



The crisis of Asian Microfinance: implications for Latin America

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Five difficult years for Asian microfinance: a rough five years



- 2006 Nobel Peace Prize to Muhammad Yunus and Grameen Bank *"for their efforts to create economic and social development from below..."**
(click graphics at right to view prize profiles)
- Almost from day prize awarded, Microfinance & Grameen have run into difficulties...
- Yunus forced to leave Grameen Bank after a Norwegian documentary accuses him of mishandling grant funds (see NY Times 2011 [Microlenders honored, now struggling](#))



* The Nobel Peace Prize 2006". Nobelprize.org. 14 Jun 2012
http://www.nobelprize.org/nobel_prizes/peace/laureates/2006

Latin America microfinance, too successful & profitable raises doubts: Compartamos for who?

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- [Ricardo Hausmann reviews Yunus' Building Social Business: a new kind of capitalism, defends the LatAm model](#)
- Says Accion precedes Mohammad Yunus' Grameen Bank, [started in on 1960s Brazil and Latin America.](#)
- Compartamos IPO and MiBanco ADOPEM "Mission drift" too profitable? See PBS Now [documentary report by Maria Hinojosa](#), who is profiting from microcredit?



Bad news from Andhra Pradesh



Residents of Madoor village in Andhra Pradesh, India. Leaders in the state have accused microloan lenders of impoverishing customers.

By [VIKAS BAJAJ](#) Published: January 5, 2011

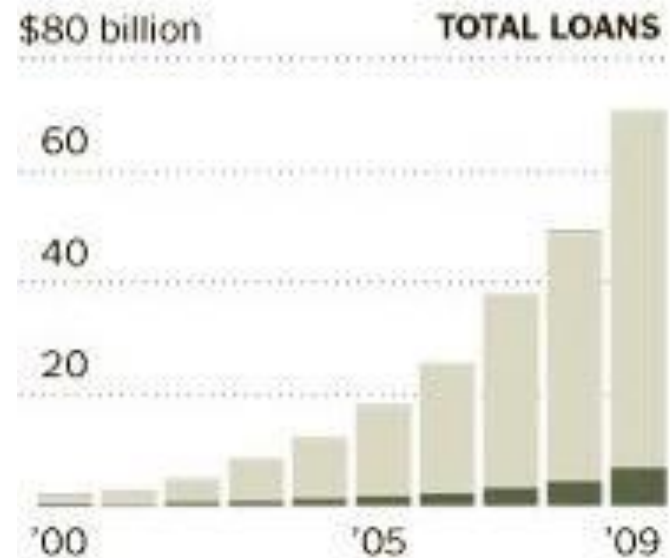
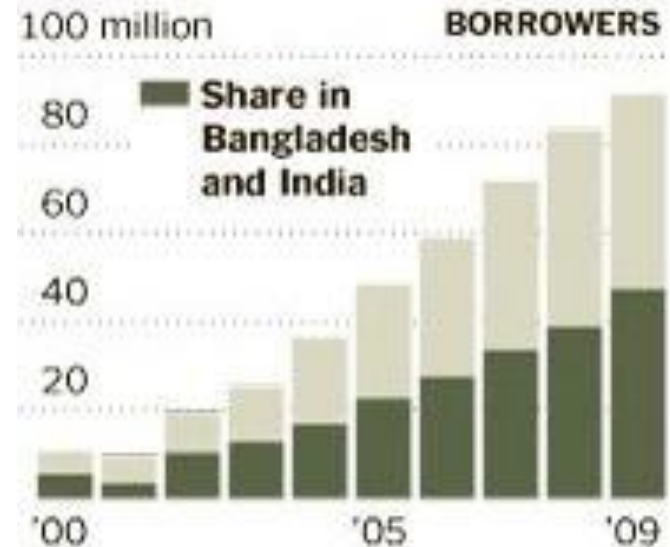


VIKAS BAJAJ

chronicles crisis in NY Times

Lending to the World's Poor

Government officials in India and Bangladesh have said microcredit lenders exploit the poor. The two countries account for more than half of the world's microcredit borrowers, although they account for a far smaller share of the total money lent.



Source: Microfinance
Information Exchange

Three crises of Microfinance: Asia

1. High interest rates and multiple loans/lenders + group lending leads to suicides and public backlash in Andhra Pradesh ... Mohammed Yunus calls for 25% interest cap

2. Experimental RTS evidence MIT-JPAL finds no impact of Microfinance on poverty Roodman & Morduch, 2010 question key World Bank Bangladesh studies....

