STUDIES IN POVERTY AND INEQUALITY INSTITUTE

Building up knowledge to break down Poverty

Dynamics between savings and credit for low-income households

Literature review

July 2013

Brian Mathebula

STUDIES IN POVERTY AND INEQUALITY INSTITUTE

Building up knowledge to break down Poverty

31 Quinn Street, Newtown
Johannesburg
South Africa
2000
Phone: + 27 11 833 0161
Fax: + 27 11 832 3085

Twitter: spii1
Facebook: SPII
Email: advocacy@spii.org.za
www.spii.org.za

1. Introduction

Access to microfinance and microcredit for the poor has sparked critical debates over its 'acclaimed' successes and failures. Advocates of the microfinance agenda argue that expanding access to microfinance and microcredit to the poor forms an important constituent of the new developmental agenda. Becker *et al* (2008) argue that financial 'exclusion' is a barrier to economic development, and that there is a need to build financial systems that will foster more financial 'inclusion'. Murdoch (1995 and 2005) argues that due to its positive results, the microfinance sector has grown, expanded and gained popularity. Impact assessments on the effects of access to microcredit on the poor indicate that it can improve the welfare of the poor.[1] Access to microcredit is seen as a mechanism that enables poor people to mitigate short term financial constraints and economic shocks. Since gaining popularity in the 1980s, the Grameen Bank has ushered a new way of thinking around access to microfinance and financial inclusion for both state and non-state actors.

Despite its popularity and expansion, in recent times, developmental scholars have questioned the impact assessment of these microcredit programmes. Duvendack and Jones-Palmer (2012) argue that there is little convincing evidence that microfinance programmes have positive impacts at a sustainable level.[2] The rise in the number of impact assessments that show positive effects of microcredit programmes has also seen an increase in the number of sceptics of these results. This has led to more studies being undertaken that seek to question these 'iconic' studies.

In their 2011 exploratory work, *'Too much Microcredit: A Survey of evidence on the over indebtedness*", Schicks and Rosenberg (2011)[3] point to the limitation in data in the microcredit sector to enable a conclusion to be drawn with regards to the levels of indebtedness for participants. The intimate relationship that exist between microfinance and neoliberalism is seen to poise problems as there is evidence to suggest that policies and institutions could deliberately be favoured simply because they support the neoliberalism and globalisation agenda.[4]

---

[1] Karlan, D, and Zinman, J (2008). Expanding Credit Access: Using Randomised Supply Decisions to Estimate the Impacts. Innovation for Poverty Action, M.I.T Jameel Poverty Action Lab. Financial Access Initiative.
[2] Duvendack, M and Palmer-Jones, 2012. High noon for microfinance Impact Evaluation: Re-investigating the evidence from Bangladesh.
[3] Schicks, J and Rosenberg, 2011. Too much microcredit : a survey of evidence on the over-indebtedness. CGAP, Occasional Paper
[4] Bateman and Chang, 2013. The Microfinance Illusion.

This paper aims to provide a literature review which covers both sides of the argument with regards to the 'acclaimed' successes and 'supposed' failures of the microfinance and microcredit agenda. In order to do this, the paper provides evidence from existing literature on microfinance, in order to showcase current performance record of such programs and effectiveness/ineffectiveness in reducing poverty. International experiments of microfinance initiatives across the globe will be highlighted. In addition, the paper will discuss key issues that have been raised by those who oppose microfinance agenda and the methodology.

2. Discussing microfinance and microcredit

In 2005, the World Bank reported that 500 million of an estimated 3 billion people in the developing world had access to formal sector financial services.[5] This number shows that one-sixth of the world's poor population still did not have access to such services, and one-sixth represents a significant gap in access to formal sector financial services. The poor and marginalised do not have access to formal financial sector services and as a result, most of them rely on informal financial sector service channels. Informal sector financial service channels are more costly, inefficient, and even when they are successful, they do not offer the user to establish a credit history and this affects their ability to acquire future loans.[6]

