



## Microcredit: A Bird's Eye View

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### Abstract

This paper deals with Micro-Credit schemes which are small loans supplied to people living in undeveloped countries who want to get out of debt and start up a self employed business, too support both themselves and their families. Women tend to be the main focus of the micro-credit industry, due to the fact that it benefits them greatly in more than just one way. It helps them financially, economically, socially and politically. It gives them a sense of empowerment. On the negative side some people are unable to get out of debt and pay back their loan, leading to things like suicide and depression.

### Introduction

Traditional banking sector cannot reach large number of poor borrowers for whom small loans could make big differences whom most of them are rural with low education levels and do not have any assets to use as collateral. As a result administrative cost of supplying loans to the poor population is extremely high causing the poor to have access to loans only through local money-lenders at high interest rates. Micro-credit financing starts with the assumption that the poor is willing to pay high interest rates to have access to finance; The system uses the social trust as the collateral. Loans are given to individuals, but an entire group is responsible for the repayment. Hence, the borrower who does not fulfill his commitment to repay back will lose his/her social capital. Micro-credit institutions report that their repayment rates are above the commercial repayment rates, sometimes as high as 97%. Today, there are millions of poor people around the world who turn to be entrepreneurs through the micro-credit sector.

### Definition:

#### Micro-credit

Is a small financial loan made to poverty-stricken individuals seeking to start their own business and enable them to become self employed. It's highly extended to poor borrowers who lack collateral, steady employment and verifiable credit history mainly to stimulate entrepreneurship, alleviate poverty and increase income. The UN Millennium Project identifies micro-credit as "one of the development strategies that should be implemented and supported to attain the bold ambition of reducing world poverty by half." Financial sector is the set and interaction of institutions, instruments, and the regulatory framework that allow transactions to be made by incurring and settling debts; that is, by extending credit. The interaction is accomplished through financial intermediaries (banks and other financial institutions) providing a link between households, firms and governments

### **History Early Beginnings**

Ideas relating to microcredit can be found at various times in modern history. Jonathan Swift inspired the Irish Loan Funds of the 18th and 19th centuries. In the mid-19th century, Individualist anarchist Lysander Spooner wrote about the benefits of numerous small loans for entrepreneurial activities to the poor as a way to alleviate poverty. At about the same time, but independently to Spooner, Friedrich Wilhelm Raiffeisen founded the first cooperative lending banks to support farmers in rural Germany. In the 1950s, Akhtar Hameed Khan began distributing group-oriented credit in East Pakistan. Khan used the Comilla Model, in which credit is distributed through community-based initiatives. The project failed due to the over-involvement of the Pakistani government, and the hierarchies created within communities as certain members began to exert more control over loans than others.

### **Modern Micro Credit**

The origins of microcredit in its current practical incarnation can be linked to several organizations founded in Bangladesh, especially the Garmin Bank. The Garmin Bank, which is generally considered the first modern microcredit institution, was founded in 1983 by Muhammad Yunus. Yunus began the project in a small town called Jobra, using his own money to deliver small loans at low-interest rates to the rural poor. Garmin Bank was followed by organizations such as BRAC in 1972 and ASA in 1978. Microcredit reached Latin America with the establishment of PRODEM in Bolivia in 1986; a bank that later transformed into the for-profit BancoSol. Microcredit quickly became a popular tool for economic development, with hundreds of institutions emerging throughout the third world. Though the Garmin Bank was formed initially as a non-profit organization dependent upon government subsidies, it later became a corporate entity and was renamed Garmin II in 2002. Muhammad Yunus was awarded the Nobel Peace Prize in 2006 for his work providing microcredit services to the poor.

Today Micro-credit has become the fashionable word with World Bank, Government and NGOs and is the key word for getting funds from funding agencies. While some consider Micro-credit as a panacea for all the ills of the society others consider the mobilization of groups as a tool for organizing the unorganised for social change. In this country approximately one third of the population live below the poverty line and majority of the people are not having basic amenities. The most affected are the women and children. From 1974 when SEWA started mobilizing poor women based on their trade we have come a long way and now there are at least 1 lake "Self Help Groups" in the country comprising 20 lakh women. If all the families under below poverty line are to be covered there is a scope for 30 lakh groups in the country.