3. Transparency credibility of Kiva & Whole Planet questioned: D. Roodman accuse NGOs Kiva and Whole Planet of not really matching customers and donors as suggested by web page, NY Times described the controversy.

Microfinance in Asia and LatAm differ both have long traditions, deep roots

Asian Microfinance

- More borrowers, rural areas
- Smaller loans, faster repayment
- Group lending, target women
- Build into NGOs that provide safety
- Hidden subsidies documented by Morduch (1998)
- Public/private transcripts differ (see Ananda Roy, 2010)

Latin Microfinance

- High interest rate informal sector targeted
- Less focus on rural, more urban informal sector
- Larger loans, fewer borrowers.... 10M loans averaging \$1100 for a total of \$12B in 2011
- Accion first MFI in world?
[Ricardo Hausmann says yes...](#)

Mission drift: What is Microfinance?

Taken largely from [Karlan and Goldberg \(2011\) chapter 1](#) of Microfinance Handbook, a survey of MFI evaluations

- (1) Small transactions and minimum balances: loans, savings, or insurance.
- (2) Loans for entrepreneurial activity (a billion entrepreneurs? See B&D, 2011, *Poor Economics...*)
- (3) Collateral-free loans (informal sector, not assets)
- (4) Group lending (Grameen I not II)
- (5) Focus on poor and poorest clients .
- (6) Target female clients.
- (7) Simple application processes.
- (8) Services target underserved communities.
- (9) Market-level interest rates???

South Asia: 39 million borrowers average loan \$161 for a total of \$6.5 billion

Total MFIs in South Asia, across all possible dates: 474

Gross Loan Portfolio \$USD 2011:	\$6.5 billion
Number of active borrowers in 2011:	39.4 million
Average loan balance per borrower 2011:	\$161
Deposits 2011:	\$1.2 billion
Assets 2011:	\$6.8 billion
Number of depositors 2011:	14 million

Source: <http://www.mixmarket.org/mfi/region/South%20Asia#ixzz2CJNGrjBY>

South Asia dominated by India and Bangladesh

Table 1: South Asia: 10 million loans averaging about \$145 in South Asia in 2011 for a total of \$1.4 billion in loans (Mixmarket).

Country	# MFIs	Active Borrowers*	Total Loans* (thousands)	Average Loan
Afghanistan	1	11	3,359	298
Bangladesh	3	5,840	730,333	125
India	15	3,542	592,066	167
Nepal	9	350	79,121	226
Pakistan	2	245	38,342	157
Sri Lanka	1	39	6,270	159
Total Average	31	10,027	1,449,492	145

Source: MIX Market Regional Profile <http://www.mixmarket.org/mfi/region/South%20Asia#ixzz1xjrnZDVe>

Table 2: Mix Market Data Reports 10.4 million loans averaging \$1150 in Latin American in 2011 (total of \$12 billion)

Country	# MFIs	Active Borrowers*	Total Loans* *thousands	Average Loan
Argentina	2	1.1	1,892	1,714
Bolivia	7	351	839,830	2,392
Brazil	4	1,838	1,655,205	900
Chile	2	230	1,624,709	7,058
Colombia	16	2,214	4,979,697	2,250
Costa Rica	1	3.5	4,074	1,178
Dominican Republic	4	278	286,431	1,031
Ecuador	6	243	415,866	1,712
El Salvador	5	91	320,273	3,532
Guatemala	6	254	144,285	568
Haiti	2	22	36,921	1,706
Honduras	9	114	158,955	1,389
Mexico	41	6,020	1,864,996	310
Nicaragua	10	227	224,389	987
Paraguay	5	498	985,149	1,977
Peru	50	3,607	8,734,089	2,421
Uruguay	1	2	7,324	3,466
Venezuela	1	45	120,928	2,699
totals/average	108	10,400	11,936,876	1,148

Source: MIX Market Regional click on the country name to get more information
Profile <http://www.mixmarket.org/mfi/region/South%20Asia#ixzz1xjrnZDVe>

Latin American Microfinance growing pains and new developments...

