B O O K   R E V I E W

Microfinance under Neoliberalism

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Bateman, Milford (2010), *Why Doesn't Microfinance Work?: The Destructive Rise of Local Neoliberalism*, Zed Books, London, pp. x+262.

Karim, Lamia (2011), *Micro-Finance and Its Discontents: Women in Debt in Bangladesh*, University of Minnesota Press, Minneapolis, pp. xxxiii+255.

Microfinance has been celebrated globally as a means of poverty alleviation and of socio-economic empowerment of poor women. Here are two recent books that strongly deny the validity of both these claims.

In the book titled *Why Doesn't Microfinance Work?,* Milford Bateman argues against the first claim: that microfinance can eradicate poverty and send "poverty to the museum," as famously claimed by the founder of Grameen Bank, Muhammad Yunus. Bateman presents a review of the existing literature to substantiate his argument that microfinance is a "poverty trap", and that it does not contribute to systematic and sustainable development at the local level.

In the book titled *Micro-Finance and Its Discontents,* Lamia Karim evaluates and criticises the second claim of microfinance, that it empowers poor women. Her critique is based on ethnographic evidence collected between 1998 and 1999, and again between 2004 and 2007, from women and men in Pirupur Thana (name fictitious) village in Bangladesh. She also undertook a survey of 158 women borrowers from Pirupur Thana in 2007. She presents the narratives of eight women borrowers in this book (the narratives are different from the survey). She supports her narratives with information on four major non-governmental organisations (NGOs) working in the field of microfinance in Bangladesh – namely, Grameen Bank, Building Resources Across Communities (BRAC), Proshika, and Association for Social Advancement (ASA). Karim's book argues that by using what she calls the "economy of shame," microfinance NGOs have in fact created a new form of domination over poor women.

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[1] The views expressed in this note are entirely of the author and not of the organisation to which she belongs.

Microfinance and Neoliberal Policy

Both Bateman and Karim describe microfinance as an instrument of "neo-liberal" economic decision-making, with corresponding advance effects on the poor.

First, microfinance is channelled through NGOs, a process that has further debilitated the already weak foundations of the welfare state in developing countries. In Bangladesh, for instance, NGOs have taken over most of the functions that a welfare state is expected to perform, from rural credit to primary education and basic health care. The proliferation of NGOs in Bangladesh has been so striking that Karim describes them as a "shadow state" (p. 200). The institutions instrumental in the creation of such a large NGO network in developing countries have been the World Bank and the governments of various advanced countries. Interestingly, these advanced countries themselves have had a long history of state intervention, which has in fact been the key to their economic success. However, they have now "kicked the ladder," to use a phrase of Ha-Joon Chang, and have become supporters of privatisation and liberalisation. Microfinance is one instrument through which these countries have flooded the developing countries with donor funds and thwarted systematic public action.

Secondly, microfinance has served as an entry point for multinational firms into the rural areas of developing countries. Muhammad Yunus, in his Nobel Prize speech, had appealed to global corporations to regard the poor as an "unrealised market". In response, NGOs in Bangladesh have entered into areas such as the provision of packaged foods, cell phones, and a variety of other commodities to the poor. The illustrations provided by Karim about Grameen and the telecommunications multinational Telenor, and Grameen and Danone Foods (a Danish dairy multinational), indicate how NGOs have entered previously inaccessible markets in rural Bangladesh. She expresses surprise about how parents who cannot afford to give rice to their children are expected to buy *Shakti Doi,* a yogurt product manufactured by Danone, for these children.

Karim also discusses the joint venture of Grameen and the French water services multinational Veolia, which is expected to provide arsenic-free water to Bangladeshi villages at a nominal price. This example shows how privatisation has attached a price tag to basic goods and services, which should ideally be publicly made available at zero cost to the poor. The global corporations that have entered rural Bangladesh through the means of microfinance have played an important role in accelerating this process of privatisation.

Thirdly, the principle of profit maximisation is the driving force of microfinance. The most striking instance of this association between microfinance and market principles is the interest rate policy of microfinance institutions (MFIs). MFIs have justified their policy of ultra-high interest rates, going up to as much as 100 per cent per annum, on various grounds. First, they argue that the poor are concerned only about the *availability* of credit and not the *cost* of credit. Secondly, as argued by the

Consultative Group to Assist the Poor (CGAP), a body created by the World Bank to promote microfinance in developing countries, the revenues from high interest rates are ultimately used for the benefit of the poor.