Otero cited in Wrenn (2005) defines microfinance as "the provision of financial services to low-income poor and very self-employed people".[7] Schreiner and Colombet cited in Wrenn (2005) define microfinance as "the attempt to improve access to small deposits and small loans for poor households neglected by banks".[8]

---

[5] Khander, Shahidur R, 2005, Microfinance and poverty: data from Bangladesh. The World Bank Economic Review, vol.19 (2), p. 263-286.
[6] The World Bank, available at http://web.worldbank.org/WBSITE/EXTERNAL/NEWS/0,,contentMDK:20433592~pagePK:64257043~piPK:437376~theSitePK:4607,00.html. updated March 2013.
[7] Wrenn, E. 2005. Microfinance: Literature review.
[8] Ibid.

Provision of microfinance to low-income households includes providing services such as insurance and payment services. In addition, these also include financial services such as savings, loans and insurance to poor people in both urban and rural setting who are unable to obtain such services from formal financial sector. Provision of microcredit is seen as forming an important aspect of microfinance. In this respect, microcredit makes available credit to the unemployed, entrepreneurs, who are considered "unbankanble" because they lack collateral, steady or permanent employment, income and verifiable credit history and in most instances they do not meet the minimum requirements of the mainstream formal sector- financial institutions.

Sengupta and Aubuchon (2008) state that microcredit and microfinance are often used interchangeably, however, it is important to recognise the distinction between the two. Microcredit refers to the act of providing the loan, whilst microfinance refers to the act of providing these same borrowers with financial services, such as savings institutions and insurance policies.

Microfinance can be defined as "banking the unbankable".[9] At the core of the provision of microfinance and microcredit to the poor is the ability to assist households and individuals to mitigate the impact of shock and reduce risks through the creation of income generating opportunities. The foundation is that if household income is increased, this will enable the household to accumulate assets, smooth consumption, and wealth creation and increase investments in education and improve the food security at a household level.

Literature also shows that microcredit has focused on the provision of credit to women. Women often represent the poorest segment of the population, especially in the Global South. Furthermore, women make up the largest number of the unemployed, and due to their payment history, they represent a smaller credit risk for the microfinance provider because they pay timeously. Lastly, making credit available to woman is seen as having more multiplier effects to the entire household, as the money will used to better the wellbeing of the household.

[9] http://www.microfinanceinfo.com/the-definition-of-microfinance/

Dr Mohammad Yunus, who is also the founder of the Grameen Bank in Bangladesh, was awarded a Nobel Peace Prize for the work he has done around provision of microcredit to the poor. Mohammed Yunus has also been credited for coming up with the concept of microcredit.[10] The concept of microfinance and microcredit represent a significant shift in the provision of financial services for the poor. Mohammed Yunus and the Grameen Bank since 1976 have been experimenting with innovative ways to provide financial services for the poor. Wrenn (2005) states that prior to the 1970s, previous attempt to provide financial services to the poor by donors and governments was mainly in the form of subsidised rural credit programmes. These programmes failed to achieve intended objectives as they resulted in high rates of loan defaults, high losses and was not able to reach the poor at scale.[11]

According to Robinson (2001), the 1980s represented a major a turning point for the microfinance sector. The concept started gaining prominence as a targeted developmental approach that was effective for poor/low-income households. This was a result of the experiences of the Grameen Bank in Bangladesh, more especially, their ability to provide loans and savings services profitably at a large scale. What made this microcredit model appealing to the international community is that it was fully commercially funded, and was not reliant on state or donor funding. However, it remained fully sustainable.

By the end of the 1980s, enough evidence was available to suggest that microfinance could be provided at a large scale with profitable returns for microfinance providers. As a result, the last two decades has seen a significant rise in the number of microfinance institutions, with an emphasis of reaching scale. Due to the apparent demand amongst the poor for other services such as savings and pensions, the microfinance sector in the 1990s experienced a shift in focus to include these services.

The Grameen Bank concept of microcredit was conceptualised as means that could enable the poor to establish or expand on their economic generating activities. With growth, expansion and popularity, the concept has progressed to capture more than microcredit; it has rather, come to include a wider concept of microfinance.

