UNIT 11 MICRO CREDIT

STRUCTURE

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11.1 INTRODUCTION
This Unit starts with defining Micro credit and elaborately deals with early beginning of micro credit and modern micro credit system. To explain further, the Unit takes grameen bank model of micro credit as a case study. It also deals with economic principles of micro credit and self help movement.

11.2 OBJECTIVES
After studying this Unit, you would be able to

- Define micro credit;
- Trace the early beginnings of micro credit;
- Discuss modern micro credit system with grameen bank as an example;
- Explain the economic principles of micro credit system; and
- Examine the micro credit and self help group movement in India.

11.3 DEFINITION

Microcredit is a broad name for the programmes that extend small loans to very poor people for self-employment projects that generate income, allowing them to care for themselves and their families. - Microcredit Summit

The word "microcredit" became a tool for development only after 1980. Now it has become a buzz-word among the development practitioners. Today it is common to see people use the term "microcredit" to mean agricultural credit, rural credit, co-operative credit and consumer credit.

The Reserve Bank of India defines Microcredit as a provision of thrift, credit and other financial services and products of very small amount to the poor in rural, semi-urban and urban areas for enabling them to raise their income levels and improve their living standards. Microcredit Institutions are those institutions which provide these facilities.

Though the definition of microcredit varies from country to country and situation to situation, it is important to keep some basic terms in mind. These include:
• **Sixe of the loans** i.e. micro or very small in size;
• **Target users** – micro-entrepreneurs and low-income households;
• **Utilization** - the use of funds for income generation, and enterprise development, but also for community use (health/education) etc. and
• **Terms and conditions** - most terms and conditions for microcredit loans are flexible and easy to understand, and suited to the local conditions of the community.

Keeping the above terms in mind, **Microcredit** can be defined as the extension of very small loans (**microloans**) to those in poverty. These loans are designed to spur entrepreneurship in individuals who lack collateral, steady employment and a verifiable credit history and therefore cannot meet even the most minimal qualifications to gain access to traditional credit. Microcredit is a part of microfinance, which is the provision of a wider range of financial services to the very poor.

Microcredit as a financial innovation is generally considered to have originated with the Grameen Bank in Bangladesh. In Bangladesh, the grameen bank has successfully enabled extremely impoverished people to engage in self-employment projects that allow them to generate an income and, in many cases, begin to build wealth and escape poverty.

Due to the success of microcredit in Bangladesh, the traditional banking industry have begun to realize that these microcredit borrowers should more correctly be categorized as pre-bankable; thus, microcredit is increasingly gaining credibility in the mainstream finance industry, and many traditional large finance organizations are contemplating microcredit projects as a source of future growth, even though almost everyone in larger development organizations discounted the likelihood of success of microcredit when it begun. The United Nations declared 2005 as the International Year of Microcredit.

### 11.4 MODERN MICROCREDIT

#### 11.4.1 Early Beginnings
When someone claims microcredit has a thousand-year history, or a hundred-year history, nobody finds it as an exciting piece of historical information. 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. Ideas relating to microcredit were mentioned in portions of the Marshall Plan at the end of World War II.

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.

### 11.4.2 Modern Microcredit

The origins of microcredit, in its current practical incarnation, can be linked to several organizations founded in Bangladesh, especially the Grameen Bank. The Grameen Bank, which is considered as first modern microcredit institution, was founded in 1976 by Prof. Muhammad Yunus. Prof. 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. Grameen Bank was followed by the organizations such as BRAC (International development Organization) in 1972 and ASA International India Micro Finance Private Limited in 1978. Microcredit reached Latin America with the establishment of PRODEM in Bolivia in 1986; a bank that later transformed itself 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 Grameen Bank was formed initially as a non-profit organization dependent upon government subsidies, it later became a corporate entity and was renamed Grameen Bank II in 2002. Muhammad Yunus awarded Nobel Peace Prize in 2006 for his work in the area of microcredit services known as Grameen-credit to the poor.

