more subtle and potentially more durable means whereby those who control capital can exploit those who have only their labour to sell. The means of production is no longer machines which require many workers to come together to operate them, and possibly also to unite against their employer. Microfinanciers can now provide capital, in the form of microcredit, which borrowers use to purchase the tiny amounts of stocks or simple tools, which they need to run micro-enterprises. The surplus they can earn is barely sufficient for survival, but because the investments are so small the borrowers can afford to pay very high rates of interest on their loans. Capitalists no longer have to organise and manage labour. They can extract a higher return on their capital not by directly employing people, but by financing their petty businesses under the guise of assisting them to become 'entrepreneurs'. Better still, these entrepreneurs will compete against one another rather than combining against capital.

A large proportion of the merchandise and tools which are used by these micro-entrepreneurs is made in factories which maintain the mode of production with which Marx was familiar, so that a return can be earned from both manufacturing and from money-lending. The micro-entrepreneurs are mainly women, which leaves their husbands free to migrate to other places within and outside their own countries to work in factories or service industries that must be located near to their customers. The Compartamos story with which we started seems to bear this out.

Compartamos' capital is mainly owned by investors in the United States, or by their fellow-elites in Mexico. They have already benefited hugely from the success of the institution, and they presumably aim to benefit more in the future. Compartamos charges interest rates of nearly one hundred per cent, and most of its clients are women, many of whose husbands are working for relatively low wages north of the Rio Grande, also in the United States.

The small loans from Compartamos enable these women to finance micro-businesses, often peddling consumer goods produced and marketed by multinational companies based in the United States. The amounts, the terms and the interest rates of the loans are such as to make 'productive' farming or manufacturing investments much less attractive, so

the borrowers' husbands have to remain away from home, working for businesses whose owners have access to more flexible sources of finance.

The women may enjoy the ritualised ceremonies of the weekly client meetings, as some distraction from the grind of their everyday existence, and their petty businesses can earn them enough to keep themselves and their children during the periods between the arrival of remittances from the North. These remittances are most likely sent at high cost through USA-based agencies such as Western Union, or through less costly but more risky informal intermediaries, and Compartamos itself provides an international remittance service to its clients, to add to the insurance and other products which customers are encouraged to purchase[6].

Marx's proposed solution to the problem of social injustice has not worked well in practice; his diagnosis, however, seems to have stood the test of time.

REMEDIES

The main purpose of this paper is to promote self-questioning and to provoke discussion. It is easy to identify feasible remedies to most of the problems that have been identified, but it is more difficult to identify who will carry them out. It is unlikely that prospective investors, or fund managers, will want to promote community-owned institutions, or that microfinance managers will willingly hand over their best customers to their competitors, or emphasise client savings as a source of funds when they know that bulk loans from commercial banks are less expensive and less trouble.

I shall nevertheless conclude with a short list of changes which can 'make a difference', in the hope that some readers who are in a position to implement them will do so, even when this may reduce profitability or require subsidy.

CLIENTS

- Microfinance institutions should attempt to redress the gender imbalance in their client profile, by including more men, and when necessary adapting existing products and delivery methods to suit male customers better;
- the institutions should carefully monitor those who drop out from their groups, and should either themselves attempt to assist such people to improve their position or introduce them to other institutions which can offer suitable programmes for them;
- more ambitious clients should be encouraged and assisted to 'fly out' and if necessary to transfer to competing institutions which will be able to serve their needs more effectively.

Products and their delivery:

- flexible, accessible, voluntary and remunerative savings facilities should be offered to all clients, irrespective of their need or desire for loans. If the microfinance institution is not itself permitted to take demand deposits, arrangements should be made to act as agent for an institution that is a regulated savings institution;
- services should be offered to clients irrespective of whether or not they are or profess to intend to be self-employed. Clients should be allowed to use their loans as they wish, so long as they can be repaid, and the distinction between 'consumption' and 'productive' purposes should be dropped;
- clients should be allowed and encouraged to remain on the books of microfinance institutions irrespective of whether they are borrowing or not;
- group methods of intermediation should be regarded as a temporary second-rate expedient, from which clients should be encouraged to move as soon as they can to more dignified and less onerous individual services;
- the various forms of group intermediation should themselves be treated as complementary steps on a 'ladder', not as competitive products. Clients should be encouraged to climb from Grameen-type solidarity groups, to self-help groups, to smaller joint liability groups and thence to individual accounts, even if this means that they will move from one institution to another.

FUNDS AND OWNERSHIP

- Client savings should be regarded as the optimum main source of funds for microfinance institutions, even if they are more expensive to raise and manage than bulk loans from commercial banks or other sources;
- local rather than foreign equity shareholders should be preferred whenever possible;
- community-owned microfinance institutions should be promoted and assisted in preference to local private for-profit finance companies or banks. ▣

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[1] See, for instance, Navajas, S. - Schreiner, M. - Meyer, R. - Gonzalez-Vega, C. - Rodriguez-Meza, J., "Microcredit and the Poorest of the Poor: Theory and Evidence from Bolivia", in *World Development*, 28(1): 333-346, and Islam, Tazul, *Microcredit and Poverty Alleviation*, Ashgate: London, 2007.

[2] Wright G.A.N., MicroSave Briefing Note No. 8, *Dropouts and Graduates: What Do They Mean For MFIs?*, Microsave: Nairobi, 2002.

[3] Sinha F. *et al.*, *Microfinance 'Self help groups in India: Living up to their Promise?*, PA Publishing: Rugby, 2008.

[4] Harper, A., *Microfinance Peer Lending Groups; Empowering the Poor or Perpetuating Inequality?* Unpublished MSC thesis, SOAS, London 2000.

[5] Dichter, T. - Harper, M., *What's wrong with microfinance*, PAP Rugby and Rawat Jaipur, 2007: 89.

[6] *Business Week*, 13.12.2007.