

# Notes on Grameen Banking and the Microcredit Movement

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**Presenter:**

**Leigh Tesfatsion**

Professor of Economics and Mathematics

Department of Economics

Iowa State University

Ames, Iowa 50011-1070

<http://www.econ.iastate.edu/tesfatsi/>

[tesfatsi@iastate.edu](mailto:tesfatsi@iastate.edu)

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# Background to the Debate

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- ◆ *Microcredit* = Extension of small loans to entrepreneurs too poor to qualify for traditional bank loans because no collateral.
- ◆ Reliance on trust and community peer pressure to maintain high repayment rates.
- ◆ Concept attributed to **Dr. Muhammad Yunus**, founder of **Grameen Bank Project** (Bangladesh, 1976)
- ◆ Winner of **2006 Nobel Peace Prize & US 2009 Presidential Medal of Freedom**

# Grameen Bank Project

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- ◆ A “socially conscious capitalist enterprise” based on **three principles**:
  - Loans are to be repaid, and on time
  - Only poorest villagers are eligible for loans
  - Loans are to be primarily made to women (most impoverished, & best way to help children)
- ◆ Transformed in 1983 into a ***private*** independent bank, the ***Grameen Bank (GB)***.

# Standard GB Loan Process

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- ◆ To qualify for GB loan, family assets must fall ***below*** a certain threshold set by GB. ***No collateral required to be a GB borrower.***
- ◆ GB borrower must join 5-member group of borrowers and behave in accordance with ***"sixteen decisions"*** promoting loan discipline.
- ◆ GB borrowers continued access to GB credit depends on prompt repayment by ***all*** of her group members.

# GB Loan Process...Continued

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- ◆ *Most GB loans are short-term* (about two years) with an annual interest rate of 20% on a declining principal.
- ◆ *GB never forgives loans*, although it restructures loan repayments (extends their maturity) when necessary.
- ◆ GB provides *no free services*.
- ◆ *GB loan repayment rate is 98%*

# Questions and Challenges

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## ◆ Long-Run Financial Viability of GB

- *Repayment problems?* (hidden by non-standard accounting procedures?)
- *Other issues?* See, e.g., D. Pearl, WSJ, Nov 2001  
[online.wsj.com/public/resources/documents/pearl112701.htm](http://online.wsj.com/public/resources/documents/pearl112701.htm)
  - Loans used for consumption, not production?
  - Groups forcing GB to offer lenient repayment rather than acting as loan repayment enforcement mechanism?
  - GB borrowers taking out multiple overlapping loans from multiple institutions?

# Questions and Challenges...Continued

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## ◆ GB transferable to other cultures?

- *Requires a culture of entrepreneurship?*

- *Success due to Mohammed Yunus?*

(charisma & leadership skills, not institution per se?)

- *Track record of microcredit in USA?*

- First program was ACCION USA in NY in 1991, currently the largest microlender in USA

( <http://www.accionusa.org/> )

- “No micro-enterprise lender in the U.S. has come close to breaking even.” Borenstein 1995

- Grameen America founded (NY) January 2008 <sup>7</sup>

# On the other hand ... !

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- ◆ Imran Matin (2002) = Empirical study that provides a much more upbeat assessment about more general move to “microfinance”.

***Microfinance*** = Savings, insurance, and credit instruments (more general than microcredit)

- ◆ **Matin concludes:** “the careful tailoring of microfinance products and arrangements to local demand and supply conditions can achieve substantial improvements in the daily lives of the poor while at the same time ensuring financial self-sufficiency.”

# What Does Official GB Site Say?

<http://www.grameen-info.org/>

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- GB has approximately 1,658 branches operating in 57,791 Bangladesh villages with staff of 14,989.
- Currently (Dec 2010) GB services over 7.5 million borrowers (96% women) with a loan recovery rate of 98%, and has been profitable in all years except 1983, 1991, 1992 (cf. audit statements).
- Borrowers of GB own 94% of total bank equity. Remaining 6% owned by Bangladesh government.
- Since 1995 GB has relied entirely on its own deposits to run and expand its credit program.
- GB has expanded into a family of GB enterprises

# Summary of Basic Issues

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- Can trust and peer pressure replace legal requirements (e.g., collateral) in ensuring high loan repayment rates?
- Should lending be primarily to women as a matter of general policy? Is this “fair”?
- Regarding “sixteen decisions,” is this an intrusion on the private lives of GB borrowers?
- Will GB concept ultimately work well in U.S.? Elsewhere?
- Should poor people be assured access to credit as a matter of general economic right?

# Recent Microcredit Controversies

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- In recent years, charges have been raised against GB and microcredit lending more generally:
  - Ulterior political ambitions (rival political party)
  - Excessive profit taking (interest rates too high)
  - Strong-arm lending tactics
  - Moral hazard problems with borrowing uses
  - Corruption charges (improper fund transfers)
- How charges will be resolved remains to be seen.