“MICROFINANCE IN THE DEVELOPING WORLD”
NINT 5187/CRN 6376
Fall 2010

Wednesdays, 8:00 pm – 9:50 pm
66 West 12th Street; Room 601

What the Course Is About

Poor people have limited if any access to financial services from the usual financial institutions, especially in developing countries. And yet small-scale financial services – safe savings, appropriate credit, personal insurance, and the ability to make and receive payments at moderate cost (such as receiving remittances from relatives working abroad) – are important services that poor households should have in trying to manage their affairs or wishing to take advantage of small business opportunities. While institutions set up by governments (e.g., postal savings banks) and community institutions (e.g., savings and credit cooperatives) have traditionally provided whatever formal financial services the poor could access, an international movement of non-governmental organizations, government donors, foundations and private investors has sought over the past 30-40 years to introduce and spread “microfinance” services to the poor worldwide. This course will examine microfinance from the policy perspective in the context of building “inclusive” financial sectors. It will look at issues of demand and supply, and at actual and desirable policies about microfinance. It will ask students to debate controversial issues, of which there are many in this field, which some people hold up as the key to fighting poverty and gender discrimination, and others consider a distraction from more crucial policy changes.

Assignments and Grades

The course seeks to give students an appreciation of the potential opportunities and drawbacks of microfinance. As such, in the first parts of the course, students are asked to master a core of materials, including on financial sector development (focusing on financial services used or not by the poor), the demand and supply of microfinance, and the policy question of how to help build “inclusive financial sectors for development.” Microfinance is, however, a contentious subject and the last part of the course asks students to engage in debates on some of the controversies involving microfinance.

Within this framework, the first parts of the course will mainly comprise class discussions of core readings, concluded by a mid-term exam. To assist students to review the material and put it into context, a “study guide” of questions, some of which will comprise the exam, will be distributed a week before the exam, which will be taken in class in the traditional way.
The last part of the course will mainly take the form of debates/discussions in class on the policy issues indicated in Part III of the syllabus. Each student will sign up to defend one side of one issue. Every effort will be made to equalize the contending sides (e.g., three students should not argue in favor of one position against one student opposed). After initial presentations, other students will be encouraged to enter the discussion by posing questions and comments to the debaters. At the end of class, students may vote on which side won the argument (does not affect grades).

In addition to the oral presentation, each student will prepare a written argument of up to 10 pages (about 2,750 words) supporting his or her position. However, your instructor does not want to see your paper until after you present your argument orally in summary form in class (although you are welcome to discuss it with him at any stage of the process). Students should make whatever revisions they might want in their papers in the light of the class discussion and submit the paper to the instructor within one week of the debate (the only exception is for the last students presenting, for whom a one-week extension is available owing to the need to prepare the final exam). I cannot emphasize enough how important it is to submit papers on time and, if impossible, to ask for an extension (which will be granted).

Lastly, there will be a take-home final exam covering the entire semester. Questions will be distributed one week before the exams are due, which is on December 15. ALL exams are to be turned in to the instructor on the due date.

The final grade will be a weighted average of grades on the mid-term (25%), the paper (25%), class participation, including the debate (15%), and the final exam (35%). If your midterm is a disaster, it will be discounted if subsequent work is improved.

The Syllabus

The basic text for the course is United Nations, *Building Inclusive Financial Sectors for Development* (referred to below as “UN Blue Book”). It is expected that you will also read all the “core” materials below and hopefully will find some of the “additional” readings intriguing enough to read as well. You will see that more readings are assigned in the first parts of the course; later readings are to give all students a common background for the debates. The final exam covers the entire course, including the debates.

[Sept. 1] Introduction: What is all the fuss about? What is the course about?