Bateman shows that, there is plenty of evidence to suggest that such claims do not hold true. It is a basic and established fact that high interest rates hurt the poor, as particularly when compared to subsidised interest rate systems. The World Bank's own "Moving Out of Poverty" study suggests that the poor want lower rates of interest, longer periods of repayment, and larger loan amounts. There is also evidence to suggest a high interest rate elasticity of demand for microfinance, indicating that interest rates *do* matter for the poor. A further point, rightly noted by Bateman but wrongly attributed to data from India's National Sample Survey Organisation (NSSO), is that a micro-enterprise can hardly generate any profit after paying interest that ranges around 24–36 per cent per annum.[2]

According to Bateman, MFIs sacrifice the interests of their poor clients in order to favour their shareholders and investors. He illustrates this with several examples. First, high interest rates are essential for MFIs to attain self-sustainability, as can be seen from the example of Compartamos in Mexico, the first MFI to go in for an Initial Public Offering (IPO). Secondly, high interest rates help shareholders and investors by making MFI stocks attractive, as in the case of SKS Microfinance, the first Indian MFI to go public (see Ramakumar 2010). High interest rates help to maintain high credit ratings, which are essential for higher valuation of the stocks of MFIs. Moreover, once the stock of an MFI fares well, as it did in the case of Compartamos, there will always be pressure on the MFI to further raise its interest rates rather than to lower them.

Karim quotes David Harvey to argue that neoliberalism redistributes wealth from the poor to the rich, and that credit has been an instrument of this redistribution. The interest rate policy of MFIs helps in such redistribution.

Bateman notes that MFIs have been so biased towards high interest rates that Compartamos, for instance, as a matter of policy, has not attempted measures such as accessing cheaper funds by raising member's savings. Such cheaper sources of funds could have lowered interest rates, but that would have meant directing the benefits of the high profits towards the clients rather than towards the shareholders, which is precisely what Compartamos did not want.

Even Grameen Bank – the pioneer in the field of microfinance – cannot be exonerated of a bias towards high interest rates. Bateman distinguishes between Grameen II, a model introduced in 2001, and the original Grameen Bank. He regards Grameen

[2] This point was discussed in Chavan and Ramakumar (2005). The wrong attribution to NSSO by Bateman appears to be carried over from an article titled "Death by Micro-Credit," published in the *Times of India*, September 16, 2006.

II as a more commercialised form of microfinance, one bearing all the attributes of neoliberal policy. Under Grameen II, the advertised annual interest rate on microfinance is 20 per cent. There has also been a tacit attempt by Grameen Bank to use various means, to further raise this advertised rate in order to bring it closer to the market-determined rate of interest.

Biased and Imperfect Impact Assessments of Microfinance

Both Bateman and Karim are critical of the fact that most of the available research on the socio-economic impact of microfinance is supported and funded by the MFIs themselves, or by their donor institutions. Hence, such research provides a biased view of the impact of microfinance on both poverty and women's empowerment. As Karim notes, such "development knowledge is not innocent." It is largely driven by short-term considerations, such as obtaining more funds for an existing project or starting a new project. Karim observes that MFIs and their donors have created a "social archive" of the poor and their lives. This archive provides large amounts of raw data that can easily be moulded to draw inferences that suit the interests of the microfinance sector. Such is the power of this kind of evaluative research led by NGOs that it can silence opposing viewpoints. Karim provides a telling instance of how the anthropologist Aminur Rahman did not get adequate support for publishing critical findings about Grameen Bank from the Canadian institution funding his research, as well as from different publishing houses in Bangladesh.

Besides being biased, assessments of the microfinance sector are also imperfect because of conceptual flaws in their research design and statistical methodology. Hence they are inadequate for drawing any definite conclusions about how microfinance affects the socio and economic lives of the poor.