1. Mission drift: *Compartamos in Mexico and ADOPEM in DR become very successful and profitable banks, but charge high interest rates 70% plus*

2. Competition from large banks– new mobile banking regulations favor established banks: *but may not benefit rural poor... key technology upgrade challenge for MFIs.*

3. Challenges of mobile banking and transfers: *Africa far ahead in this area M-PESA: new regulations remittances*

4. New technologies and financial regulations in U.S. *impact remittances: Dodd-Frank has new regulations for remittance transfers– some “alternative financial services” (AFS) firms will exit market*

Asian vs. Latin and African: Microfinance Models converging on financial access, savings

1. *Asian becomes Latin... Grameen II relies less group lending, individual savings lending, small loans perhaps at high rates:* Compartamos in Mexico and SKS India, have similar image and (See Ananda Roy, on Grameen Private vs. public transcript.
2. **Still Asian model is subsidized and** embedded in broader safety net in BGD: in U.S. too, welfare payments out of reach of creditors...
3. **Learning from Africa: microfinance now driven by mobile remittance transfer technologies: Hybrid** models combine micro-saving and financial access via MPSA for example: Rutherford's [SafeSave](#) ; and [P9](#) experiments....
4. New experiments in Mexico combine Microfinance, remittances and mobile banking, financial diaries project with Oportunidades recipients... see also

Ananya Roy's Bangladesh Consensus*

1. **Access to credit is a human right** (with or w/o interest rate cap?)
safe savings vs. borrowing
2. **Microfinance key component of a broader social safety net...**
examples ASA, BRAC and Grameen (also Nidan in India) +
development strategy.
3. **Public vs. Private transcript: presentation of BGD MFIs as** self-financing and profitable, but this is basically wrong— **private transcript** microfinance as part of larger safety-net... parallels to U.S. policy regarding creditor access to transfers.
4. **The subsidy component of Microfinance runs about 30%: but**
about 70% operations self financed (Morduch , 1998).
5. **Grameen II moves toward Accion model** from group to individual lending& savings sans high market interest rates....

*See Ananya Roy, 2010, *Poverty Capital* [pp. 93-132](#).

MFI part of Mohammed Yunus' Bangladesh miracle

1. **Empower women** education & health programs (NGOs +UNICEF+WB –NARI)
2. **Microfinance** + NGO form shadow government (Grameen, BRAC, ASA)
3. Garment exports; **women's jobs** college educated entrepreneurs...?? (UNDP unleashing entrepreneurship report)
4. NGOs/**social entrepreneurship**: mobile Phones Grameen phone, Grameen Yogurt
5. MIA: Migration and remittances?? Check this.

**See also Poverty Capital [pp. 93-132](#) first 10 minutes of this video.*

High interest rates for and against

For high market rates:

- Costs for small loans are higher than large loans: loan fees...
- Local moneylenders charge/hurt more (Sopranos pilot)
- Demand for return to loans is high, among self employed
- Private capital is new low cost source of finance for MFIs .
- High rates select neediest borrowers, assure supply of funds when needed.
- Subsidized lending breeds corruption misallocates capital
- Poor have no collateral (see Hernando de Soto & R&Z)
- Interest rate caps hard to enforce, punish savers.

Against high rates

- High rates can make poorest poorer... the poor always pay
- Moral outrage, predatory lending
- Adverse selection: attracts risky borrowers.
- Moral Hazard & Time consistency problems worse
- Nominal caps close door to private capital restrict supply
- Better incentives than other forms of aid
- Why not subsidize lending to the poor (Morduch?).
- Poor lack legal protection from money lenders (suicide)
- Asymmetric information problems can be addressed