In class video: “Microfinance, Seen Openly” (Produced for the International Year of Microcredit, 2005 by Agence Française de Développement)

Core

[Barry Herman], *Notes on La Microfinance à visage découvert/Microfinance, Seen Openly*, 3pp [some details in the video explained]

Sam Daley-Harris, *State of the Microcredit Summit Campaign, Report 2009*, Microcredit Summit Campaign, Washington, D.C., pp. 1-6, 35-37 [Enjoy the enthusiasm; mind the hype]

Additional

Daley-Harris, *op. cit.*, pp. 19-32 and peruse Appendix 1 [To get a feel for the scope and variety of

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1 Papers should be double-spaced, with normal margins. Not only is this most fair to the instructor’s tired eyes, it also leaves space for comments and unfortunately your instructor’s handwriting is not clear even under the best of circumstances.
microfinance institutions, as listed in the Appendix]

Elisabeth Rhyne and María Otero, “The Scale of Microfinance” and “Questions about Scale,” in Microfinance through the Next Decade: Visioning the Who, What, Where, When and How, ACCION International, Boston, November 2006, pp. 6-14 [Range of estimates of size of the “microfinance” sector; regional differences]


Part One. Financial services and the poor: evolution of a relationship

[Sept. 15] I. What a financial sector does and how it does it

We take note of the functioning of basic financial institutions in market economies (banks, insurance companies, securities markets and their institutions and financial instruments). We focus on banks and insurance companies, which provide most of the retail financial services that people use, at least non-poor people, although even the middle classes use them less intensively in developing than developed countries.

Core


Warren Brown and Craig Churchill, Providing Insurance to Low-Income Households, Part I: Primer on Insurance Principles and Products, Chapter One “Risks Faced by Low-Income Households,” and Chapter Three “Insurance: The Provider’s Perspective,” pp. 5-9 and 21-29 [Why people demand insurance; how it works as a business; why the poor are usually not well served]


Additional


Inter-American Development Bank, Unlocking Credit: The Quest for Deep and Stable Bank Lending, Economic and Social Progress in Latin America, 2005 Report, chapter 15, “Foundations of Housing Finance,” pp. 209-223 [Why only a small percentage of the region’s housing is financed with mortgages]
United Nations, *World Economic and Social Survey, 1999, op. cit.*, Chapter VI “Capital Markets in Developing and Transition Economies” and Chapter VIII “Venture Capital in Developing and Transition Economies,” pp. 153-182 and 207-224 [Scope and functioning of securities markets (a potential source of funds for microfinance institutions); nascent role of venture capital in emerging economies (a type of finance for “small and medium-sized enterprises” (SMEs) of the non-poor)]

[Sept. 22] II. Who traditionally provides financial services to the poor?

The poor worldwide mainly rely on “informal” finance to meet their financial needs: moneylenders, merchants and families, but also rotating savings and credit associations (ROSCAs). In addition, formal financial institutions for the poor have been created, first in Europe and America in the 18th and 19th centuries and then in Japan and developing countries: savings banks, building societies (savings and loans), credit unions; also, governments often set up small-scale credit programs. Whether government or private initiatives, they started as non-profits, although many have been transformed in the neo-liberal era.

Core

Abhijit Bannerjee and Esther Duflo, “The Economic Lives of the Poor,” *Journal of Economic Perspectives*, vol. 21, No. 1 (Winter 2007), pp. 151-159 and 161-165 [How poor people earn a living and consequences of their little access to financial services]

MicroSave and Financial Access Initiative, “Portfolios of the Poor Briefing Note #9: Three Country Analysis,” June 2010, 5 pp [Summary of findings in Bangladesh, India and South Africa]


Shishir Sharma and S. Chamala, “Moneylender’s Positive Image: Paradigms and Rural Development,” *Economic and Political Weekly* (Mumbai), April 26, 2003, pp. 1713-1720 [Compares recent positive academic rethinking of moneylenders vs. continuing (failing) efforts to replace them]


Additional

Bannerjee and Duflo, *op. cit.*, pp. 141-151; 159-161[Rest of article: who are the poor, how they live]


Juan Buchenau, “Innovative Products and Adaptations for Rural Finance” Excerpt from paper and comments by Carlos Cuevas and Marguerite Robinson, International Conference on Best


[Sept. 29] III. The microfinance revolution

The innovation in microcredit and the different types of institutions that emerged: small and large, non-profit and state (and lately, for-profit), credit only and multiple service providers; enthusiasm and criticism.