While earlier groups evolved slowly based on the felt need, today the Government is forcing and hurrying people to form groups through various agencies showing subsidies and loan handouts as carrots. The experiences of organizations like SEWA, MYRADA etc who are pioneers in the field and now the 7-8 years of experiences of People's Science Movements (PSMs), especially the Tamilnadu science Forum in this area have shown the potential, the limitations and the problems of Micro-credit in providing support for poor women and assistance in their livelihoods. While SEWA has promoted successful Women's Co-operatives in different fields it is not seen as equally active in the fight for the rights. It is seen as restricting its activities to lobbying for concessions. MYRADA has promoted strong women's groups and linked community based schools and skill development but not they are limited in their outreach. The development of micro enterprises is also a problem. Other groups require large and often sustained resource inputs from funding agencies and their growth is limited by the availability of such funds.

For the PSMS who entered the Mass Literacy Campaigns in the nineties in a partnership with the Government, the honeymoon days were over quickly as the Literacy Mission became more and more bureaucratized and politicized. But some of the offshoots especially the Anti-Arrack Movement of Andhra Pradesh showed its potential for empowerment. Coming in the wake of the anti-arrack movement was the first successful post literacy savings groups in Nellore's Podupu Lakshmi programme. These were not merely savings and credit groups but women empowerment groups. When the Literacy Campaign in Kanyakumari was abandoned suddenly by the Government, Tamil Nadu Science Forum initiated women groups after prolonged discussion. Started on a voluntary basis with no full timers and no external resources the organization has grown into a federation of around 1000 SHGs comprising 20000 women with 26 full time staff and 210 part time village co-coordinators. The most important highlight of this program is that the entire staff is fully supported by the people through membership fee and sharing of interest. Based on this experience groups have been formed under SAMATA MICRO CREDIT NETWORK in Tamil Nadu in 10 more districts, in Kerala, Karnataka, Madhya Pradesh, Andhra Pradesh, Maharashtra, Uttar Pradesh, Bihar, Orissa, Himachal Pradesh, Assam, Tripura, Punjab and Rajasthan. There are 7000 groups in the network now. This has proved that self-reliant women's organizations can be built with people's support and they can help to empower women if planned properly. It has also been shown that Govt. or funding agency support is not critical to this process.

## **Principles**

### **Economic principles**

Microcredit is ideally based on a unique set of principles that are readily distinguished from trends in the wider credit market. Microcredit organizations were initially created as alternatives to the "loan-sharks" known to take advantage of clients. Indeed, many microlenders began as non-profit organizations and operated with government funds or private subsidies. By the 1980s, however the "financial systems approach," influenced by neoliberalism and propagated by the Harvard Institute for International Development, became the dominant ideology among microcredit organizations. The commercialization of microcredit officially began in 1984 with the formation of Unit Desa (BRI-UD) within the Bank Rakyat Indonesia. Unit Desa offered 'kupedes' microloans based on market interest rates.

Ironically, many microcredit organizations now function as independent banks. This has led to their charging higher interest rates on loans and placing more emphasis on savings programs. Notably, Unit Desa has charged in excess of 20 per cent on small business loans. The application of neoliberal economics to microcredit has generated much debate among scholars and development practitioners, with some claiming that microcredit bank directors, such as Muhammad Yunus, apply the practices of loan sharks for their personal enrichment. Indeed, the academic debate foreshadowed a Wall-street style scandal involving the Mexican microcredit organization Compartamos.

Even so, the numbers indicate that ethical microlending and investor profit can go hand-in-hand. In the 1990s a rural finance minister in Indonesia showed how Unit Desa could lower its rates by about 8% while still bringing attractive returns to investors. Today, smaller investment firms are adopting the microlending movement's original ideals. For instance, whereas small coffee farmers in Honduras are typically charged an 18% bank rate, a private investment firm in the US has room to offer more ethical loan terms and offer an attractive return to investors.