Normal nonpoor borrowers

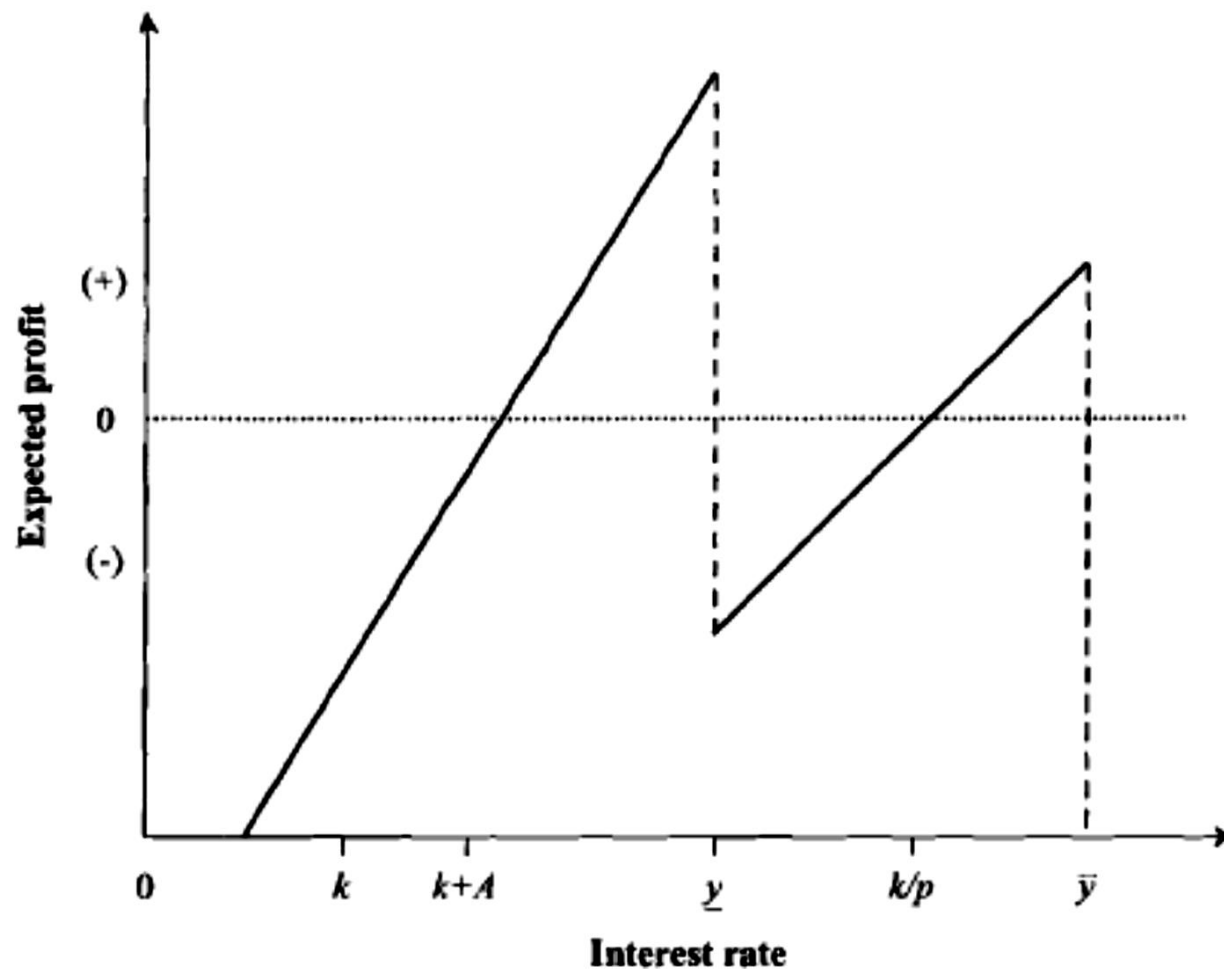


Figure 2.1

Adverse selection example (a). At gross interest rates between $k + A$ and \underline{y} the bank earns a profit and both safe and risky types want to borrow. Safe types leave the market once interest rates rise above \underline{y} , and the bank loses money. Once gross interest rates are pushed up to k/p , the bank can again earn profit, while serving only risky borrowers. At gross interest rates above \bar{y} even the risky borrowers leave the market.