Core


Hans Dieter Seibel, “Does History Matter? The Old and the New World of Microfinance in Europe and Asia,” University of Cologne, Development Research Center, for “From Moneylenders to Microfinance,” National University of Singapore, 7-8 October 2005, 16pp [From centuries of social finance for poor people in Ireland, Germany, India to microfinance]


Patrick Honohan, Financial Sector Policy and the Poor: Selected Findings and Issues, World Bank Working Paper No. 43, 2004, Chapter 4 “Impact,” pp. 23-33 [Difficulties in quantifying impact of microfinance on poverty; more confidence in positive impacts on poverty of improved mainstream financial systems, even if poor don’t use them]

Tara Nair, “Commercial Microfinance and Social Responsibility: A Critique,” Economic and Political Weekly (Mumbai), vol. XLV, No. 31 (July 31, 2010), pp. 32-37 [Addressing social responsibility concerns of donor/investors versus clients’ needs]

Additional


Jim Roth, Michael McCord and Dominic Liber, The Landscape of Microinsurance in the World’s 100

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2 India’s numbering system, used in this article, differs somewhat from ours. Lakh denotes 100,000 and crore denotes 10 million; this summer, Rs 100 (100 rupees) = $2.12.
Part Two. The economics of microfinance

[Oct. 6]  I. Issues of demand: Why the poor use or avoid microfinancial services

Demand for microfinance: where you live and how you make your living matters; how confidence in microfinance institutions (MFIs) gets compromised; designing the specific services for needs of target clients matters a lot.

Core


Rani Deshpande, “Safe and Accessible: Bringing Poor Savers into the Formal Financial System,” CGAP Focus Note No. 37 (September 2006), 16pp


Additional


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3 For reference, at the time of writing, about 7 Rand = $1.
II. Issues of supply: The economics of microfinance

Issues: economies of scale and scope in retail finance; bureaucrats versus profit seekers in management; essential ancillary services (credit bureaus, access to inter-bank payments system) and sources of funds for micro-lending (credit union model versus capital market funds). Will commercial banks reach down into the microfinance market?

Core


Brigit Helms, *op cit.*, Chapter 4 “Financial Infrastructure: The Meso Level” pp. 59-74 [IT, payments, credit bureaus and other complementary services for MFIs]

Patrick Honohan, *op. cit.*, Chapter 3 “Is Microfinance Different to the Mainstream?” pp. 11-21

David Porteous, *op. cit.*, Chapter 4 “Promoting Financial Markets which Work for the Poor,” pp 28-38

Jennifer Isern and David Porteous, “Commercial Banks and Microfinance: Evolving Models of Success,” CGAP Focus Note, No. 28, June 2005, 8 pp

Women’s World Banking, *op. cit.*, section 3 “Building Retail Capacity in Microfinance,” pp. 13-18 [Boiled down to bullet points for MFIs, banks and coops]

Additional


Kiendel Burritt, *op. cit.*, Chapter 7 “The Supply of Microfinance in Malawi” (pp. 87-113)

Beatriz Marulanda and María Otero, “The Profile of Microfinance in Latin America in 10 Years: Vision and Characteristics,” ACCIÓN International, Boston, April 2005, pp. 4-34

III. Issues of public policy: regulation, subsidy, how much, how long

Midterm exam study guide/questions distributed today

Controversies over government controls, incentives/subsidies, and regulation of independent microfinance providers reflect the broader controversies about efficiency and equity in economic policy; protecting consumers and protecting institutions.

Core


Patrick Honohan, *op. cit.*, Chapter 5 “Protecting the Vulnerable,” pp. 35-41 [Consumer protection:
predatory lending and discrimination issues]


Additional


David Porteous and Brigit Helms, “Protecting Microfinance Borrowers”, CGAP Focus Note No. 27, May 2005, 8 pp


[Oct. 27] In-Class Midterm Exam on Parts One and Two of the Course

**Part Three. Major policy debates in microfinance**

[Nov. 3] I. Should we worry about high interest rates?

Microcredit is expensive to provide and hardly an example of a classical competitive market. Still, many people say the market should be left alone to set the interest rate. What is the problem if interest rates are high? Targeted subsidies can bring down interest rates from levels that would be needed to fully cover costs, but is this a good use of public monies? Advocates of uncontrolled interest rates say that high profits of lenders will attract new entrants and competition, but how reliable is this and is it fair to those who pay in the meantime?