### 11.4.3 Grameen credit

Grameen credit is based on the premise that the poor have skills which remain unutilized or under-utilized. It is definitely not the lack of skills which make poor people poor. Grameen
believes that the poverty is not created by the poor; it is created by the institutions and policies which surround them. In order to eliminate poverty all we need to do is to make appropriate changes in the institutions and policies, and/or create new ones. Grameen does not believe in charity and it is not an answer to poverty. It creates more and more dependency and takes away individual's initiative to break through the wall of poverty. Unleashing of energy and creativity in each human being is the answer to poverty.

Grameen brought credit to poor, women and the illiterate who pleaded that they did not know how to invest money and earn an income. Grameen created a methodology and an institution around the financial needs of the poor, and created access to credit on reasonable terms enabling the poor to build on their existing skills to earn a better income in each cycle of loans.

**General features of Grameen credit are as follows:**

a) It promotes credit as a human right;
b) Its mission is to facilitate poor families to help themselves to overcome poverty. It targets low income family, particularly women from low income family;
c) The most distinctive feature of Grameen credit is that it is not based on any collateral or legally enforceable contracts. It is based on "trust", not on legal procedures and systems;
d) Grameen-credit is offered for creating self-employment for income-generating activities and housing for the poor, as opposed to consumption;
e) Grameen-credit was initiated as a challenge to the conventional banking which rejected the low income group by classifying them as "not creditworthy". As a result it rejected the basic methodology of the conventional banking and created its own methodology;
f) Grameen-credit provides service at the door-step of the low income groups based on the principle that the people should not go to the bank, but the bank should go to the people;
g) In order to obtain loans a borrower must join in group as group of borrowers;
h) Loans can be received in a continuous sequence. New loan becomes available to a borrower if previous loan is repaid;
i) All loans need to be paid back in installments (weekly, or bi-weekly);
j) More than one loan can be received by a borrower at one time;
k) Grameen-credit comes with both obligatory and voluntary savings programmes for the borrowers;
1) Generally these loans are given through non-profit organizations or through institutions owned primarily by the borrowers. If it is done through for-profit institutions not owned by the borrowers, efforts are made to keep the interest rate at a level which is close to a level commensurate with sustainability of the programme rather than bringing attractive return for the investors. Grameen-credit’s thumb-rule is to keep the interest rate as close to the market rate, prevailing in the commercial banking sector, as possible, without sacrificing sustainability. In fixing the interest rate, market interest rate is taken as the reference rate, rather than the moneylenders’ rate. Reaching the poor is its non-negotiable mission. Reaching sustainability is a directional goal. It must reach sustainability as soon as possible, so that it can expand its outreach without fund constraints; and

m) Grameen-credit gives high priority on building social capital. It is promoted through formation of groups and centres, developing leadership quality through annual election of group and centre leaders, electing board members when the institution is owned by the borrowers. To develop a social agenda owned by the borrowers, something similar to the "sixteen decisions", it undertakes a process of intensive discussion among the borrowers, encouraging them to take these decisions seriously, and implement them. It gives special emphasis on the formation of human capital and concern for protecting environment. It monitors children’s education, provides scholarships and student loans for higher education. For formation of human capital it makes an effort to bring technology, like mobile phones, solar power, and promote mechanical power to replace manual power.

Check Your Progress Exercise 1

Note: i. Use this space given below to answer the question.

ii. Compare your answer with the one given at the end of this unit

1. What is microcredit?
2. What is Grameen credit? List out any three important features of Grameen credit

3. Compare Grameen credit to traditional loans in the context of interest rates.

11.5 ECONOMIC PRINCIPLES OF MICROCREDIT

Microcredit is based on a separate set of principles, which are distinguished from general financing or credit. Microcredit organizations were created to serve in the place of local [loan-sharks] known to take advantage of their clients. Many microcredit organizations began as non-profit organizations, running off government or private subsidies. By the 1980s, the ‘financial systems approach,’ influenced by neo-liberalism propagated by the Harvard Institute for International Development became the dominant ideology among microcredit organizations.

The commercialization of microcredit began with the formation of Unit Desa (BRI-UD) within the Bank Rakyat Indonesia in 1984, which offered ‘kupedes’ microloans based on market interest rates. Most microcredit organizations now function as independent banks, leading to high interest rates and a greater emphasis on savings programmes. 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, are employing the
practices of a loan shark for their own personal enrichment. Indeed, a Wall Street style scandal involving the Mexican microcredit organization Compartamentos illustrated the limitations of profit-driven microcredit institutions.