Poor all high risk borrowers

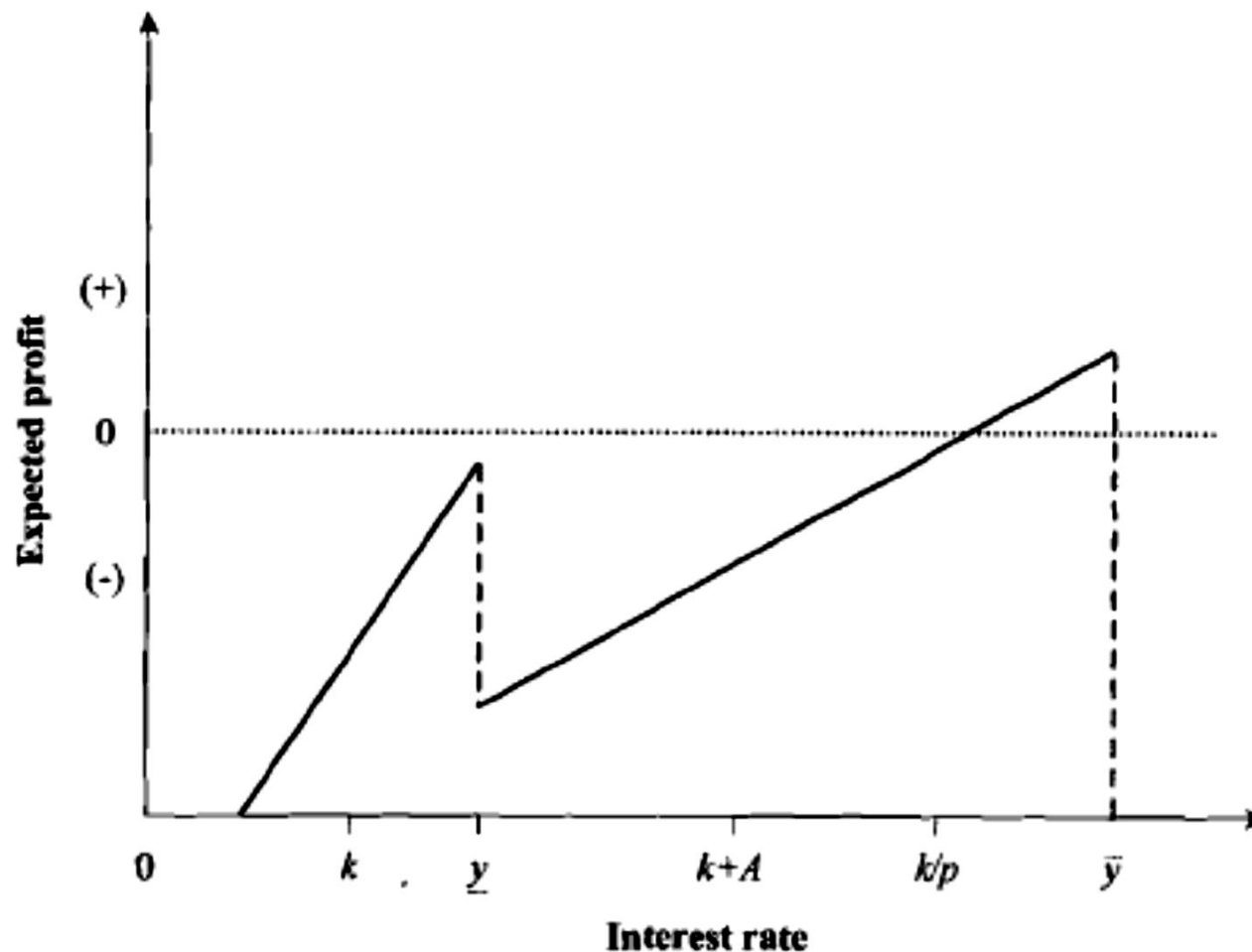


Figure 2.2

Adverse selection example (b). Here, the "risky" types are riskier than in example (a) in figure 2.1. Now the "safe" types can never be served by a bank aiming to break even (since profit is negative even at interest rate y). The bank must raise gross rates to k/p to earn profit, at which price the bank will only attract risky borrowers. At gross interest rates above \bar{y} , the risky borrowers leave the market.

How to reduce cost of small loans?

1. Caps problematic lead to credit rationing ([see Economist](#)) hard to enforce, interest relabeled fees, hidden “overdraft” charges cap on spread cap better, but hard to explain and enforce .
2. Reduce asymmetric information: credit reports, APR , prevents multiple loans....
3. Increase competition in loan market : new entry, banks, mobile or branchless banking....
4. Give/find poor’s collateral (Hernando De Soto’s idea, tyranny of collateral— see Rajan and Zingales Saving Capitalism) Make debt collection easier? (French vs. Spanish legal system)
5. Subsidize lending or guarantee loans (Fannie Mae) but then how to target? Tie to other forms of assistance?
6. ***Best but not easiest way: encourage savings, financial literacy legal aid, transparency (APR) : market rate is return to savings... (opportunity cost) and or,***

Or introduce new savings technologies, or raise return to poor's businesses

1. Larger markets: new technologies (sewing machines, tractors, tube wells.
2. Mobile money, branchless banking, the end of a dangerous [cash economy](#)... remittances costly and lumpy... less so with mobile phones— see the [economics of M-PESA](#)
3. **New BoP products:** mobile phones, (Grameen yogurt) water purifying solar power, large corporations do not block access in developing countries... See Stuart Hart Capitalism at the crossroads...