Core

MicroSave and Financial Access Initiative, “Understanding Price,” Portfolios of the Poor Briefing Note #8, June 2010, 2 pp


Adrian Gonzalez, “Analyzing Microcredit Interest Rates: A Review of the Methodology Proposed by
Mohammed Yunis,” MIX Data Brief No. 4, February 2010, 6 pp.

David Porteous, “Competition and Microcredit Interest Rates,” CGAP Focus Note No. 33 (February 2006), 16 pp [Competition said to have brought down interest rates in Bolivia, although not in Bangladesh nor Uganda]

Rahul Dhumale and Amela Sapcanin, “An Application of Islamic Banking Principles to Microfinance,” UNDP Regional Bureau for Arab States, in cooperation with the World Bank, December 1999, 14 pp

Additional

Dean Karlan and Jonathan Zinman, “Credit Elasticities in Less-Developed Economies: Implications for Microfinance,” American Economic Review, vol. 98, No. 3 (June 2008), pp. 1040-1068 [Full study on which Karlan above is based]


[Nov. 10] II. Should we be an anti-poverty program or a bank?

Once MFIs grow to a size that can operate relatively efficiently, what next? One part of the industry promotes transforming these MFIs into commercial banks, offering the full range of banking services, with a continuing focus on serving the poor. Others say that is the path of “mission drift” and they should remain anti-poverty institutions that offer a financial service as part of a broader package. Proponents of commercial microfinance deny mission drift, although even proponents acknowledge areas need attention, such as in maintaining a focus on serving poor women.

Core


BRAC [excerpt from BRAC web page], July 29, 2008 (7 pp.)


Michael Chu, “Commercial Returns at the Base of the Pyramid,” Innovations, Winter/Spring 2007, pp. 115-146 [It’s a profitable business and the only way to adequately scale]

Additional

Comments on “Compartamos IPO: Microfinance Doing Good, or the Undoing of Microfinance?” Microcredit Summit E-News, vol. 5, Issue 1 (July 2007), extract, 5 pages [Three pro and three con]


[Nov. 17]  III. Micro-insurance for health care?

Micro-insurance policies can be attractive to poor people who face the risk of heavy personal outlays or having to do without. However, purchased insurance (whether or not subsidized) may be compared with mandatory coverage and/or state (or subsidized private) provision of the service. Health care is a case in which state-provided quality in developing countries has sometimes been low. Which should be promoted: microinsurance for purchased health care or a more effective national health care system?

Core


Denis Drechsler and Johannes Jütting, “Private Health Insurance for the Poor in Developing Countries?” Development Center of the Organization for Economic Cooperation and Development, Policy Insights No. 11 (5 pp)


Additional

Akash Acharya and M Kent Ranon, “Health Care Financing for the Poor: Community-based Health Insurance Schemes in Gujarat,” Economic and Political Weekly (Mumbai), September 17, 2005, pp. 4141-4150


[Dec. 1]  IV. Does microfinance empower women?

Microfinance has been seen as a way to empower women, but there are accusations that it has been manipulated by men and caused additional violence against women. Does access to financial services equal empowerment? Is it sustainable?

Core

Beatrix Armendáriz de Aghion and Jonathan Morduch, The Economics of Microfinance (Cambridge:

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4 See footnote 3 on India’s numbering system.


Additional


UN Capital Development Fund, Innovating from Experience: Gender Initiatives in Microfinance, Roundtable Proceedings, New York July 2001 (14 pp)

[Dec. 8] V. Should I donate to a microfinance institution?

Microfinance promotion is seen as “social” and “economic” development policy. Microfinance seeks international official sector grant and loan financing, and private donations. Is this a good use of aid funds or charitable giving?

Core

Women’s World Banking, op. cit., section 5 “Role of Global Players” pp. 22-23 [“State of the art” on international aid guidelines, 2005, boiled down to bullet points]


Richard Rosenberg, “Does Microcredit Really Help Poor People? CGAP Focus Note No. 59 (January 2010), 8 pp [The industry fights back]


Additional


Part Four. Closing out the semester

[Dec. 15] Summary, stock-taking, suggestions for next time

*Final exam due by class time*