---

[10] Ibid.
[11] Ibid.

4. International experiences with microfinance and microcredit

In the last 20 years, impact evaluation studies on the effects of access to microcredit for the poor have been undertaken and results indicate an improved welfare of the household and poverty reduction. Subsequently, these studies have gained 'iconic' status. It has also been argued that the results from the impact evaluation have shaped/legitimated in some contexts, policy development, more especially in the developing world.[12] Provision of microfinance has been credited for assisting the poor to access credit, remunerative activities and relieving them of onerous debts, and when targeted at women, there are more multiplier effects. Duvendack and Palmer-Jones (2012) argue that research studies such as work by Pitt and Khandker (1998) that have authoritatively supported this notion. Research on the impact of microfinance tries to link and expand the role of financial inclusion and its impact on the people that exist outside the scope of mainstream formal financial system. These studies also show that there are positive impacts of access to microfinance at the macro level, including poverty rates, and poverty impacts from expansion of bank branches network on aggregate poverty.[13]

- **Impact of microcredit in Bangladesh**

Bangladesh has been operating the largest microcredit programmes in the world for the last 30 years. Between 1996 and 2007, the World Bank[14] financed programmes to the value of US$ 260 million, reaching 6 million poor households individuals in the country. Women made up the largest number of recipients of the programmes. Results show that the finance was used in various economic generating activities such as small grocery shops, trading stores, tailoring, rickshaw pulling and agricultural activities such as rearing cattle, poultry and farming fish.

---

[12] Duvendack, M and Palmer-Jones, R, 2012. High noon for microfinance impact evaluations: re-investing the evidence from Bangladesh. Journal of Development Studies. Oversee Development Institute
[13] Ibid
[14] http://web.worldbank.org/WBSITE/EXTERNAL/NEWS/0,,contentMDK:21153910~pagePK:34370~piPK:34424~theSitePK:4607,00.html

Evaluations of the impact of microcredit on a sample of borrowers carried out in 2001 found that:	99% report increase in income, often by more than 15%
	96% report improved quality of life
	99% eat better and more food
	99% are clothe better
	86% live in better housing
	88% are now able to send children to school
	83% have better access to sanitation
	55% of rural borrowers now own land
Source: World Bank , 2001	

Furthermore, the Financial Services for the Poorest programme, which piloted microfinance initiatives in 18 districts achieved positive results, to the extent that, the Bangladeshi government replicated the project at a larger scale. The Financial Services for the Poorest programme was introduced by the World Bank, and aimed to build on the success of the microcredit programmes in the country. This programme targeted those that did not qualify for the conventional microcredit, such as beggars or household help.

The Bangladeshi government replicated the project across the country with excellent outcomes	**Results**
	Around 450, 000 of the poorest of the poor have benefited
	Repayment rate has been more than 95%
	Already 20, 000 of those who received micro-credit 3 years ago can now access regular rural microcredit programs
	More than half of these borrowers no longer live on less than a dollar a day
	Most of the recipients have upgraded their housing conditions from "jhupri" to semi-durable structures within 3 years.
Source: World Bank , 2001	

- **The Jipange KuSave Experiment in Kenya**

The Jipange KuSave (meaning to 'organise one to save') Experiment in Kenya was an adaptation of P9[15] in Bangladesh. The model allows the client to repay at their own pace, and only when the client

[15] P9 is based on a principle *"lend to save model"*, which enables clients to access loans with no interest. In this '*lend to save model'*, one third of the loan is located in a savings account.

has repaid the loan in full are they eligible for a larger loan under the same conditions. [16] Fundamental to the P9 model is the provision of easily accessible quick liquidity to enable clients to handle day to day monetary management needs, whilst providing mechanism which will enable the poor to save.[17] The adaptation of P9 in Kenya was through M-PESA[18]-a mobile payment wallet in Kenya. The Kenyan mobile network has over 35,000 cash –in and cash-out agents and a transaction volume of US$665 million per month. Between 2007 and 2012, M-PESA moved from having over 1 million clients in the first year, to 15 million registered users. In 2010, a new company (Mobile Venture Kenya Ltd) in Kenya decided that Kenya provided the right context to adapt the P9 from Bangladesh.[19]