The case for high vs. low interest rates, again: with or without safety net?

For high interest rates:

1. credit when you need it most: everyone needs credit, especially the poor— a human right?
2. Small loans mean high costs, high interest rates?
3. Informal moneylenders worse; see Sopranos pilot
4. Lenders have agency problems: asymmetric information
5. No collateral + limited liability = high default rates....

For low interests rates

1. Social Justice caps make repayment more likely...
2. Less adverse selection, not just risky borrowers (mission drift)
3. Use NGO's to monitor, provide implicit subsidy, NEDAN video

The IPA-JPAL* critique of MFI's & other Aid:

1. The poor are must not be hungry because they do not spend extra income on calories (Banerjee & Duflo chapter 2, “A billion hungry people?”) – but there are millions of underweight and stunted children?
2. Without randomized trials (RTS) we do not know what really works to reduce poverty, malnutrition, illiteracy, etc. (example: microfinance), they are the “gold standard”
3. Traditional economic analysis of aid and credit and malnutrition needs to take into account corruption and irrationality– people do not always do what is good for them or their children, and this applies even more to the poor (harder to make good choices)

*[Abdul Latif Jameel Poverty Action lab or JPAL](#)

RCTs not Gold Standard, Deaton, 2009

recent experiments flawed (even J-Pal - DFID).

“in ideal circumstances, randomized evaluations of projects are useful for obtaining a convincing estimate of the average effect of a program or project. The price for this success is a focus that is too narrow to tell us “what works” in development, to design policy, or to advance scientific knowledge about development processes. Project evaluation using RCTs is unlikely to discover the elusive keys to development, nor to be the basis for a cumulative research program that might progressively lead to a better understanding of development.” [Angus Deaton, 2009, Randomization in the tropics, and the search for the elusive keys to economic Development, Princeton University,](#)

[See also DFID 2010 Review](#) evidence positive or negative is not strong

Problems with microfinance or direct lending as at Kiva.org or wholeplanet.org:

1. In most randomized trials microfinance does not reduce poverty much (Hyderabad, J-PAL experiments see pages 72-79 in Karlan and Appel, 2011)
2. Mohammed Yunus: interest rates are too high, moneylenders replaced with money lenders.
3. People use funds for consumption not investment. If people cannot afford to save, they cannot afford to borrow either.
4. Kiva.org can mislead regarding direct lending, goes to agency see KA, 2011, p. 15-16, 75, 139.

*Abdul Latif Jameel Poverty Action lab or JPAL

In Defense of microfinance, direct lending :

1. There is some econometric evidence from Bangladesh that microfinance works (BGD is doing well, 10 million borrowers can't be wrong) see [Pitt's reply to Roodman and Morduch](#).
2. Ananya Roy: Social protection + microlending works best private transcript: part of social protection system... ASA, BRAC & Grameen all part of social protection scheme (not real banks).
3. Even at high interest rates, loans reduce Poverty (South Africa experiment, see Karlan and Abel, 2011, p. 44-51, 64-66)
4. Individual lending (Grameen II) is more reliable ROSCAs (rotating savings and credit associations) Tandas, KA, 2011 p. 92-98.
5. Strong evidence that MFIs smooth consumption over time (A&M, 2010 Chapter 9) even if they do not reduce poverty(wrong measure of poverty, vulnerability reduced)
6. But what about Micro Savings?

Compare CCTs to Microfinance: or should we combine them?([World Bank](#))



Growing demand for social safety nets

Demand for well-designed safety net programs to assist poor families is growing across the developing world, as 2009 develops into a year of tough economic challenges.

Governments are concerned that the financial crisis could turn into a humanitarian one, especially for poor households already hit by the recent food and fuel crises.

Not for smoothing income.... During crises hard to scale up... though does protect poorest reducing child labor

CCTs at Glance (World Bank)

Conditional cash transfer (CCT) programs

CCT programs offer qualifying families cash in exchange for commitments such as taking babies to health clinics regularly or sending children to school.

These programs, now found in over two dozen countries, can reduce poverty both in the short and long term, particularly when supported by better public services.

