“Microcredit”

Microcredit is the practice of distributing very small loans to people who have a very low income as a means of poverty alleviation and economic development. Microcredit is a subset of the broader category of microfinance, which includes all financial services such as insurance and money transfers. The very poor often do not have access to any financial services, and microcredit enables individuals to borrow for a profit-making enterprise in hopes of beginning an upwards spiral out of poverty. In 2009, there were an estimated 150 million borrowers in 10,000 microfinance institutions (PlaNet Finance 2009).

The idea of giving very small loans to people who do not have access to banks has existed for a long time (CGAP 2006), but the current interest began with experimental programs in the 1970s with the Self Employed Women’s Association in India and the Grameen Bank in Bangladesh. Since then, microcredit has garnered a great deal of attention. The excitement about microcredit being the answer to the world’s poverty problems culminated with proclaiming the goal of alleviating all poverty through the practice of microcredit by the year 2005. In 2006, the Nobel Peace Prize was awarded jointly to Muhammad Yunus (the founder of the Grameen Bank) and the Grameen Bank itself.

The main innovation in microcredit is the use of “social collateral” to ensure repayment from borrowers who have little or no financial collateral. Social collateral is created by structuring the borrowing groups in various ways so that borrowers experience social pressure to
repay the loans. One standard microcredit program uses a group model where borrowers form small groups and are jointly responsible for the loans. Repayment is incentivized by using social structures. In one model, the borrowers in the group receive loans one at a time, so the next person in the rotation cannot receive a loan until the current borrower repays. In another, the entire group receives subsequent loans only if everyone repays in the current loan cycle. Because incentives are structured so that it is in the interest of each borrower for others to repay, borrowers are expected to monitor and apply social pressure to each other to repay the loans.

Much of the discourse about microcredit has focused on empowering women, although many programs lend to both men and women. Some critics say that women are not necessarily helped because the programs tend to define women’s needs narrowly in terms of the neoliberal agenda (Fernando 2005), while others say that women have been targeted in some societies because they are easier to bully into making repayments (Todd 1996).

Sociologists have observed microcredit groups in the United States to understand mechanisms of group cooperation, finding more borrowing is associated with group identity, sanctions and reciprocity, but only reciprocity is associated with less loan delinquency and group longevity (Anthony 2005). Gender differences in microcredit groups seem to result from expectations associated with group gender composition rather than the gender makeup of the groups themselves (Anthony and Horne 2003).

In other areas of the world, sociologists have made efforts to evaluate the success of microcredit programs, warning policy makers to exercise caution in applying microcredit approaches universally (Westover 2008; Hung 2003; Morduch 1999). Failure within group-based
microcredit programs have shown the importance of understanding the nature and extent of social relations among group members, between group members and staff, and among program staff (Woolcock 1999).

The use of group-based lending around the world has uncovered the importance of culture in economic activity where microcredit programs are administered. In rural China, deeply rooted Confucian traditions have been observed, and person-to-person obligations more important than person-to-group obligations. Therefore, despite strong interpersonal relationships, group-based obligations remain weak and borrowers were much more responsive to microcredit programs when they are structured in guarantor-borrower relationships (Hsu 2007). In Nepal, honor and social obligations in Newar society are considered a matter of great import for which women are willing to bear extraordinary costs, and attempting to build microcredit programs on existing reputations of honor was questioned as something that may have a more detrimental consequence than intended (Rankin 2002).

Scholars have observed that microcredit has affinities with neoliberalism, which is a major reason for its popularity with western donors. In other words, the ideology underpinning the microcredit movement is that the market is the solution to poverty, and that it can correct its own problems of inequality through economic growth and the creation of sustainable self-employment. Microcredit has been described as part of a larger agenda of “rolling back the state” which includes removing welfare provisions, dismantling labor protection, placing the provision of health and education in the hands of the free market economy (Mayoux 1995). Moreover,
although the loans are intended for profit-making, it is common for loans to be used for survival
(Morduch 2004; Rahman 1999).

REFERENCES AND SUGGESTED READINGS