Beyond micro-credit: an evolving microfinance

Microfinance is evolving and our understanding of it must too. Joanna Wilkin, drawing on her research and her experience working in microfinance for BRAC, argues that we need to reconceptualise microfinance and its priorities and to increase and extend access to financial tools to those previously ignored by the formal financial system, whilst keeping the role of governance, regulation and human collaboration intact.

"Global microfinance portfolios have grown explosively in recent years, linking the developing world's poor into the global financial system as never before. But the evolution of a once-niche development activity into a commercial business has been accompanied by growing concerns about whether practitioners have lost sight of their original social mission."

> – Amy Kazmin, The Financial Times, 7th December 2010

The summer of 2010 was a marked time in the history of microfinance. SKS microfinance, India's largest microfinance institution, went public raising almost $350 million through its IPO. Only two months later, it was blighted by negative press, after several suicides by its customers in the Andhra Pradesh state were linked to the pressure tactics of its project officers. The controversies were not only limited to India: the front cover of First News, a socio-economic review magazine based in Dhaka, lead with the story 'is [microfinance] the vaunted tool of poverty alleviation turning into a vicious trap of poverty aggravation?'

Weeks later, Muhammad Yunus became the focus of a damaging Danish documentary that claimed he had committed fraudulent activity, ciphering money allotted for the Grameen Bank to Grameen Kaylan. The consequence was his forced resignation from Grameen by the Bangladeshi government, with its Prime Minister, Sheikh Hasina reportedly calling Yunus and the entire Microfinance movement, 'the blood suckers of the poor'. For a once niche development project, the summer established the movements global presence as a political and financial tool, concomitant with the attention that often ensues.

The summer of 2010 then, was a defining point in microfinance; the introduction of a major non-Latin/South American microfinance institution into the global economy through an initial public offering represented more than an economic value. In a country where economic growth rates are predicted to soon match those of China, and where finance is becoming a substantiate industry, the connection between the rural poor and urban rich across all scales, whether locally regionally or globally, became increasingly interlinked; as exemplified by the negative effect the suicide crisis had on the SKS stocks, and the ramifications this had on regional and national government policy at the time. As Kasmin identifies, we are now witnessing an unprecedented integration of microfinance into the global financial system, whether in terms of: capital investment for commercial microfinance institutions; changing aims and concepts, such as financial sustainability; or even the integration of new financial products into microfinance schemes that are recognisant of the formal system. Microfinance has been an inherently socialised tool, born from gender and income inequality. Whilst its originators may have been educated in the West and their economics gleaned from market liberalism, microfinance, through its focus on women and productive activities rather than strictly profit-driven, ensures that it remains a development tool.

With the integration into the formal financial system resulting in microfinance becoming a keystone in the global economy, it is now becoming subject to more rules, more stringent governance and political scrutiny. The challenge is how we transform our understanding of microfinance to suit its new situation, inclusive of the political and economic ramifications, and its potential application in the future. Our basic conception of microfinance can be understood in a sentence:

> Microfinance is the provision of small loans to rural women on a weekly basis to invest in economically productive activities.

This common understanding of microfinance generates the standardised image of twenty or so sari-clad women congregating in the centre of their village paying in their weekly instalment after receiving their yearly loan. It is a system that works on trust and social pressure, with no need for collateral, and based on using local knowledge and local people. It also relies on high interest rates, fixed payment plans and potential social outcast for failure.

Microfinance, as we appear to know it, is a system of compromises that generates a multitude of viewpoints; those who support the movement argue that it provides access to finance to the inaccessible (or the 'financially untouchable'), empowers women by providing them with a financial and social position within their households and communities and helps alleviate poverty through smoothing income. Those against argue that the continual exploitation of people through unrelenting loan officers, the exorbitant costs of borrowing and the pressures on those not financially attuned, results in the aggravation of poverty. But how do we move on from these viewpoints? The 40 years of research and studies? How do we transform these to reflect contemporary microfinance? For this, we need to study the organisations, the industry and their tools, and not the effects of microfinance; there is a need to recognise that the microfinance movement is an evolution, not a revolution, and change has been occurring ever since Muhammad Yunus walked into the fishing village of Jobra.

Twenty-five years ago, it was the case that microfinance was conducted with small groups of rural women in full intent and purpose to improve the livelihood of the poor and improve the women's status within the household; this basic conception is referred to as microcredit from here on. Now, the many organisations, whether commercial or non-profit, incorporate much wider aims and the services they provide go beyond this microcredit, towards offering a way of 'micro-banking' to the poor. Focussing on the Bangladeshi microfinance industry, the two largest – and original – Microfinance Institutions, the Grameen Bank (GB) and BRAC have undergone major changes, in size, geographical outreach, in priorities and in structure. The GB has evolved within the Grameen umbrella of organisations, whether next to a non-profit fisheries programme to a commercial telephone company, the GB interacts with its as a recognisable national brand (for example, the GB 'telephone ladies' programme works in partnership with Grameenphone and Grameen Telecom). BRAC itself is a registered NGO with a dedicated microfinance division, which connects with its non-profit programmes such as Targeting Ultra-Poor and its commercial social enterprises such as BRAC Chicken and Aarong through various schemes.