The reform of the interest rate regime has constituted an integral part of the financial sector reforms initiated in our country in 1991. In consonance with this reform process, interest rates applicable to loans given by banks to microcredit organizations or by the microcredit organizations to Self-Help Groups/member-beneficiaries has been left to their discretion. The interest rate ceiling applicable to direct small loans given by banks to individual borrowers, however, continues to remain in force. Banks have been given freedom to formulate their own lending norms keeping in view ground realities. They have been asked to devise appropriate loan and savings products and the related terms and conditions including size of the loan, unit cost, unit size, maturity period, grace period, margins, etc. Such credit covers not only consumption and production loans for various farm and non-farm activities of the poor, but also include their other credit needs such as housing and shelter improvements.

Microcredit emphasizes trust building, which can enable micro-entrepreneurship, so generating employment and helping people to help themselves during enterprise initiation and during difficult times.

11.5.1 Group Lending

Though group-lending 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. 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 of one participant in group-lending depends upon the successful repayment of another member, thus transferring repayment responsibility of microcredit institutions to loan recipients. This is facilitated by the participation of Self Help Groups.
11.5.2 Self-Help Group
A Self-Help Group (SHG) is a registered or unregistered group of micro-entrepreneurs, having homogenous social and economic background, voluntarily coming together to save small amounts regularly, to mutually agree to contribute to a common fund, to meet their emergency needs on mutual help basis. The group members use collective wisdom and peer pressure to ensure proper end-use of credit, and timely repayment thereof. In fact, peer pressure has been recognized as an effective substitute for collaterals.

An economically poor individual gains strength as part of a group. Besides, financing through SHGs reduces transaction costs for both lenders and borrowers. While lenders have to handle only a single SHG account instead of a large number of small-sized individual accounts, borrowers as part of an SHG cut down expenses on travel (to & from the branch and other places) for completing paper work, and on the loss of workdays in canvassing for loans.

11.5.3 Lending to Women
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. 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. Microcredit is a tool for socio-economic empowerment.

Case 1
Rajalakshmi 41 years old women is treasurer in Kadamalai Federation. She studies up to class VIII and got married at the age of 15. Her husband left when she is pregnant thinking that she delivers girl baby again since they have already two daughters. But she delivered boy. She stays with her parent. She associated with Kalanjiyam micro credit organization for many years. After understanding the system, she can able to lead the other women and she also actively
participate in group activities. Due to her ability, she became group leader and then cluster leaders. Finally she became the treasurer of the federation. In the process, she got confidence and courage. She became a trainer and started providing training to cluster associations. Not only micro credit activities, she is conscious of social development issues and she successfully negotiated HDFC for 8 million loan to housing project.


Check Your Progress Exercise 2

Note: i. Use this space given below to answer the question.

ii. Compare your answer with the one given at the end of this unit

1. What is group lending?

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2. What is the advantage of financing through Self-Help Groups?

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3. Why does microcredit mostly concentrate on loans for women?

11.6 STRENGTHS OF MICROCREDIT SYSTEMS

In the past few years, savings-led microfinance has gained recognition as an effective way to bring very poor families low-cost financial services. For example, in India, the National Bank for Agriculture and Rural Development (NABARD) finances more than 500 banks that lend funds to Self-Help Groups (SHGs). Each SHG comprises of 20 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. Groups generally pay interest rates that range from 30% to 70% APR, or 12% to 24% a year, based on the flat calculation method. 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 programme in the world. Similar programmes are being set up in Africa and Southeast Asia, with the assistance of International organizations.

Micro financing also helps in the development of an economy by giving everyday people the chance to establish a sustainable means of income. It works on the principle that eventual increases in disposable income will lead to economic development and growth.

As for women’s empowerment is concerned, it has been proven that women experience higher bargaining and decision-making power within the family as they bring more income to the household. The increase in the household income trickles down to impact higher consumption standards, education for children, and better nutrition.