Bateman argues that "displacement effects" and "client failure" are two key conceptual factors ignored by most such poverty impact assessment studies. The term "displacement effects" refers to the loss of employment and income in existing micro-enterprises as a result of the entry of client micro-enterprises. This loss is particularly striking in the case of products or services for which the demand is price-inelastic, which is often the case with micro-enterprises. As a result, displacement effects are widely prevalent at the local level in most developing countries. As most impact assessment studies do not capture such displacement effects, they tend to overestimate the positive impact on poverty resulting from the entry of client micro-enterprises.

Client failure refers to the failure of micro-enterprises, which pushes micro-entrepreneurs into deeper poverty. Such failures are very common among micro-enterprises, particularly when the poor are forced into entrepreneurial ventures due to poverty and destitution rather than for profit. Lack of skill development and training can also result more failures than successes among micro-enterprises. Since most impact studies do not take such failures into account, they present an inaccurate picture of the impact of microfinance on poverty.

Bateman reviews various studies, from the pioneering study by Mark Pitt and Shahid Khandker onwards, to emphasise the relatively weak evidence regarding the positive impact of microfinance on poverty alleviation. This point is corroborated in a recent report published by the University of London (Duvendack *et al.* 2011a), whose authors undertook an extensive survey of 2,643 impact assessment studies of microfinance. Duvendack *et al.* classified these studies in descending order, based on the validity of their research design. Next, they cross-classified the studies into three categories based on statistical method. They then applied a heuristic scoring of research design and analytical methods. They fixed a minimum cut-off score and excluded studies with a score below this level, to ensure a minimum quality of research design and statistical method. This exercise reduced the sample of studies to just 58. A detailed examination of these 58 studies did not reveal any robust evidence of microfinance being either pro-poor or pro-women.

Duvendack *et al.* (2011b) note that authors "draw policy conclusions generally supportive of microfinance" despite the "weak methodology and inadequate data" of their studies (p. 2). It is evident, therefore, that we exercise caution before accepting the many tall claims made about the benefits of microfinance, including Muhammad Yunus's famous claim that five per cent of Grameen borrowers escape poverty every year.

Microfinance Exacerbates Poverty

Bateman asserts that in developing countries – including Mexico, Bosnia, India (with specific reference to the State of Andhra Pradesh), and Bangladesh – which are "saturated" with microfinance, microfinance has had hardly any impact on poverty alleviation. Far from being able to make a dent on poverty levels, microfinance in fact has the potential to exacerbate it. Bateman's argument of microfinance being a poverty trap is based on: (a) its inability to provide economies of scale to micro-enterprises; (b) its promotion of an informal agricultural and micro-enterprise sector; (c) its ability to "infantilise" a developing economy by deindustrialising it of its medium enterprises, which are the key to sustainable development.

Bateman's book makes important arguments about the dangers of treating microfinance as the only mechanism for economic development. However, in the absence of any original research of his own to support these arguments, he may not fully succeed in convincing the readers about their validity. The book presents these arguments, particularly the argument of deindustrialisation, in somewhat superficial manner. In his ambitious attempt to cover all developing countries, Bateman fails to offer a deeper and more analytical insight into the working of the industrial sector in any of these countries.

Microfinance Disempowers Poor Women

Through the narratives she presents in her book, Karim seeks to assert that microfinance has disempowered poor women by thrusting a new form of governance over them. While the credit is received by women, it is almost always used by men – hence it is doubtful if the loan in itself empowers women or gives them more security within the household. Further, though women may not always be the ones to take the decision on how to use the loans, when it comes to repayment, it is they who are held responsible by the MFIs. This adds to the social and economic burden of poor women.

When a member of a loan group defaults, the MFIs and other members of the group often break defaulter's house or confiscate her belonging in order to recover the loan. Although, on paper, MFIs do not advocate mutual guarantees for loans, in practice, group members come under pressure from MFIs to extract payments from defaulting members – or else they may have to pay up on behalf of the defaulters. Income-poor women are thus pitted against each other in the actual practice of loan recovery. In the process, the MFIs effectively use a woman's sense of shame and her social vulnerability as their collateral.

As MFIs have grown, so has their drive to push greater amounts of microfinance into developing countries. Their primary preoccupation has become lending and extracting repayment by any means, rather than ensuring that loans are used in such a manner that women are empowered. This has also led to income-poor women becoming members of more than one MFI, further increasing the pressure on them of repayment.

