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The Myths Behind Microfinance

By Jude L. Fernando

Recent revelations about the role of Nobel Prize winner Muhummad Yunus in the alleged misuse of $100 million by the Grameen Banks (and the cover-up of that misallocation) have begun to provoke overdue discussions on the value of microfinance in the developing world. Arguments against microfinance center around the claim that it is a development strategy increasingly forced on the poor, and that those who are claimed to benefit from it the most--poor women--are actually its chief victims. Critics have long sought a platform to reveal the weaknesses and explode the myths supporting microfinance.

The first myth is that microfinance requires no collateral. That is nonsense. Microfinance group leaders and NGO field officers take control of all the household assets of the borrower (land, home, jewelry, equipment, food reserves, animals, remittances, savings, furnishings, etc.), and force borrowers to convert those assets to cash if there is the slightest threat of default of any borrower within the group. Peer-group pressure is combined with the threat of being stripped of essential belongings, and becomes a powerful disciplinary. Borrowing households lose control over physical assets, the ability to determine its pattern of consumption, and use of labor, ceding them all to the community and the microfinance lending agency. Given a model like this, it is no surprise that those viewed as potential defaulters are harassed not only by the lenders, but by their peers, sometimes to the point of physical violence and suicide as has been the case in India.

The second myth is that microfinance empowers women. Women are often the target of microfinance programs, but they do not benefit in proportion to their numbers. A Grameen Bank loan officer in Tangail explained this in no uncertain terms: "Women are willing to make any sacrifice to repay the loans, even if it means sacrificing their own personal consumption. Don't you know that all mothers do that? And it is easier to control women than men. Men could easily disappear after borrowing money, but women stay at home to take care of children." If a woman defaults, it's considered a failure of household management, and brings shame and dishonor on the families. Lenders mobilize the same forces that already oppress women, taking advantage of the inherent inequity of gender roles to apply peer-group pressure. This worsens, rather than improves, the situations of poor women. Children also suffer. In Bangladesh, many children drop out of school to assist their parents in making weekly loan repayments.

The third myth is that microfinance provides low-interest loans on reasonable terms. The nominal interest rate charged by NGOs is often much higher than that of local money-lenders. Real interests are even higher because group leaders and NGO officials withhold a percentage of the total loan amount, while at the same time charging interest on the full amount, in addition to the various fees and compulsory savings program. Nor are NGOs flexible in terms of repayment. Money-lenders regularly grant extended grace periods and often accept payments in kind. Microfinance fails to take the money-lenders out of the equation, and money-lenders regularly supplement NGO loans as well as functioning as their guarantors. This ensures that the wealthiest community members will retain financial control over the poor.

The fourth myth is that loan repayments correspond to increases in income and sustainable economies. They don't. NGOs don't care where their borrowers invest, and productive local enterprises are often undermined by cheap imports, indicating conflict between the theory of pro-poor microfinance, and the reality of free-market policies. The unsustainable nature of microcredit is evident in ever-higher rates of loan defaults. Far from making NGOs self-sufficient, and covering all their costs, gains from microcredit tend to be used to pay above-average salaries for NGO employees and expensive overheads. Donor organizations describe this as "credit pyramiding," and NGOs resort to dubious practices and oppressive methods to cover up the shortfall, including using donated funds to cover losses, and moving money around in and between organizations.

Micro-finance can only be considered a temporary measure. It does not cure the problems of poverty, make communities self-sufficient, or empower women. It does provide an attractive cover for states and donors who wish to rationalize de-funding state social and economic programs for the poor, and allocating resources to support high-growth industries for the benefit of the rich. Feminists, especially, should be aware that their rhetoric has been hijacked by the very institutions that oppress women and enforce gender inequality, and that have increasingly feminized poverty.

More than micro-loans, what the poor need are investments in health, education, and the development of sustainable farm and non-farm related productive activities. Donors have decreased investments in health and education in favor of microfinance, and NGOs have been forced to adopt microfinance as a path to their own financial self-sufficiency. But microfinance cannot compensate for the decades of privatization and reduction of state investment in the public sector. Nor can borrowers meet larger social and economic needs through their meager incomes, so the end result is that the poor once again pay the price for the inadequacy of national and international institutions.

In the end, the microfinance industry looks less like aid, and more like the export of global capitalism. Microfinance demonstrates the creativity and power of neoliberal capitalism, using the misery of the poor to further the interests of the global financial system. It is time for the international donors to review the microfinance industrial complex to ensure microfinance will not exploit the poor and not substitute for investments in education, health and institution building.

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