The Bangladeshi microfinance industry is also beginning to change. The creation of the Microfinance Regulatory Agency (MRA) in 2006 was representative of step towards a more formalised and regulated financial industry. Though the impact of the MRA is yet to be seen – after all microfinance has operated in Bangladesh for the last forty years, whilst the MRA has for only five – it's main challenges in the initial period, to register all of operating microfinance institutions, has resulted in the closure of numerous 'illegal' microfinance schemes. Furthermore, their introduction of an interest rate cap at 27% last year, that was to be in place by July 2011, was one of the first official legislations that legitimated microfinance as a formal industry.

The change in microfinance does not only occur in the organisations and the industry environment, but also more importantly – and often missed in statistical and even development research – the financial tools which they offer. For both BRAC and GB, the introduction of multiple savings accounts (including compulsory, voluntary, long-term, and even insurance) and 'top-up' loans are just an example of new financial tools more akin to the formal financial system then the original social pressure loans. Studying just these two microfinance providers, and discussing their predictions for the future, suggests that the aim is to go beyond microcredit towards creating a formal (micro) finance sector. The introduction of consumer product loans, education loans, housing loans and even 'economic migration' loans are formulating a system that is not microcredit, but a new microfinance. And it is not only the content that is changing. For example, SafeSave, a small commercial microfinance institution set up by Stuart Rutherford in the slums of east Dhaka, has used handheld devices to record and transfer electronically customer accounts; a daily collection round by female slum dwellers employed by SafeSave also challenges the original weekly meeting structure to microfinance provision. The question is, where does this end?

An exciting prospect at BRAC in 2010, and no doubt GB, was the development of a mobile microfinance. With a proliferation of mobile technology in Bangladesh, and pertinently an extensive network coverage (provided also by Grameenphone), the potential for members to conduct their payments through their mobiles is apparent. For Bangladesh, a sparsely populated country in the majority, the formal system of local branches could easily be superseded by the advent of mobile (and even internet) banking. However, not only does this require a huge investment in technology, training and education (and hence capital), it also challenges our fundamental understanding of microfinance. Microfinance customers were inaccessible and untouchable; technology upsets the first, removing the need for weekly group meetings, but importantly the latter often remains.

Understanding the impacts these changes could have within microfinance must thus be a priority for all. The reason? The consequences of creating a pseudo, or shadow banking system, not dissimilar to that of the red-lining and predatory lending seen in the Dustbelt of the United States, could result in the marginalization of those microcredit was created for in the very first place: rural women. For example, during many interviews, the businessmen in the PROGOTI programmes with BRAC were asking for internet banking, overdraft facilities and credit cards. For the women in the villages, whilst it may not be rare to see a few holding mobile phones, the capacity for them to integrate and use the new technology to work for them, especially in such a cash-based society, is still a few generations off. Problems have already emerged in the changing system, including the need of a national insurance number and passport photographs as required documentation, going beyond the original requisite of community trust. As stated, microfinance was an inherently social tool born from inequality, a finance that worked for the bottom line through its simplicity; the introduction of demands that stem from the formal financial system, if left unfettered, could result in the system outpacing those who use it. Whilst the ambition may be there, as we have seen with the formal financial system (and subprime mortgages working on teaser rates), there is a need for an education to occur concurrently to the provision financial tools. As we reconsider our understanding of what microfinance is, we must not forgot to recognise its clients, tools and institutions. The transformation from microcredit to microfinance, understanding and intent in providing a formal financial system that works for its customers and their needs.

So where does this leave us? For many, it may be uncouth to argue that microfinance should now no longer aim primarily to work to alleviate poverty or empower women (though this may be the role of microcredit). If microfinance is to continue to integrate into the formal financial system, which undoubtedly it will (whether through IPOs or the tools provided), we need to reconceptualise microfinance and its priorities; to increase and extend access to financial tools, to those previously ignored by the formal financial system through programmes and methods that work to an efficacy that suits its customers. Put simply, microfinance should aim to create a 'finance for the poor'. Whether this viewpoint is too liberal, or even possible in our capitalist economy, the role of governance, regulation, and as shown by Yunus and Abed, human collaboration rather than greed cannot be ignored. Microfinance is evolving, and our understanding of it must too.

1 Ferdous, F. and Uddin, G.M. (2010), 'Microfinance', First News, 8th August 2010, p. 1, 36-47.

2 Personal Communication, part of Author's Dissertation research, "Heading Towards Commercialisation? Continuing NGO Participation in Microfinance", (unpublished), May 2011.

Joanna read for a Bachelor of Art in Geography at St. Peter's College, University of Oxford; during her time at University, she pursued her interest in the relationship between development and finance, specialising in Financial Geography. Her undergraduate dissertation was completed under the title "Heading Towards Commercialisation? Continuing NGO Participation in Microfinance. BRAC: A Case Study." The blog is partly based on research conducted in Bangladesh during a Summer Internship (2010) in the Microfinance Department at BRAC, one of the largest NGOs participating in providing microfinance. She acknowledges that it is only through the internship and the experiences providing by BRAC that her own personal microfinance education really begun.

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