CCTs at Glance (World Bank)

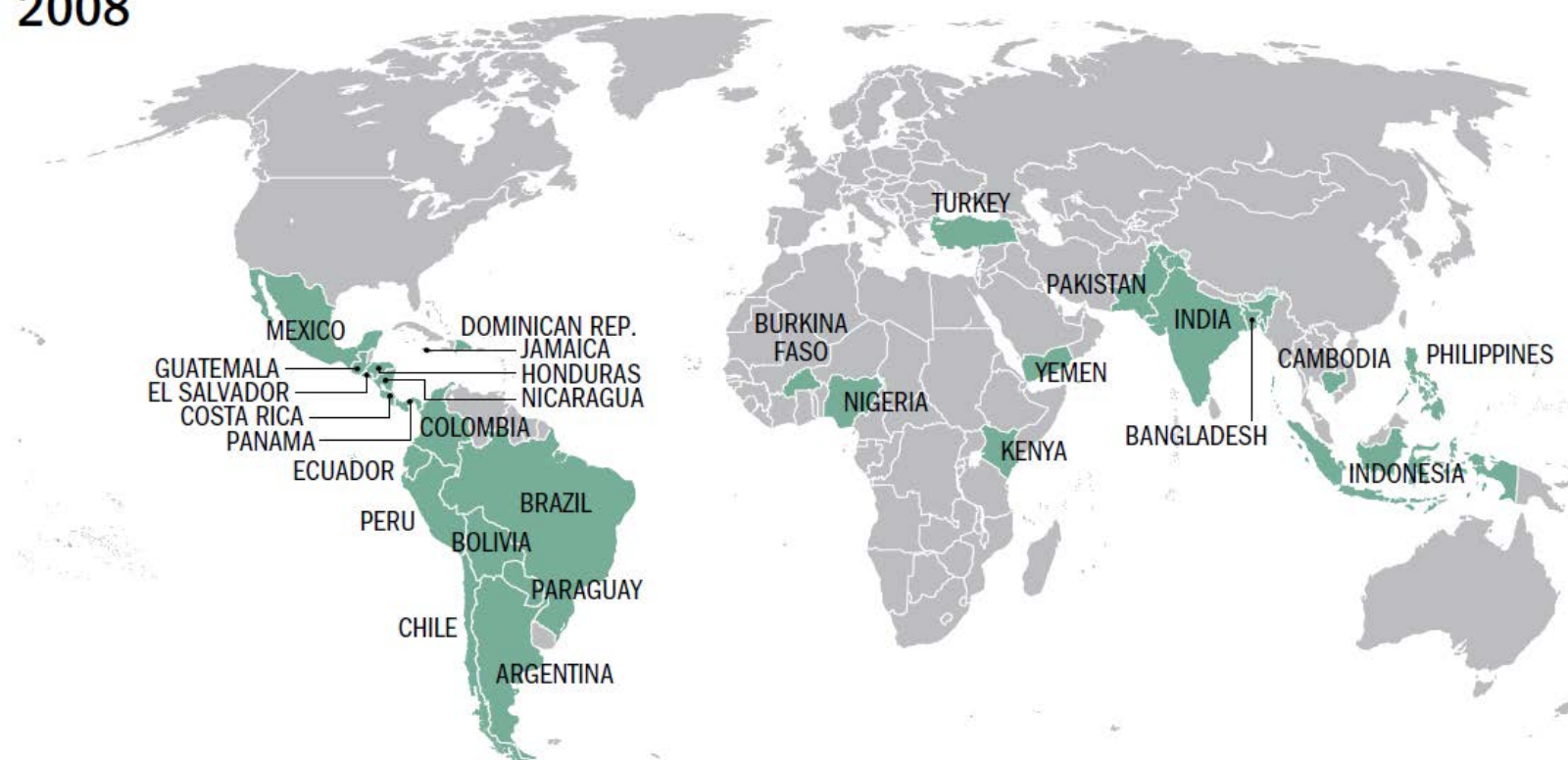
Figure 1 CCTs in the World, 1997 and 2008

1997



CCTs at Glance (World Bank)

2008



Source: World Bank.

Microcredit NIDAN video

- So when you show the YouTube video in class please make sure that you show this attached clip so that you can see the actual correct closed captioning:

<http://www.nytimes.com/2012/04/24/business/global/in-bangladesh-strong-promise-of-economic-growth.html?pagewanted=all>