Results from the experiment show that clients are "interested in a product that delivers immediate liquidity and a convenient savings feature. Usage levels and average speed of repayment are sufficient to ensure the products' viability. Clients are willing to pay the fees included in the product design in exchange for greater customer experience based on speed and convenience. Client's repayment behaviour will remain constant even when intensity of reminders calls is reduced. The product can be delivered to mass market low-income clients through a mobile channel (although initial client acquisition requires the direct involvement of agents)". [20]

Rotman *et al* (2012) points out that this experiment shows that there is a room, desire and demand from those who are not part of the mainstream financial system for financial services that are different from current models offered. However, from the pilot study there was not enough evidence to suggest that there was room for a standalone business, which could be created to meet this demand or whether it must inevitably form part of an existing regulated provider. [21]

- **The KGFS Model in India**

Kshetriya Gramin Financial Services (KGFS) aims to provide access to financial services to every individual and enterprise. The KGFS has four institutions operating in India that are using different

[16] Rotman, S, Ferrand and Rasmussen, S, (2012). The Jipange KuSave Experiment in Kenya. CGAP Brief
[17] Ibid
[18] M-PESA enables users to move money using mobile technology move money around.
[19] Ibid
[20] Ibid
[21] Ibid

legal structures that aim to enable access to a wide range to financial products, such as savings accounts through appropriate risk-sharing with partner financial institutions.[22] Geographical commitment is fundamental to the model design. The model design put emphasis on regional institutions servicing a specific territory with distinct geographical, economic and linguistic characteristics. A KGFS branch should be at least seven kilometres from the nearest town centre and the service area should not extend beyond five kilometres from the nearest branch office. The model aims to maximise on in-depth knowledge of a particular area and deepening relationships with its clients. Uptake through enrolment enables clients to access services from ten KGFS. It takes approximately 30 minutes for potential clients to enrol, without an enrolment fee.[23]

The branch staff, who are commonly referred as wealth managers are tasked with gathering baseline information on the client's information income, expenditure assets and liabilities. During the baseline investigation, adults in the household identify five household financial goals, such as covering marriage expenses, having income for old age, paying school fees, or purchasing property. The information gathered during the baseline investigation is used to generate a financial well-being report, which is then used to develop recommendation of financial products for each client.

KGFS model in India	**Results**
	• -Branches in existence for more than 30 months have an average enrolment rate of nearly 70%. • spatial dimension critical • -in Tamil Nadu, enrolment happened across a spectrum of income levels, with the largest share distributed among households with between $500 (INR 25,000 to $2,000 (INR 100,000) annual Income • Substantial demand for non-credit services amongst residents • There was a heavy demand for personal accident insurance, driven by the need to protect the income of household bread-winners. • There was a similar need for protection drives in terms of life insurance requests. • -Over 60 of enrolled households in the Tamil Nadu KGFS are insurance clients. Almost 20,000 clients signed up for the National Pension Scheme Lite product in the first 18 months after it was launched.
Source: Anath *et al*, 2012	

Questions have been raised with regards to the adaptation and appropriateness of the KGFS model in varied countries with different contexts. This approach has not been tested in more urban

[22] Anath, B, Chen, G and Rasmussen, 2012. The Pursuit of Complete Financial Inclusion. The KGFS Model in India. Access to Finance Forum, Reports by CGAP and partners, No.4 May.
[23] Ibid

localities where distances are shorter, more services choice exists and financial services needs are different. If the regional coverage increases or decreases, this might warrant an adjustment to ensure viability, while not losing the emphasis on deep local knowledge.[24]

- **Impact of microcredit in Africa**

Launched in 1999, The Hunger Project (THP) Microfinance Program[25] has reached over 2, 4 million across 8 countries on the continent. This programme has also reached 21 rural banks, these banks: - have qualified as independent, community owned, woman led rural financial institutions. THP provides training, savings and credit focusing on supporting female producers at the bottom end of the food chain on the continent. This programme has allowed participants to partake in income generating activities. The programme has also seen participants increase their income to a position whereby they are able to invest and expand in their businesses. One of the key results from the programme is that participants, through this programme were able to pay school fees, access health care and build and improve their homes.