11.7 SYSTEMS AND METHODS OF MICROFINANCE
With a view to facilitating smoother and more meaningful banking with the poor, a pilot project for purveying microcredit by linking Self-Help Groups (SHGs) with banks was launched by NABARD in 1991-92. The Reserve Bank of India had then advised commercial banks to actively participate in this linkage programme. The scheme has since been extended to RRBs and co-operative banks. Different models were adopted for establishing linkages with the banks. Some of them were:

Model I: A linkage directly established with the SHGs without intervention/facilitation of any NGO which comprising of 16% of the projects.

Model II: A linkage established directly to SHGs with facilitation by NGOs and other formal agencies amounts to 75% of the projects.

Model III: A linkage established through an NGO facilitator and financing agency which represents 09% of the total linkage. While 488 districts in all the states/UTs have been covered under this programme, 444 banks including 44 commercial banks (including 17 in the private sector), 191 RRBs and 209 co-operative banks along with 2,155 NGOs are now associated with the SHG-bank linkage programme.

While the SHG-bank linkage programme has surely emerged as the dominant micro finance dispensation model in India, other models too have evolved as significant micro finance purveying channels. The other successful models that have emerged are:

(a) An Intermediate Model that works on banking principles with focus on both savings and credit activities and where banking services are provided to the clients either directly or through SHGs.

(b) There is also a Wholesale Banking Model where the clients comprise NGOs, MFIs and SHG Federations. This Model involves a unique package of providing both loans and capacity building support to its partners.

(c) Further, there is an Individual Banking-based Model that has its clients as individuals or joint liability groups. While programme management and client appraisal in this Model may be a challenge, it is best suited to lending to enterprises.

Keeping these validated models for delivery of credit to the poor and the unorganized sector in view, RBI is moving towards a systems perspective for providing effective policy support not only because a number of different institutions including banks, MFIs, NGOs & SHGs are involved, but also because these institutions have very different institutional goals. With this in
view, a series of initiatives are being planned in the coming months for putting in place a more vibrant micro finance dispensation environment in the country, where complementary and competitive models of micro finance delivery would be encouraged to co-exist.

11.7.1 Foreign Investment in Micro Credit projects

The Government of India in 2000 included ‘Micro Credit/Rural Credit’ in the list of permitted Non-Banking Financial Company (NBFC) activities for being considered for Foreign Direct Investment (FDI)/Overseas Corporate Bodies (OCB)/Non-Resident Indians (NRI) investment to encourage foreign participation in microcredit projects. This covers credit facility at a micro level for providing finance to small producers and small micro enterprises in rural and urban areas.

11.7.2 Micro Finance Development Fund

In 2001 it was felt that there was an urgent need for micro credit providers to shift from a minimalist approach – that is offering only financial intermediation – to an integrated approach to poverty alleviation, taking a more holistic view of the client including provision of enterprise development services like marketing infrastructure, introduction of technology and design development. Therefore, the Micro Finance Development Fund was set up and a Rs. 100 crore Fund created in NABARD to support broadly the following activities:

(a) Giving training and exposure to self-help group (SHG) members, partner NGOs, banks and Government agencies.

(b) Providing start-up funds to micro finance institutions and meeting their initial operational deficits.

(c) Meeting the cost of formation and nurturing of SHGs;

(d) Designing new delivery mechanisms.

(e) Promoting research, action research, management information systems and dissemination of best practices in micro finance. This Fund is thus expected to address institutional and delivery issues like institutional growth and transformation, governance, accessing new sources of funding, building institutional capacity and increasing volumes. RBI and NABARD contributed Rs. 40 crore each to this Fund. The balance Rs. 20 crore was contributed by 11 public sector banks.
Check Your Progress Exercise 3

Note: i. Use this space given below to answer the question.
   ii. Compare your answer with the one given at the end of this unit

1. Describe the process of microcredit through SHGs

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2. Briefly outline the different models outlined for linking up SHGs with banks

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3. When was the Micro Finance Development Fund created and why?

