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The Limits of Microcredit—A Bangladesh Case

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Since its emergence in the 1970s, microcredit has grown in popularity as a tool for development. Today, microcredit organizations have assets well in excess of $22 billion USD and serve more than 113 million clients.[1] Microcredit has enormous potential as a tool for poverty alleviation. Yet as this strategy moves into the development mainstream there is an urgent need to reflect on its role in market-led development initiatives and its limitations, as well as its historic successes. There is significant risk in microcredit's often uncritical adoption. This risk is compounded by the systematic failure of many microfinance institutions (MFIs) to engage the communities where they work in the process of designing and evaluating microcredit programs. As with many development programs, the voices of communities and individuals who are the supposed beneficiaries of microlending are conspicuously absent from the projects that seek to determine their futures. As debates over the pros and cons of microcredit rage and donor support encourages rapid adoption, it is crucial to evaluate the impact of microcredit from the perspective of those who have the most to gain and lose — the recipients.

This Backgrounder outlines the results of a study on the impact of microcredit on recipient livelihoods in rural Bangladesh. It is a story that highlights the dangers of viewing microcredit as a "silver-bullet" for development and the limits of employing purely market-led development approaches as strategies for poverty alleviation. Microcredit claims to improve the lives of recipients by providing them with small

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loans to purchase productive assets for entrepreneurial activity. Advocates of microcredit argue that this helps recipients break cycles of poverty, reduce dependency on "charity" and other forms of aid, and empowers women as economic decision makers within the homes by targeting women as loan recipients. While microcredit has helped accomplish these goals in particular situations and contexts, it also relies on economic integration as the *primary* mechanism for development and assumes that all poverty is a function of the inability to enter into market relations.

While lack of credit is a critical issue in impoverished rural regions throughout the world, it is only one structural aspect of poverty. Food insecurity, lack of access to health and education, and gender inequality (not just in economic but also in *social and cultural* contexts) are realities for those living in rural poverty that microcredit may not be suited, in-and-of-itself, to address. Indeed, donor and practitioner enthusiasm for such market-based development strategies, at the expense of addressing these other critical issues, threatens to make conditions of poverty worse.

In Bangladesh, the "birth-place" of microcredit,[2] microcredit is seen as a key strategy in overcoming many of the hurdles of rural life, including low per-capita land holdings, underemployment, poverty, and gross wage disparity.[3] As microcredit has grown in popularity with funders, it has become relatively easier to fund microcredit projects in Bangladesh than other kinds of programming. Not only are many new NGOs forming specifically to deliver microcredit, but other organizations are increasingly shifting their funding away from social safety net programs and towards microfinance. This has led to a marked reduction in the diversity of services available in rural areas.

What follows is an exploration of what happens to recipients in an oversaturated microcredit market; a market in which microcredit has become the, as opposed to a, mechanism for poverty alleviation. In rural Bangladesh, microcredit is not achieving its core goals of poverty alleviation, financial independence, and gender equality. While this is very much a story about Bangladesh, we stress that with the increasing global popularity of microcredit, it is also a cautionary tale for donors and practitioners alike. This research was conducted cooperatively with a group of landless laborers living in Arampur, a village in Northern Bangladesh. Using digital voice recorders, they conducted unstructured interviews with their peers and neighbors, gathering life histories and experiences with microcredit. What follows is based directly on villagers' words, concerns, experiences, and ideas.

Poverty Alleviation, Metrics, and Relationships Between MFIs And Borrowers

Proponents of microcredit frequently argue that high repayment rates — many report rates as high as 98% — indicate the success of microcredit on the ground.[4] Grameen Bank founder Muhammad Yunus, for example, has strongly argued that such high repayment rates indicate that recipients are both using their loans productively and learning financial discipline by adhering to repayment schedules to remain eligible for additional loans.[5] This argument has been largely accepted within the microcredit community and repayment rates are the standard metrics for success used by practitioners and donors alike.

Our experience in Arumpur leads us to question the use of repayment rates as a proxy for measuring poverty alleviation. The vulnerable positions of people living in poverty often makes it easier to coerce, pressure, and extort them into repaying, often at the expense of their livelihoods. Where repayment rates are the primary metric by which MFIs are judged, they become a way to track job-performance of their field officers. As residents of Arampur reported in countless stories, this leads to an inherently exploitative relationship. Residents reported that it was not uncommon for field officers — who are in charge of granting and collecting weekly payments or "installments" — to resort to violence in collecting on loans. Physical and sexual abuse were common. Unauthorized repossession of assets, including the very roofs off of recipients' houses, was not infrequent.

Borrowers have little recourse in such events. They are forced to choose between protecting themselves, their homes, and their families and purchasing basic needs. As one recipient put it, *"They use many kinds of force to get their money back… torturing people or dragging people… it is a serious injustice. Say I tell the field officer 'I can't give you the installment today, my child is sick.' And then I bring the doctor to my house and he is sitting and giving my child medicine. Then the field officer comes and says 'why can you buy medicine for your child, but you can't give me the installment?' What kind of a way is this to treat anyone?"* Microcredit loan payments thus become a high priority among other household expenditures, including food and medicine. Rather than empowering individuals and communities, repayment creates an environment of fear and intimidation where recipients must regularly sacrifice basic needs to meet an inflexible repayment schedule.