South Africa

The last 19 years in South Africa's social and economic development has revolved around reversing the legacies of decades of successive legislated racial discriminatory practices under the apartheid regime. During his 2003 State of the Nation, President Thabo Mbeki coined the term 'dual economy' within the South African economy, namely the first and second economy. [26] In his analysis, Mbeki aimed to highlight the plight of the poor in South Africa and structural fault in the economy. Calvin and Coetzee (2009) states that the 'dual economy' has largely defined the microfinance sector in South Africa. In 2013, using the unofficial unemployment rate, which includes those who have been discouraged to look for work, over 35% of South Africans were unemployed.[27] In the South African context, those who are better educated participate in the first economy, and those who are less

[24] Ibid.
[25] http://www.thp.org/
[26] The first economy is modern, rivals economies in the developed world and produces the bulk of the country's wealth. The second economy consists of the majority of the population who are located in both rural and urban areas.
[27] Statistics South Africa, 2013, Quarter labour Force Survey, Q1.

educated are reliant on the second economy for survival. [28] The black majority continue to live in poverty as they remain on the peripheral of economic and social development.

In his 2011 Budget Speech, Minister of Finance, Pravin Ghodhan emphasized the need to 'transform the financial sector' in South Africa.[29] The transformation of the financial sector highlights the deep underlying issues in the South African finance sector.[30] Historically, the finance sector did not cater to previously disadvantaged groups. Calvin and Coetzee (2009) note that the microfinance sector in South Africa is one that in maturing and with scope for expansion. The microfinance sector in South Africa is heavily based on two primary products: micro deposit services and salary based microloans. Calvin and Coetzee (2009) note that in microenterprises lending is lagging behind achieving less than 20% of potential market penetration.[31]

Microfinance category by product in South Africa	
Microcredit services	• Banked population increased from 14,3 million or 47% in 2005, reaching 20,0 million or 63% in 2008. • However, during the recession of 2008/2009, the number dropped to 19, 0 million. • The increase can be attributed to variety of factors, namely, legislation that required major banks to create products for previously unbanked and the response by the financial sector institutions. • The creation of Mzansi account (designed for low-income households) by the four large banks and emergence of three smaller banks and Postbank reaching the low-income market
Salary based microloans	• Despite the 2008/2009 recession, the primary microloan saw an increase between 2007 and 2009. The value of short term credit agreements granted in the quarter grew by 5% from R883 million to R928 million. • Of the loans granted, 72% were granted to individuals with monthly incomes below R3500 and 80% of these were 30 day loans. • However, declined over this period by 26% from 444 000 to 352 000 and the debtors book outstanding for short-term credit dropped by 13% from R682 million to R594 million.
Microenterprises loans	• Remains underdeveloped • Three microenterprise lending organisation is the space (Small Enterprise Foundation, Women's Development Business and Marang Financial Services) • These organisations utilise a group-based methodology and active loans at their respective 2009 year ends totalled 115 000, compared with the estimated market of survivalist segments approximating 2 million. • With annual loan loss rates consistently below 5% of average portfolio, the three large organisations have proven that strong portfolio quality can be maintained

[28] Calving, B and Coetzee, G, 2009. A review of the South African Microfinance Sector: Success, Challenges and Policy Issues. Centre for microfinance and FinMark Trust. Volume 1, Summary of Findings.
[29] Pravin Ghordhan, 2011. Budget Speech. National Treasury.
[30] Two pieces of legislation have been credited for the development of the microfinance sector in South Africa, namely the namely the National Credit Act (NCA), No. 34 of 2005 and the Cooperatives Banks Act (CBA), No. 40 of 2007
[31] Ibid

	utilising a group-based methodology.
Source: Calving and Coetzee, 2009.	