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11.8 IN THE DEVELOPED WORLD

Microcredit is not only provided in poor countries, but also in one of the world's richest countries, the USA, where 37 million people (12.6%) live below the poverty line. Among other organizations that provide microloans in the United States, Grameen Bank started their operation in New York in April 2008. According to economist Jonathan Morduch of New York University, microloans have less appeal in the US, because people think it is too difficult to escape poverty through private enterprise. The Bank of America has announced plans to award more than $3.7 million in grants to non-profit organizations to use in backing microloan programmes.
Other developed countries in which the micro-loan model is, in fact, gaining impetus include Israel, Russia, and the Ukraine, where micro-loans given to small business entrepreneurs are also used to overcome cultural barriers in the mainstream business society. The Israel Free Loan Association (IFLA) has lent out over $100 million in the past two decades to Israeli citizens of all backgrounds.

Even so, efforts to replicate Grameen-style solidarity lending in developed countries have generally not succeeded. For example, the Calmeadow Foundation tested an analogous peer-lending model in three locations in Canada, rural Nova Scotia and urban Toronto and Vancouver, 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. However, debates have continued about whether the required subsidies may be justified as an alternative to other subsidies targeted at the entrepreneurial poor, and VanCity Credit Union, which took over Calmeadow's Vancouver operations, continues to use the process of peer lending.

Some organizations, however, have been able to find success bringing the microfinance model to the United States. ACCION USA, the US subsidiary of the better-known ACCION International, has been able to provide US$117 million in microloans since 1991, with an over 90% repayment rate.

### 11.8.1 Microcredit and 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, Lend for Peace, the Microloan Foundation, and iMicroInvest. Another web-based micro lender United Prosperity uses a variation on the usual micro lending model; with United Prosperity the micro-lender providing 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 non-profit 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.

11.9 CRITICISM

Enthusiasm for microcredit among government officials as an anti-poverty programme can motivate cuts in public health, welfare, and education spending. The success of the microcredit model has been judged disproportionately from a lender's perspective (repayment rates, financial viability) and not from that of the borrowers. For example, the Grameen Bank's high repayment rate does not reflect the number of women who are repeat borrowers that have become dependent on loans for household expenditures rather than capital investments. Studies of microcredit programmes have found that women often act merely as collection agents for their husbands and sons, such that the men spend the money, while women are saddled with the credit risk. As a result, borrowers are kept out of waged work and pushed into the informal economy.

Many studies in recent years have shown that risks like sickness, natural disaster and over-indebtedness are a critical dimension of poverty and that very poor people rely heavily on informal savings to manage these risks. It might be expected that microfinance institutions would provide safe, flexible savings services to this population, but—with notable exceptions like Grameen II—they have been very slow to do so. Some experts argue that most microcredit institutions are overly dependent on external capital. A study of microcredit institutions in Bolivia in 2003, for example, found that they were very slow to deliver quality micro-savings services, because of easy access to cheaper forms of external capital. Global data tables
from *The Microbanking Bulletin* show that savings represent a small source of funds for microcredit institutions in most developing nations.

Because field officers are in a position of power locally and are judged on repayment rates as the primary metric of their success, they sometimes use coercive and even violent tactics to collect installments on the microcredit loans. Some loan recipients sink into a cycle of debt, using a microcredit loan from one organization to meet interest obligations from another. Also, counter to the original intention of the microcredit system to empower women, one of the effects of an infusion of cash into local economies has been to increase dowries, with women forced at times to take microcredit loans as the only means to pay these increased dowries for their daughters.

In recent years, there has been increasing attention paid to the problem of interest rate disclosure, as many suppliers of microcredit quote their rates to clients using the flat calculation method, which significantly understates the true Annual Percentage Rate.

Professor Dean Karlan of Yale University, a point was raised concerning a comparison between two groups: one African, financed through microcredit and one control group in the Philippines. The results of this study suggest that many of the benefits from microcredit are in fact loaned to people with existing business, and not to those seeking to establish new businesses. Many of those receiving microcredit also used the loans to supplement the family income. The income that went up in business was true only for men, and not for women. This is striking because one of the supposed major beneficiaries of microfinance is supposed to be women. Professor Karlan's conclusion was that whilst microcredit is not necessarily bad and can generate some positive benefits, despite some lenders charging interest rates between 40-60%, it isn't the panacea that is purported to be. He advocates giving citizens in poor countries access to rudimentary and cheap savings accounts, rather than focusing strictly on microcredit.