Microfinance Informalises Rural Financial Markets

Contrary to the popular belief that microfinance curbs informal sources of credit, Karim notes that the women borrowers themselves become moneylenders by on-lending money borrowed from MFIs. She has only one narrative of such a female moneylender in her book, however, which makes it difficult to conclude how widespread this phenomenon is in Bangladesh. Karim asserts that moneylending is common among women in Bangladesh even though none of the women admitted to the practice during her survey of 158 women borrowers; she ascribes their disavowal to the fact that usury is prohibited in the Quran. Karim claims that she is not blinded by the "scientific" data collected through the survey, for, as an ethnographer, she could sense the existence of moneylending among these women.

The narrative of the sole female moneylender in Karim's book is indeed very insightful. It brings out the complicity of MFIs (Grameen Bank, in this instance) in the forcible recovery of loans by moneylenders. It is also interesting to note that Grameen Bank does not seem to object to the woman moneylender diverting her funds to lend to other women, or to her taking proxy loans in the names of other women. In fact the Bank's agents are keen on lending to this woman as she is deemed creditworthy. It must be stated, however, that Karim's assertion about the widespread presence of moneylending would be more convincing if this narrative had been supported by data from the survey.

Grameen Bank Model of Microfinance

Both books under review recognise the status of Grameen Bank as a pioneering institution in the field of microfinance, and discuss at length its role in shaping the microfinance sector in developing countries. While Karim is critical of Yunus and his neoliberal vision of microfinance, Bateman presents Yunus as someone who has been marginalised in the world of commercialised microfinance and who has been forced to adopt the new form of microfinance under Grameen II.

Bateman's portrayal of Yunus as a victim of commercialised microfinance is surprising, especially since Yunus himself has always championed the free market economy (Yunus 2006). He has argued that an economic system has to be competitive and profit-maximising; this, according to him, is the central thesis of capitalism (Ramakumar 2000). He distinguishes *his* form of capitalism, of course, using terms like "social-conscience driven capitalism," but it is hard to see how this is different from capitalism the way we know it (*ibid.*). After the controversy broke out about Compartamos in Mexico and SKS Microfinance in India, Yunus has been increasingly critical of these two institutions. He has distanced himself and his model of microfinance from the kind of microfinance practised by them. He has faulted them for charging high rates of interest (exceeding 20 per cent) and tapping the capital market to raise funds.

As has been discussed earlier in this review, Grameen Bank too can be accused of charging high rates of interest. As regards raising funds, Yunus has proudly stated that Grameen Bank has never had to resort to the capital market, and that it never faced any dearth of funds because it relied on mobilising savings from the poor.[3] This is only half the truth, however, for Grameen Bank has always relied heavily on donor funds. In fact, as noted by Bateman, Grameen Bank has remained financially viable because of donor funds, as its repayment rate was below the advertised rate. It is only under Grameen II that the institution has started to pay more attention to mobilising savings. Once an MFI expands its scale of operations and there are limits on its capacity to mobilise deposits, as was the case with SKS Microfinance, it can no longer rely solely on donor funds.[4] It has to tap the capital market and seek innovative ways of raising funds by securitising its assets. Yunus's defence of the Grameen model and his critique of the SKS Microfinance model, therefore, are not

[3] See interview with Mohammad Yunus, "Dr. Yunus on Interest Rates and Microfinance," at www.youtube.com.
[4] SKS Microfinance is a non-deposit-taking Non-Banking Financial Company (NBFC) in India. The Reserve Bank, as matter of policy, discouraged NBFCs from seeking public funds in the form of deposits, due to concerns about the safety of the deposits and financial stability.

convincing. Consequently, Bateman's defence of Yunus and his idea of microfinance is also not convincing.

Alternatives to the Grameen Model of Microfinance

Both Karim and Bateman provide their own alternatives to microfinance – more specifically, to Grameen-type microfinance. Karim restricts her discussion to the creation of a citizen's movement that questions privatisation and raises other public issues. Bateman provides specific examples from various developed and developing countries of how development finance can be more effectively channelled at the local level. His focus is on public banks in South Korea, China, and Japan that lend to micro, small, and medium enterprises. He deems these institutions successful, given the way they have transformed the industrial sector in their respective countries.