## Group lending

Though lending to groups has long been a key part of microcredit, microcredit initially began with the principle of lending to individuals. Despite the use of solidarity circles in 1970s Jobra, Grameen Bank and other early microcredit institutions initially focused on individual lending.<sup>[12]</sup> Indeed, Muhammad Yunus propagated the notion that every person has the potential to become an entrepreneur. The use of group-lending was motivated by economics of scale, as the costs associated with monitoring loans and enforcing repayment are significantly lower when credit is distributed to groups rather than individuals. Many times the loan to one participant in group-lending depends upon the successful repayment from another member, thus transferring repayment responsibility off of microcredit institutions to loan recipients.

## Lending to women

Women have double burden of being women and being poor. Lack of accessibility to land and other assets are the major problem along with lack of credit availability. Land and Dwelling places are to be provided by the Government. Credit availability is becoming easier today through SHGs. This can bring marginal changes in their livelihood. For example, with credit they can escape from usurious moneylenders and cope with illnesses and other emergencies thus increasing the quality of their lives and their health. In the area of livelihoods women have leased land for cultivation, purchased animals and birds and entered into small business as well as micro or cottage industries.

Lending to women has become an important principle in microcredit, with banks and NGOs such as BancoSol, WWB, and Pro Mujer catering to women exclusively. Pro Mujer also implemented a new strategy to combine microcredits with health-care services, since the health of their clients is crucial to the success of microcredits. Though Grameen Bank initially tried to lend to both men and women at equal rates, women presently make up ninety-five percent of the bank's clients. Women continue to make up seventy-five percent of all microcredit recipients worldwide. Exclusive lending to women began in the 1980s when Grameen Bank found that women have higher repayment rates, and tend to accept smaller loans than men. Subsequently, many microcredit institutions have used the goal of empowering women to justify their disproportionate loans to women.

## Example

Mumbai Headquarters of the National Bank for Agriculture and Rural Development of India, which on-lends funds to banks providing microcredit).

Grameen Bank in Bangladesh is the oldest and probably best-known microfinance institution in the world. In India, the National Bank for Agriculture and Rural Development (NABARD) finances more than 500 banks that on-lend funds to self-help groups (SHGs). SHGs comprise twenty or fewer members, of whom the majority are women from the poorest castes and tribes. Members save small amounts of money, as little as a few rupees a month in a group fund. Members may borrow from the group fund for a variety of purposes ranging from household emergencies to school fees. As SHGs prove capable of managing their funds well, they may borrow from a local bank to invest in small business or farm activities. Banks typically lend up to four rupees for every rupee in the group fund. In Asia borrowers generally pay interest rates that range from 30% to 70% without commission and fees. Nearly 1.4 million SHGs comprising approximately 20 million women now borrow from banks, which make the Indian SHG-Bank Linkage model the largest microfinance program in the world. Similar programs are evolving in Africa and Southeast Asia with the assistance of

organizations like IFAD, Opportunity international, Catholic Relief Services, Compassion International, CARE, APMAS, Oxfam, Tear fund and World Vision. Garmin Bank launched their US operations in New York in April 2008. Bank of America has announced plans to award more than \$3.7 million in grants to nonprofits to use in backing microloan programs. ACCION USA, the US subsidiary of the better-known ACCION International, has provided US\$117 million in microloans since 1991, with an over 90% repayment rate. One research study of the Garmin model shows that poorer individuals are safer borrowers because they place more value on the relationship with the bank. Even so, efforts to replicate Garmin-style solidarity lending in developed countries have generally not succeeded. For example, the Cal meadow Foundation tested an analogous peer-lending model in three locations in Canada during the 1990s. It concluded that a variety of factors — including difficulties in reaching the target market, the high risk profile of clients, their general distaste for the joint liability requirement, and high overhead costs — made solidarity lending unviable without subsidies. Microcredit's have also been introduced in Israel, Russia, Ukraine and other nations where micro-loans help small business entrepreneurs overcome cultural barriers in the mainstream business society. The Israel Free Loan Association (IFLA) has lent more than \$100 million in the past two decades to Israeli citizens of all backgrounds

### **Peer-to-peer lending over the Web**

The principles of microcredit have also been applied in attempting to address several non-poverty-related issues. Among these, multiple Internet-based organizations have developed platforms that facilitate a modified form of peer-to-peer lending where a loan is not made in the form of a single, direct loan, but as the aggregation of a number of smaller loans—often at a negligible interest rate. There are several ways by which the general public can participate in alleviating poverty using Web platforms.