Furthermore, there are widespread accumulations of studies that indicate that the Grameen Bank system does not reach very far down the poverty spectrum, either in absolute terms or relative to other income categories. So according to Tazul Islam, it risks the exclusion of the below poverty line, since the clients of the bank incline to be clustered around the poverty line of
predominantly moderately poor or vulnerable non-poor. Also, of the poor who join the bank’s microcredit programme, a high percentage often dropout after only a few loan cycles, while many others eventually dropout in later loan cycles as loan amounts begin to exceed their repayment capacity. For women, their loans are seen as the source of capital acquisition and this may lead to manipulation of women by putting pressure on them to gain membership of a credit group. Also, there are criticisms over microfinance institutions (MFIs) in creating small-debt traps for the poor with high interest rates and coercive methods of recovery. In Andhra Pradesh, the villagers who take out the loan often do not know the interest that they were being charged and are not aware of the consequences of taking multiple loans as they take the second loan to clear the first loan. Also, some studies reveal that the repayment rate of Grameen’s loans does not match anywhere near what the bank claims, that at least one quarter of its loans were being used for household consumption and there is no serious supervision of bank, which leads to bank delaying defaults and hiding problem loans.

**Negative Impact on Women**

Studies note that there is increase in domestic violence for women who do not get the loan or have to wait a long time to get the loan and often times their loans are given over to their male relatives or husbands. Women are more likely to retain control over their loans in traditional women’s work like livestock rearing that are considered “women’s work”. Moreover, the bigger the size of the loan, easier the women lose control on it. For example, Montgomery’s studies show that women have 100% control over loans that are smaller than Rs 1000, but only 46% of control if the loan is bigger than Rs 4,000. Women also face the situation that they have to depend on men when they cannot generate enough income, which can lead to gendered pattern of dependency and a new source of tension within the household.

**Check Your Progress Exercise 4**

**Note:** i. Use this space given below to answer the question.
ii. Compare your answer with the one given at the end of this unit

1. Describe the process of microcredit in developed countries
2. Briefly outline some of the problems with microcredit

11.10 SUMMING UP

In this Unit you have learnt about microcredit and its importance in alleviating poverty and empowering women. Economists and research scholars in have shown how small loans given to women can help in not only managing household financial needs, but also make them economically self-reliant in the long run. Though some critics of microcredit say that the loans obtained by women are often used by men in the households, who sometimes pressurize the women to take more and more loans, the role microcredit plays in helping women rise themselves and their families above the poverty line cannot be ignored.

11.11 GLOSSARY

**Target users** - The beneficiaries of any scheme or people at whom the programme or scheme is targeted. In the case of microcredit the target users are the micro entrepreneurs and low-income households

**Loan-sharks**: An individual or group of individuals who loan money to people at a high rate of interest, to repay which, the debtor takes more and more loans- often falling into an abyss of poverty and deprivation and being forced to sell all his possessions to the creditor.

11.12 ANSWERS TO CHECK YOUR PROGRESS EXERCISES

Check Your Progress Exercise 1

1. Microcredit can be defined as the extension of very small loans (microloans) to those in poverty. These loans are designed to spur entrepreneurship in individuals who lack collateral,
steady employment and a verifiable credit history and therefore cannot meet even the most minimal qualifications to gain access to traditional credit. Microcredit is a part of microfinance, which is the provision of a wider range of financial services to the very poor.

2. The Grameen Bank, which is generally considered the first modern microcredit institution, was founded in 1976 by Prof. Muhammad Yunus. Prof. 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. This microcredit came to be known as Grameen Credit.

Some of the features of Grameen credit are:

- Grameen credit is offered for creating self-employment for income-generating activities and housing for the poor, as opposed to consumption.
- Loans can be received in a continuous sequence. New loan becomes available to a borrower if her previous loan is repaid. All loans are to be paid back in installments and a person can receive more than one loan at a time.
- Grameen credit provides service at the door-step of the poor based on the principle that the people should not go to the bank, but the bank should go to the people.