A 2011 country report by CGAP looked at the payment of cash transfers grants across four countries (Brazil, South Africa, Mexico and Colombia). In South Africa, social assistance, which is commonly known as 'social grant system'[32], form an important part of state's poverty alleviation strategy. The study by CGAP sought to answer the following questions by exploring three areas of enquiry: (a) use of accounts by recipients, through analysis of transactional data; (b) costs to banks and governments; and (c) perceptions of recipients about ease of access, challenges by the payment process, and value placed on having access to the account.[33]

Financial inclusion and social grants	
A 2011 South Africa country report by CGAP (Covers interviews with three government agencies (Department of Social development, South African Social Security Administration, National Treasury, Standard Bank, ALL PAY and 10 focus groups)	• No indication from the interviews that there was no clear coordination between government departments with regards to greater inclusion on financial inclusion to social grants. • It is noted that between both the government department, which included DSD and SASSA, the question of financial inclusion was shifted towards Treasury. Both DSD and SASSA saw the role of financial inclusion with regards to social grants falling within the jurisdiction of Treasury. • In the latest SASSA application for the tender, which is for the distribution of Social grants, had a marker on the winning bid to place emphasis on financial inclusion. This tender "application did not include a mechanism for rewarding tenders that address this objective compared to other more fundamental aspects of the cash delivery system." • SASSA had the objective to migrate recipients from cash payments to electronic payments, as noted by CGAP (2011), this move was motivated by the need to reduce the cost of delivering this service than pushing the financial inclusion agenda.

5. Criticism of microfinance

The microfinance sector has grown, expanded and gained popularity in the international community in the last 30 years as a vehicle to reduce poverty. Most of the studies that are undertaken in this microcredit market have mostly shown positive impacts. This notion has seen the rise in sceptic of these results. Schicks and Rosenberg (2011) in the exploratory work *"Too much Microcredit: A survey of evidence on the over-indebtedness"* discuss the underlying conceptual issues and limitation

[32] Work by Samson et al (2004), which was commissioned by the Department of Social Development (DSD) indicate that these grants have assisted in the reduction of poverty, promoted household development and have produce positive outcomes in health and education. The social grant is administered under the SASSA Act of 2004, and it is funded by National Treasury. However, the Department of Social Development oversees the policy development.

[33] CGAP, 2011, CGAP G2P Research Project: South Africa Country Report.

in data in the microcredit sector. Over indebtedness implies the heightened levels of vulnerability and can contribute to the impoverishment of borrowers. In this instance, material effects of over-indebtedness can have the following effects on borrowers; reduced consumption levels, late fees, asset seizures, downward spiral of ever-increasing debt, and eventually, a loss of creditworthiness. Furthermore, over-indebtedness can also have socio-logical and physiological effects on the borrower. Schicks and Rosenberg (2011) argue that due to the lack of enough data across the various macro-credit markets, it is difficult to draw conclusion about the prevalence of over indebtedness in most microcredit markets. [34]

Summary of empirical studies on microcredit

Setting (author)	**Methodology**	**Definition of over-indebtedness**	**Findings**
Bolivia 1997-2001 (Gonzalez 2008)	Household (HH) survey	Costly unanticipated actions to repay	85% of HH had at least one occurrence during the four years
Ghana 2009 (Gramming 2008)	Rapid market assessment, borrower surveys, info exchange between MFIs	Microbusiness recapitalizing (as assessed by researchers)	12% over indebted, another 16% at risk
Country X 2009 (restricted report)	Debt service and expense data from credit bureau and loan files of lenders	Debt service greater than 100% of HH income net of other expenses	17% over-indebted and another 11% at risk (debt service 75-100% of net income)
Kamataka, India 2010 (Krishaswamu 2011)	Loan records and HH survey	Subjective report of stress; sacrifices to repay	Over-indebtedness reportedly high in mass default towns, but low in nondefault towns.
Tamil Nadu, India 2005-2009 (Guerin, Roesch, Subramanin, and Kumar 2011)	Qualitative interviews, observation, and HH survey (N=344)	Impoverishment through debt	More (possibly much more) than 20% over-indebted
Multi-country study (Kappel, Krauss, and Lontzek 2010)	Preliminary composition of an early warning index, largely based on signalling analysis with an MFI survey + MIX market data	Chronic and involuntary inability to meet all payment obligations by means of the household's excess cash. Proxies: arrears, write-offs, loan losses, debt-service ratio	14 potential early warning indicators for over-indebtedness. Highest risk countries in sample: Bosnia-Herzegovina, Cambodia, Peru
Source: Schicks and Rosenberg (2011)			