The Link Between Microcredit, Consumption, and Dependancy

Microcredit promises to help recipients achieve economic self-sufficiency and break cycles of poverty by providing cash infusions necessary to purchase productive assets. These assets, whether crops or durable

goods, provide the basis for entrepreneurial ventures that can help recipients begin to earn more income. However, in Arampur, respondents described a different scenario, in which microcredit produces dependency on additional loans, trapping them in deepening cycles of debt. In the words of one respondent, *"NGO workers come to our house and try to make us understand the benefit of taking microcredit. After getting the loan, if we fail to repay the installments on time they put pressure on us. So, we are bound to get another loan to repay the previous loan."*

With eight microloan providers in a village of approximately 1500 households, it is fairly common for households to have upwards of four loans at any given time. In this overcrowded debt-market, it is common to cover old debts by taking out new loans from different sources (and not infrequently from the same sources), often with the encouragement of field officers. These recipients frequently find themselves in positions of greater dependency and reduced self-sufficiency.

The notion that microcredit is a mechanism for breaking cycles of poverty and achieving financial independence is one that is questioned by recipients in Arampur. Rather than freeing them from the burdens of poverty and enabling them to move away from reliance on local moneylenders for emergency cash, many view microcredit itself as producing insidious cycles of dependency. One respondent observed, *"At the beginning, the NGOs said that their loans would bring happiness to our lives, as we would get money to start businesses. They lured us by telling us we would have chickens, a latrine, and many other things. We believed them. They said that we would have to repay the installments every week but we would never feel burdened by the loan. But later we felt the burden. Then we understood that we could never get rid of the loans even after selling our skin."*

Such crises of dependency are deepened by the need to use loans for consumption. In Arampur, microcredit has replaced other NGO-provided rural services and, as many told us, eroded long-standing social safety mechanisms within the village. Many reported that during the hungry season, they had no choice but to use loans for the purchase of food. *"I don't want to take microcredit loans any more,"* one respondent observed, *"but at times of serious food problems we have no other way."* Many in the village told us that they had avoided taking microcredit for a time, but ultimately were forced to take loans during a household crisis (the most common were hunger or medical emergencies). This initiated a cycle of debt from which many have been unable to escape.

Microcredit and Gender Relations

A central claim and goal of many MFIs is to empower women and promote gender equality by elevating women's status in household decision making. However, while women were certainly the primary targets of MFI programs, women were more often conduits to, rather than end users of, credit. As one respondent told us, *"Women take microcredit as their husbands order them to do so. When their husbands fail to pay the installment, then NGO workers abuse the women a lot. Women have to bear the pressure coming from both sides."* In Arampur, it is often the case that women bear the risk of loans, but do not directly benefit from its rewards.

One of the early goals of microcredit programs in Bangladesh was to free women and families from the burden of a dowry. Yet respondents in Arumpur report that microcredit is actually strengthening the dowry system by precipitously inflating dowry prices. Numerous respondents used their loans to pay for their daughter's dowries, often requiring multiple loans to cover the costs. One woman who earns 100tk (approximately $1.50) per day took a loan for 25,000tk (over $360) to pay for her daughter's marriage. Another woman who took a loan to pay for her daughter's dowry was forced to give up her home when she had no way to repay the loan after the loan money had been given for dowry.

Moving From Sustainable Institutions to Sustainable Communities

While we share the belief that access to credit is a human rights issue, we also suggest that its delivery has

become a human rights concern. If microcredit is to play a constructive role in breaking cycles of poverty in rural areas, it must be rethought with and from the perspective of recipients and communities.

In contemporary microcredit, "sustainability" has come to refer to the financial viability of MFIs. We argue that this term should be re-appropriated in the name of recipients and the communities in which they live. If microcredit is to contribute to poverty alleviation, donors and practitioners must:

- Reevaluate metrics for success
- Ensure that other critical services (such as health care, food security programs, and schools) are in place in communities where MFIs operate
- Engage in sustained dialogues and build partnerships with communities to better address the needs of recipients.

These are critical first steps in moving beyond the assumption that market integration reduces poverty and increases social equality. Microcredit programs will not achieve their stated goals of eliminating the crushing burden of poverty and providing social equality only when they move beyond repayment percentages as the sole measure of success.

Notes

1 Real numbers are likely to be higher. See MICROCAPITAL STORY: What Are the Total Global Assets in Microfinance?" 2007. *Microcapital: The Candid Voice for Microfinance Investment.* Available at http://www.microcapital.org/microcapital-story-what-are-the-total-global-assets-inmicrofinance-leading-sources-weigh-in-mix-microcredit-summit-microbanking-bulletin-mbb-acci-onmicrofinance-gateway-blueorchard-uncdf/

2 The Grameen Bank was founded in the mid-1970s to provide microcredit loans. While it may be disputable whether this organization was the first microcredit provider, they have certainly, over the past thirty years, become the most famous, resulting in the joint awarding of the Nobel Peace Prize to the Bank and its founder, Mohammad Yunus, in 2006.

3 For an excellent overview of the context of microcredit in Bangladesh see Qazi Kholoquzzaman Ahmad (2007), Socio-Economic and Indebtedness-Related Impact of Micro-Credit in Bangladesh. 2007. Dhaka: University Press Limited.

4 Though our data suggests that such numbers, at least in Arampur, might be somewhat exaggerated.

5 Muhammad Yunus (2003), *Banker to the Poor: Micro-Lending and the Battle Against World Poverty.* New York: Public Affairs; Muhammad Yunus (2007), *Creating a World Without Poverty: Social Business and the Future of Capitalism.* New York: Public Affairs. For a more developed articulation of this argument, see the somewhat menacingly titled Asif Dowla and Dipal Barua (2006), *The Poor Always Pay Back: The Grameen II Story.* Bloomfield: Kumarian Press.

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