3. Grameen credit’s thumb-rule is to keep the interest rate as close to the market rate, prevailing in the commercial banking sector, as possible, without sacrificing sustainability. In fixing the interest rate, market interest rate is taken as the reference rate, rather than the moneylenders’ rate. Efforts are made to keep the interest rate at a level which is close to a level commensurate with sustainability of the programme rather than bringing attractive return for the investors.

Check Your Progress Exercise 2

1. Group lending is a process in which the loan is given to a group of people and not an individual. 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 of one participant in group-lending depends upon the successful repayment of another member, thus transferring repayment responsibility of microcredit institutions to loan recipients.
2. Lending money through SHGs reduces transaction costs for both lenders and borrowers. While lenders have to handle only a single SHG account instead of a large number of small-sized individual accounts, borrowers as part of an SHG cut down expenses on travel (to & from the branch and other places) for completing paper work, and on the loss of workdays in canvassing for loans.

3. 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. 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. Microcredit is a tool for socio-economic empowerment.

Check Your Progress Exercise 3

1. Each SHG comprises of 20 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. Groups generally pay interest rates that range from 30% to 70% APR, or 12% to 24% a year, based on the flat calculation method. 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.

2. There are three basic models for linking up SHGs with banks. These include:
Model I: A linkage directly established with the SHGs without intervention/facilitation of any NGO now accounts for 16% of the projects.
Model II: A linkage established directly to SHGs with facilitation by NGOs and other formal agencies amounts to 75% of the projects.

Model III: A linkage established through an NGO facilitator and financing agency which represents 09% of the total linkage.

3. In 2001 it was felt that there was an urgent need for micro credit providers to shift from a minimalist approach – that is offering only financial intermediation – to an integrated approach to poverty alleviation, taking a more holistic view of the client including provision of enterprise development services like marketing infrastructure, introduction of technology and design development. Therefore, the Micro Finance Development Fund was set up and a Rs. 100 crore Fund created in NABARD to support broadly the following activities:

(a) Giving training and exposure to self-help group (SHG) members, partner NGOs, banks and Government agencies.

(b) Providing start-up funds to micro finance institutions and meeting their initial operational deficits.

(c) Meeting the cost of formation and nurturing of SHGs;

(d) Designing new delivery mechanisms.

(e) Promoting research, action research, management information systems and dissemination of best practices in micro finance. This Fund is thus expected to address institutional and delivery issues like institutional growth and transformation, governance, accessing new sources of funding, building institutional capacity and increasing volumes. RBI and NABARD contributed Rs. 40 crore each to this Fund. The balance Rs. 20 crore was contributed by 11 public sector banks.

Check Your Progress Exercise 4

1. Microcredit is not only provided in poor countries, but also in some of the world’s richest countries. Among other organizations that provide microloans in the United States, Grameen Bank started their operation in New York in April 2008. The Bank of America has announced plans to award more than $3.7 million in grants to non-profit organisations to use in backing microloan programs. Other developed countries in which the micro-loan model is gaining
impetus include Israel, Russia, and the Ukraine, where micro-loans given to small business entrepreneurs are also used to overcome cultural barriers in the mainstream business society. The Israel Free Loan Association (IFLA) has lent out over $100 million in the past two decades to Israeli citizens of all backgrounds.

3. According to some critics the high repayment rate in microcredit does not reflect the number of repeat borrowers who have become dependent on loans for household expenditures rather than capital investments. It has also been found that women often act merely as collection agents for their husbands and sons, such that the men spend the money, while women are saddled with the credit risk. Microcredit field officers are said to use coercive and even violent tactics to collect installments on the microcredit loans. Some loan recipients sink into a cycle of debt, using a microcredit loan from one organization to meet interest obligations from another. Also, counter to the original intention of the microcredit system to empower women, one of the effects of an infusion of cash into local economies has been to increase dowries, with women forced at times to take microcredit loans as the only means to pay these increased dowries for their daughters.

11.13 REFERENCES


www.grameen-info.org
www.rbi.org.in / nabard

11.14 QUESTIONS FOR REFLECTION AND PRACTICE

1. Analyze the importance of microcredit and its role in empowering women to rise above the poverty line.

2. What are the different models of micro-financing and what are their advantages?

3. What are the challenges of the microcredit program and how can they be overcome?