New platforms that connect lenders to micro-entrepreneurs are emerging on the Web, for example Kiva, Zidisha, and the Microloan Foundation. Another WWW-based micro lender United Prosperity uses a variation on the usual micro lending model; with United Prosperity the micro-lender provides a guarantee to a local bank which then lends back double that amount to the micro-entrepreneur. United Prosperity claims this provides both greater leverage and allows the micro-entrepreneur to develop a credit history with their local bank for future loans. In 2009, the US-based nonprofit Zidisha became the first peer-to-peer micro lending platform to link lenders and borrowers directly across international borders without local intermediaries. Vittana allows peer-to-peer lending for student loans in developing countries.

### **Impact of Micro credit**

The impact of microcredit is a subject of much controversy. Proponents state that it reduces poverty through higher employment and higher incomes. This is expected to lead to improved nutrition and improved education of the borrowers' children. Some argue that microcredit empowers women. In the US and Canada, it is argued that microcredit helps recipients to graduate from welfare programs.

Critics say that microcredit has not increased incomes, but has driven poor households into a debt trap, in some cases even leading to suicide. They add that the money from loans is often used for durable consumer goods or consumption instead of being used for productive investments, that it fails to empower women, and that it has not improved health or education. The available evidence indicates that in many cases microcredit has facilitated the creation and the growth of businesses. It has often generated self-employment, but it has not necessarily increased incomes after interest payments. In some cases it has driven borrowers into debt

traps. There is no evidence that microcredit has empowered women. In short, microcredit has achieved much less than what its proponents said it would achieve, but its negative impacts have not been as drastic as some critics have argued. Microcredit is just one factor influencing the success of a small businesses, whose success is influenced to a much larger extent by how much an economy or a particular market grows.

### Criticism of Microcredit

As per one study only 0.2% of Global commercial lending reaches the poor women. A study of 38 branches of major banks in India found that only 11% of the borrowers are women (UNDP, 1995). So the present schemes of NABARD, SIDBI and Rashtriya Mahila Kosh are welcome as they are able to cater to the poor through SHGs. Some of the criticisms of Micro Credit that are valid are:

1. They are offered as The Solutions or Panacea to eradicate poverty.
2. It is indebting the poor
3. Poor are asked to look after themselves
4. Coercion and High Rate of Interest are seen
5. It does not help the poorest of the poor
6. Men are left out but the credit reaches men through women and is misused and burden of repayment is on women.
7. It is being used to promote products of MNCs.

Much of this is true. What is not true is that in anyway such aspects are essential to or unavoidable to Micro-credit. Micro-credit groups are an innovation from the voluntary and NGO sector. But like so many other innovations it can be hijacked by the powerful to serve their interests. The response of people should be to fight for the sort of credit cooperatives they need and NOT to fight against credit cooperatives by which one equally or even more avidly helps finance capital and monopoly. PSMs are clear on these issues and the PSM groups have been trying to go gets the right sort of cooperatives going and to go beyond micro-credit. For example people are clearly told that credit alone cannot solve their problems and they are encouraged to understand the causes of their deprivation and find ways to challenge them. A bulletin brings out articles that educated them on such social and economic issues and regular group reading of the bulletin is cultivated as a desirable and almost universal practice in these groups. Our financial independence of the staff also ensures that one has no necessity to please donors. Similarly the women are provided with support services like Continuing Education, Health awareness, training for skill development, Counseling on legal matters and are encouraged to participate actively in the democratic system. The Interest rate is kept minimum and at diminishing returns. (Remember also that women outside these groups in these same villages are getting bled at interest rates five times as much. The view that Micro-credit is indebting women and we should not be in it only serves to push them into bondage.)

There are many cases where women have contributed money to close the loans of their group members who are in distress. There is a social security fund created to help these women also. Poorest of the poor who are illiterate are carefully brought into the system and helped. While it is true that MNCs have tried to tie up with NABARD to promote their products, it is also true that many networks with us have been encouraged to buy locally produced goods and avoid products of MNCs. One example is SAMATA soaps promoted by women

in Kerala instead of the Hindustan Lever Products. MNCs will always have ways to promote their goods ,but for poor women's cooperatives such a network is essential to capture markets! Nor is there any evidence that women in such groups get diverted or co-opted.