Duvendack and Jones-Palmer (2012) have argued that there is little convincing evidence that microfinance programmes have positive impacts. In their 2012 study, Duvendack and Palmer-Jones

[34] In this paper, indebtedness includes those that have serious problems repaying their loans. Using this definition, borrowers can be over-indebted even if they are repaying their loans.

(2012) test the robustness of propensity score matching results to selection on observables using sensitivity analysis, and investigate propensity score matching estimates of impacts by gender of borrowers. They argue that "the mainly insignificant impacts of microfinance differ greatly by gender of borrower, but are all vulnerable to selection on observables. We are therefore not convinced that the relationship between microfinance and outcomes are causal with these data".[35]

Robinson in Karlan and Zinman (2008) states that there is less consensus on the role of consumer credit, especially when it is at scale. Current trends with regards to lending patterns show that microfinance institutions are rapidly moving away from the "traditional" forms of lending which were initially geared towards entrepreneurial credit and are now focusing more on providing consumer loans. Robinson (2001) warns that this shift in lending patterns might prove 'unproductive'. Work by Stango and Zinman (2007) shows that with regards to consumer credit, consumers tend to underestimate the interest on short term instalment loans, and in most instances, they tend to borrow heavily and expensively. [36]

In their paper *'The Microfinance illusion'*, Bateman and Chang (2013) argue that despite its growth and expansion since its 'discovery' in the 1980s, it is a given assumption that their impact has been positive with regards to poverty reduction and development. Due to this, there has been strong correlation been drawn that 'more microfinance' will lead to 'more poverty alleviation'. Despite the World Bank initially dismissing the concept as a poverty reduction methodology in the 1980s as being too 'leftist', the change in approach by the World Bank [37] has led Bateman and Chang (2013) to draw the conclusion that the support for the microfinance agenda by the USAID[38] and World Bank was asserting the intimate relationship between microfinance and the neoliberalism agenda. Apotheosis for the microfinance movement came in 2006, with the award for the Nobel Peace Prize jointly to Dr Muhammad Yunus and the Grameen Bank".[39] The association between microfinance and the neoliberalism is seen to poise problems as there is evidence to suggest that policies and institutions could deliberately be favoured simply because they support the neoliberalism and globalisation project.

---

[35] Ibid

[36] Stango, V and Zinman (2007a). Fuzzy Math and Household finance: Theory and Evidence'. Working paper. November. Stango, V and Zinman (2007b). Fuzzy Math, Disclosure Regulation, and Credit Market Outcomes. Working Paper. November.

[37] The World Bank started providing significant technical advice and financial support for new microfinance programmes.

[38] Through the USAID, the microfinance agenda was pushed as the 'best practice' and many US-based NGO's started using this new agenda to pursue poverty alleviation interventions. The Consultative Group to Assist the Poor (CGAP) also started endorsing the new MFI concept.

[39] Bateman and Chang, (unknown), The microfinance illusion. Accessed at http://www.econ.cam.ac.uk/faculty/chang/pubs/Microfinance.pdf. July 2013.

More importantly, Bateman and Chang (2013) have argued against the notion that microfinance represents a new way to approaching the social and economic developmental agenda. In fact, they argue that the new microfinance agenda constitutes a new and very modern powerful form of poverty trap. Work by Lont and Hospes (2004) also questions the optimistic view with regards to the microfinance agenda as the setting the developmental agenda. Ellerman (2007) also raises the question regarding the methodical approaches used in these 'impact evaluations', by stating that they are widely used to 'prove' the positive impacts of microfinance. Murdoch (1998 and 2005) in Bateman and Chang (2013), a long term advocate of the microfinance agenda admits that "rigorous evidence that shows it happening just doesn't exist ……The evidence is pretty dicey"[40]. Also, there is actually surprisingly little evidence to suggest that the microfinance model in Bangladesh has succeeded in establishing a sustainable and generalizable exit mechanism out of poverty. Compared to its counterparts and neighbouring South and East Asian countries, Bangladesh is one of the least successful in sustainably reducing poverty and promoting 'bottom-up' productive enterprise development.

