Microfinance Institutions: Norms, Values And Rules In The Growth Of Self Help Groups

A.V.V.S. Subbalakshmi, Project Officer, VIT University, Vellore – 632 014 TN

Abstract

Some microfinance institutions base their interactions on rigid norms or rules; while others are based on values. It is argued that the private sector will tend to produce the operating rules of the microfinance system while the not-for-profit institutions that are using an inclusive decision-making process are more likely to influence the ethical norms in the sector. Nevertheless, this classification is not static as recent events in South-India shows that norms, such as the interest rates, can be politically and emotionally invested to the point that they are about to become values in the sector. Micro credit has established itself as an integral part of financial sector policies of merging and developing countries in the past decade. In the field of international finance, it is renowned for its bottom-up approach, because of the main role of non-governmental organizations in the launching and the development of the sector, with the financial support of donors. This paper studies the micro credit institutions through their internal workings and studies the role of norms and values in the microfinance sector.

Key Words: Microfinance - Investment - Merging – Non-governmental institution – International Finance.

Introduction

Although the word FINANCE is in the term microfinance, and the core elements of microfinance are those of the finance discipline, microfinance has yet to break into the mainstream or entrepreneurial finance literature. The purpose of this paper is to study the finance academic community to the discipline of microfinance, microfinance institutions, rules, norms in the growth of Self Help Groups. Throughout the world, poor people are excluded from formal financial systems. Exclusion ranges from partial exclusion in developed countries to full or nearly full exclusion in lesser-developed countries (LDCs). Absent access to formal financial services, the poor have developed a wide variety of informal, community-based financial arrangements to meet their financial needs. In addition, over the last two decades, an increasing number of formal sector organizations (non-government, government, and private) have been created for meeting those same needs. Microfinance is the term that has come to refer generally to such informal and formal arrangements offering financial services to the poor. Focused interest in microfinance has lagged behind industry development, but it too is now growing rapidly. Before 1997, academic journals published only an occasional article on microfinance, but since that time, academic journals have published hundreds of peer-reviewed articles on the topic. Nonetheless, microfinance has yet to break into finance journals. This despite the term finance in microfinance and the fact that the basic products offered by microfinance institutions (MFIs) namely investing (savings), lending (credit services), and insurance (risk management) are all well-established topics of mainstream finance research.

Norms- Values and Rules of Microedit Institutions

The key insight that this figure provides is the importance of the positioning of cooperatives. They have a relatively high inclusive decision-making process, and could provide a counterweight to the centralized regulation-driven private for-profit sector. There could also theoretically be a role for the Regional Rural Banks in this balancing effort, as they were specifically created to be active in the void between the private sector and the non-profits. However, as long at they will be subject to political interference that distorts their priorities, it is unlikely that they will be able to fulfill that role. The Public
Trust Organizations in India that are involved in microfinance are in fact consensus decision-makers, and exhibit both the negative and positive effects of this structure. Finally, there is a logical correlation between the hierarchical decision-making and centralized development processes; while inclusive decision-making supports more un-centralized development models.

**Interactions: Between Norms and Values**

Another reason why a complementary approach is a valid one in microfinance can be found in the type of group interactions operating within different institutions. Our starting point to assess the institutions’ interactions is the classification of human interactions developed by Merckelbach and Dupas (2001). This new model provided an additional insight about the internal workings of the institutions. Instead of the centralization of decisions, the key criterion becomes the type of group interactions that are used to reach a decision. In short, it provides another way of slicing through the human fabric of the different MFIs. To analyze the group interactions, the concepts of norms, rules and values must first be introduced. We will define as “norms” standards of behavior on which individuals adjust them more or less voluntarily.