The Indian Alternative

In his discussion of India, Bateman poses Kudumbasree, a model of microfinance in the southern State of Kerala, as an alternative to Bangladesh's Grameen Bank. He notes that many of the faults in the Grameen model have been overcome in the Kudumbasree model.

The Kudumbasree scheme includes the following features: (a) local-level planning to ensure that micro-enterprises have access to the market and avoid overinvestment in any one activity; (b) it enabled economies of scale in self-help groups (SHGs) that undertook production through micro-enterprises; and (c) subsidised rates of interest on credit were offered by cooperatives/banks, with the State government providing the subsidy – an important factor, and one that Bateman fails mention. Bateman is correct in concluding that there is indeed a lot that can be learnt from the Kudumbasree model, by the existing Grameen-type models of microfinance.

Bateman's discussion of India is limited, however, to the success of Kudumbasree in Kerala, on the one hand, and the failure of microfinance in Andhra Pradesh, on the other hand. There is a third, important segment of microfinance in India, which he does not consider. This is the segment that has been created by India's public banks. Since 1992, microfinance in India has been implemented by the Self-Help Group–Bank Linkage Programme of the National Bank for Agriculture and Rural Development (NABARD). Under this programme, cooperatives and banks lend to SHGs directly (either by forming and nurturing SHGs themselves, or by taking the help of NGOs to do so). As the Reserve Bank of India (RBI) considered lending to SHGs an effective means of directing credit to poor women, it included such loans under the priority-sector credit of banks.

The crisis that unfolded in the microfinance sector of Andhra Pradesh was on account of non-banking financial companies (NBFCs) functioning as MFIs. Several major

NBFCs, including SKS Microfinance, Spandana Sphoorty Financial Limited, Share Microfin Limited, and Asmitha Microfin Limited, have been very active in the State. Women borrowers in Andhra Pradesh have reported harassment from the recovery agents of these MFIs (Ramakumar 2010). Further, these MFIs have been accused of charging very high annual rates of interest, ranging between 24 per cent and 50 per cent (*ibid.*).

Although banks in India have been active in reaching microfinance directly to SHGs, in recent years, they have also been very keen on lending to NBFCs for on-lending to the poor. This way of directing microfinance has been an easier for the banks than forming and nurturing SHGs, and catering to their individual credit needs. Moreover, once loans to MFIs–NBFCs were included as a part of priority-sector credit, such lending by banks became legitimised. Consequently, the growth in bank lending to MFIs has been much higher, in recent years, than the growth in direct bank lending to SHGs. However, the quantum of microfinance given by banks directly to SHGs continues to be greater than the quantum of microfinance given by them to NBFCs.

After the crisis of microfinance in Andhra Pradesh, questions have been asked about whether NBFCs, which have been no different than usurious moneylenders, should be allowed to get funding from public banks. Concern has also been raised about the need to set up a regulatory body for the microfinance sector in India. The conditions for giving credit to MFIs–NBFCs by banks have now been made more stringent (RBI 2011a). Banks have been directed by the RBI to form SHGs and lend to them directly, rather than routing the funds through NBFCs (RBI 2011b).

Thus, the microfinance sector in India has the Kudumbasree model, which definitely needs to be encouraged, at one end of the spectrum; and, at the other end of the spectrum, it has the NBFC model, which needs to be regulated stringently and discouraged over time. Between these two lies the Self-Help Group–Bank Linkage model, which needs to be strengthened on the lines of Kudumbasree, particularly with respect to of local-level planning and lowered rates of interest.

Conclusion

To conclude, the authors of the two books, offer valuable insights into the working of the microfinance sector in developing countries within the larger context of the policy framework of neoliberalism. In a world where sweeping and unfounded claims are made about microfinance, these books offer a fresh perspective about what can go wrong, and has gone wrong, if microfinance, particularly for profit microfinance is made the only plank for development. However, it cannot escape mention that while Bateman and Karim are rightly critical of the methodological issues in the existing literature, it is not always clear whether their own studies meet the standards that they set for others.

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