One of the key issues raised with regards to the microcredit model, is the saturation of micro-enterprises. This is seen as being widely problematic, especially in developing context.[41] This can lead to lenders lending to too many micro-enterprises in market that will not grow due to over-crowding and market saturation. Also, lack of development in key technologies in the developing world is seen as key constraint to the development, especially in the informal sector. This micro-enterprise funding model is seen as not addressing these core sustainable development imperatives, as compared to same models that were undertaken in the EU and East Asian, where the microenterprise sector was strongly promoted as an agent of technology absorption and diffusion and local technology. As a result, Bateman and Chang (2013) argue that for this form of microfinance to actually world in the developing country contexts is to support those enterprises that can repay their expensive microloans in the short period permitted.[42]

[40] In his 1998 and 2005 work, Murdoch stated on the effects of microfinance that they can improve the welfare of the poor.,

[41] In 2007, the Indian government was forced to close down many MFI in the state of Andhara Pradesh were 'hard selling' microfinance and putting their own growth and profitability in a crowded market way ahead of the ability of the poor clients, including very many new tiny retail outlets, to productively use and repay any microloan.

[42] Ibid

Bangladesh, with the 'achievements' of the Grameen Bank are considered the leaders in the microfinance sector. The last 30 years has seen a significant increase in the number of informal sector microenterprises in their large cities, and this seen as problematic[43]. . Due to the increase in the number of micro-enterprises, this sector is becoming hyper-competitive with declining returns. The concern is that the increase in microenterprises activities, coupled by high interest rates charged by many new commercial MFI's[44], this could lead many microenterprises getting into debt.

6. Conclusion

There are many positive results reported on the impact of access to microcredit to the poor, and thanks to the achievements of Grameen Bank and their innovativeness in this regard. More than anything, the microfinance agenda does represent a significant and an alternative approach to reaching those that have been historically neglected by the mainstream formal sector financial institutions. Despite these reported 'achievements', as pointed out by scholars who disagree with the microfinance model, there are still questions that linger with regards to the sustainability of this model. The lack of data, as pointed out by Schick's and Rosenberg (2012) over the levels of over-indebtedness of credit receivers also raises pertinent questions. The fact that these impact evaluations are mostly undertaken by either the funder or the MFI's does not stand well with the sceptics, as questions will forever remain with regards to the 'acclaimed positive' impact and validity of the findings.

With regards to addressing the challenges of the poor, just as in the industrialised world, the 21st century has ushered a radical shift in thinking around poverty in the Global South that has been heavily influenced by better understanding of the impact of neoliberalism, social protection and international aid. Countries like South Africa, Brazil, India and Mexico have adopted different, but equally lauded social protection programs. These conditional cash transfers programs provide a consistent and predictable source of income and have an excellent record of getting small sums of cash to those in need. These programs are well targeted and they provide an improved mechanism for providing small sums of money to those in need, without the added risk of microcredit. The

[43] More than 63% of the population in the Capital City Dhaka is now located in the informal sector.
[44] The microenterprise fails; the microloan has to be repaid by selling long-held family assets (equipment, land, buildings, etc) which could lead to further indebtedness.

South African example, whereby new social grant (cash transfer), are paid through a bank account provides a great opportunity to build the financial inclusion for low-income households.

SPII
STUDIES IN POVERTY AND INEQUALITY INSTITUTE
Building up knowledge to break down Poverty

31 Quinn Street, Newtown
Johannesburg
South Africa
2000
Phone: + 27 11 833 0161
Fax: + 27 11 832 3085

Twitter: spii1
Facebook: SPII
Email: advocacy@spii.org.za
www.spii.org.za