Women are now participating in International Women's Day celebrations and agitation against atrocities in a meaningful manner with other women's organizations. Their being in local organizations help them cope with and often contend with domestic violence. Evidence also shows that all dimensions of women's movements, from membership to agitations on policy issues have been strengthened where credit groups are linked with sensitized and progressive NGOs or peoples movements. It is almost impossible to show the reverse even where the NGO is not committed to social change-- that in some way credit groups diffused women's desire to organize and resist. The transformation from credit cooperative network to a network of enterprises however is not easy. To succeed in enterprises women need more technological, accounting, managerial and marketing skills. Not to forget that they have to compete with the products of MNCs. Here we have a crucial role to play. Bringing low cost technologies, accounting skills, provide managerial training and providing alternative methods of marketing. Already work are going on in this matter but this needs more input. Beyond technology and management contending with MNCs also needs a different ways of "doing politics." Like the people of Kerala who are deciding to boycott Palm oil and MNC soft drinks to protect the coconut economy, networks of women's groups will be able to protect local products from MNC products if there is proper planning, co-ordination & collaboration between NGOs & likeminded political parties.

### **Government intervention in credit groups**

The problem today is the Government's large scale entry into credit cooperatives. Through schemes like Swarnajeyanthi Gram Swarozhar Yojana [SGSY] & Swarna Jeyanthi Sahahari Swarozhar Yojana [SJSRY] the Govt. has started subsidy linked target oriented credit through SHGs. Though the subsidy can help, a number of bureaucratic rules like the so-called Below Poverty Line rule and the target oriented credit, the a priori decision on a few trades as worthy of funding are all hindering the real growth of self-reliant cohesive women's groups. Dialogue and pressure is needed to prevent these changes. One must remember that when banks or government agencies start credit groups, whatever their motivation and whatever the articulation in policy papers, the concern at the ground level is how to confine the groups to only credit issue and how to keep it from growing into a center of dissent and resistance. To the extent that they can impose rules, pay functionaries, and demand that the women turn up or government functions, they can try to limit such a consciousness. From time to time the groups, even the worst of them transgress these limits, and have to be contained. Selection of NGOs by the government for playing catalyst roles also goes by who presents least threat to local power structures and slowly the corrupt ones get a survival advantage. All these processes should be viewed as the means that the state adopts to limit and subvert the credit cooperatives rather than as reasons for denying the validity of the credit cooperative experience. The way forward for the people's camp is to contend with these trends and shape the credit cooperatives into a process of empowerment. By linking Literacy, Continuing Education, Health, Participative decentralized democracy, legal rights & input for micro-enterprise it will be possible to continuously educate women & promote their contribution to social change.

We know from the MALAR experience that:

1. Without proper guidance, co-ordination and monitoring mechanism the groups will fail. But this support should not depend on the government.
2. Forming Groups for Savings and Loans alone will not be sustainable. They need linkage to other empowerment and livelihood activities.
3. Unless we have a clear idea of what is to be done at each stage these groups can be taken over by the Government and this ultimately fails not only as empowerment but even as credit mechanism.
4. We should shape Micro-credit as a tool for mobilizing the unorganized sector, and such a potential exists.
5. Empowerment does not occur spontaneously. It has to be planned for and if we have a proper plan and a self-supporting structure for implementing such plans then it is possible to empower women quickly.
6. Micro-Enterprises will not succeed unless we give external support like training, accounting skills, marketing skills and networking them.
7. Continuing education can be effectively linked to these groups.
8. If we guide and monitor properly this network of groups they have the potential to become catalysts for social change and they can be mobilized to fight Globalization.
9. Voluntarism should be insisted upon but on the long run self-generated fund from the groups should support a full-time plus part time structure.
10. Health campaigns especially community health worker programmers linked to SHGs are successful and benefit both programmes.
11. We can work with Government on our terms and lobby to bring changes in policies if there is better coordination in the NGO sector.
12. Self-Reliant women's organizations should be built up based on the credit networks. Linkages with other women's organizations like AIDWA, JWP, NFIW, NAWO will help women to fight the atrocities against women and also lead them towards social change.
13. Linking micro-credit and livelihood issues are not only possible but also feasible. Let us take up the challenge.

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