It suggests a standard of conduct, which people believe they ought to follow lest they should expose themselves to some way of sanctioning (Coleman, 1987). Different organizational structures easily lead to different norms. For instance, a norm in the Grameen-style institutions is the weekly meetings, which are supervised by a MFI worker. The worker also maintains the records, while the savings and repayments are collected by the members and given to the worker (Harper, 2003). Some norms by the SHGs are, for instance, the fact that the interest rate level that is decided by the group themselves. The SHG carries out all the same functions as required by the Grameen system, but they do this on their own behalf. Moral norms act as a substitute for, or a reinforcement of, state-engineered rules or control mechanisms, with the result that enforcement and punishment institutions become of secondary importance (Platteau and Baland, 1996). They can be seen as cultural beliefs that have the effect of truncating the players’ space or modifying their preference or payoffs. However, moral norms are never completely compelling and decision outcomes cannot be considered to be mechanically determined. Social or community norms are stable expectations shared among repeatedly interacting players concerning each other behavior in default contingencies that would make a certain standard of behavior self-enforcing (Aoki, 2001). “Rules” are crystallized norms, stiffening into a hard code of conduct, and are therefore less flexible than norms. “Values” are norms emotionally invested. Are there moral norms in microfinance? Very few. Keeping interest rates low is not per se a moral norm in microfinance (Hudon, 2006). Nevertheless, example of MFI with high ROA and FSS, high-operation costs, and high-interest rates charge to their clients can be a case of moral norms.

For instance, Compartamos, a member of ACCION international network based in Mexico, charges borrowers an effective interest rate above 110 percent per year, above the moneylender interest rates, with a relatively inefficient administrative structure. Nevertheless, this has enabled the MFI to get a A rating by the Standard and Poor’s rating agency and get extra funds for instance through a 100 million-peso bond (approximately $10 million) (Armendariz de Aghion and Morduch, 2005) and maybe to expand their activities and serve additional clients. Many actors in the sector criticize this financing strategy and operating process. It is the addition of the factors that can lead to a moral norm. Some old norms can evolve while others simply disappear. Group lending was a norm in the 1970s and 1980s. Later on, many institutions have offered individual loans, some even fully switching to individual lending. One can, however, estimate that the microfinance sector’s values remain the same, with the global poverty alleviation as common leitmotiv. This does not mean that they all share the exact same mission. For instance, the President of Accion, a major explained that: BancoSol is not mission-driven it is segment-driven. Just as McDonalds is not likely to start serving haute cuisine, BancoSol is not likely to move away from the segment of market it serves best (Rhyne, 2001). Nevertheless, the value of poverty reduction is present in most MFI’s mission and communication. To classify different types of
relations inside a group, Merckelbach and Dupas (2001) use a matrix with on the horizontal axis the common action; and on the vertical axis the values and ambitions shared by the members. This matrix identifies thereby four types of group interactions. They have been nicknamed as follows: the “Council,” the “Circle,” the “Band” and the “Partners”

On the other hand, one can estimate that it is, until now, the not-for-profit and the inclusive decision-makers that have the biggest impact on the ethical norms and values in the sector. They thereby shape what is different in the practices of microfinance compared to conventional finance. Some norms can be emotionally invested, through political or social actions. Recently, South-India has seen social movement where borrowers would refuse to repay after the publication of articles arguing that microfinance institutions are exploiting their clients (Fouillet, 2006). District authorities then decided to close 50 branches of two main MFIs following allegations that they were charging usurious rates (Shyldendra, 2006). Interest rate ceilings established to limit the level of interest rate on the basis of their potential effect on the poor are examples of emotional investment of norms.

Conclusion

The profitability and the inclusion of the decision-making process, to show that the various strengths of the organizational structures can be combined within an effective overall microfinance framework. The final objective of microfinance is not just to reach all the poor, but also to provide a way for them to systematically improve their long-term income. Norms have strongly involved in microfinance since the start of the sector at the end of the 1970s. Some norms, such as the group lending methodology, are no more overwhelming while others have emerged, such as the financial self-sufficiency. The sector is increasingly shaped by norms, such as the financial independence from donors, and incentives to reach these norms. Specifically, for the case of the Southern Indian development, the complexity and diversity of the social and economic realities is such that it would be believe that one single type of organization structure would be perfect to deal with all of them.

Exploiting the full range of the possibilities of those different structures may be valuable for a fully successful development in India. We find that one of the described organizational structure, the private commercial banking one; base his working process on rigid rules; while other types of institutions are still much based on values.

References


