MICROFINANCE AND SOCIAL CAPITAL

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One of the pillars of microfinance's strength lies in its channeling of pre-existing community social capital via joint liability and group repayment meetings. Yet, beyond being an input into the group-lending model, is expanded social capital also a product or output of microfinance? And if so, does expanded social capital bring potential economic or social returns to either microfinance clients or microfinance institutions? A CMF study in peri-urban of Kolkata provides preliminary some answers.

POLICY QUESTIONS[1]

The group repayment meeting, one of the pillars of microfinance, is typically a short weekly event where members convene to repay installment on their loans. Within the fifteen to thirty-minute gathering the members usually repeat an organizational oath, and then methodically pay the loan officer who marks passbooks; in between payments the members interact with each another and if necessary, vouch for delinquent clients.

Besides being a stock practice of most microfinance institutions, group repayment meetings are also a focal point for debate and research on microfinance's impact. As a development and financial intervention, microfinance is thought to have both economic and social impact on poor households. While metrics of capturing impact are manifold, the Centre for Micro Finance has launched an innovative study to examine group repayment meetings as a mechanism for impact. In conjunction with the Village Welfare Society (VWS), the Centre for Micro Finance and development economists at Harvard University are conducting research on social capital generated through the frequency of group meetings.

The Village Welfare Society (VWS), a microfinance institutions based out of West Bengal, allowed the Centre for Micro Finance to engage with their clients for this project. VWS lends only to women and targets entrepreneurially-inclined households that run on under $2/day. Groups at VWS range from eight and thirteen clients and members receive an initial loan of Rs 4000 (~USD$80); while members repay in groups the liability is primarily individual.

1.Results for this policy memo were taken from the CMF Working paper "Building Social Capital through Microfinance." By Benjamin Feigenberg, Erica Field and Rohini Pande (last revised October 2009). Paper available online at **http://ifmr.ac.in/cmf/publications/wp/2010/35_Feingenberg_Social_Capital_Microfinance.pdf**

INTERVENTION

The research team randomly divided one hundred groups of new microfinance clients, just over 1000 women, into two categories – the first category met weekly to repay their first loan, while the second category met monthly. Clients either repaid their Rs. 4000 loan through 44 weekly installments of Rs 100 if they were on the weekly repayment schedule or eleven Rs. 400 installments if they were on a monthly repayment schedule. This translated into weekly clients' meeting on average 37 times and the monthly clients meeting on average 10 times, over the course of the first repayment period. By comparing these two categories of clients, who aside from the repayment schedule were indistinguishable along socioeconomic lines, the research team could examine differential impacts of meeting frequency.

FINDINGS

After five months of loan repayments, both weekly and monthly clients knew more about one another and interacted more frequently outside their meetings. However, as one might expect, clients in weekly groups knew more about their fellow group members than those in the monthly groups. Members of weekly repayment groups, for instance, were 90% more likely than monthly members to know group members' families and to have visited them in their homes. Clients in weekly repayment schedules trusted fellow members more - for example, weekly clients were 25% more likely to say that group members would help one other in a health emergency.

When the research field team revisited a sub-sample of weekly and monthly clients a year after the initial Rs. 4000 loan repayment period had concluded, they found that weekly repayment clients still interacted socially at a significantly higher level than monthly clients. Thus the frequency of interaction of the repayment meetings generates greater social knowledge, social capital, and trust between group members.

Returns of Social Capital to Clients

To gauge whether this newfound social knowledge had any positive external effects, an additional field experiment was conducted in the form of a lottery. The research team approached a random subset of weekly and monthly clients roughly twelve months after the first Rs. 4000 repayment cycle had concluded. The lottery was a single draw contest for a Rs. 200 voucher prize redeemable at the Village Welfare Society (VWS) bazaar store; entrants joined a pool of ten other clients from VWS branches in different neighborhoods.

Researchers asked the randomly selected subset of weekly and monthly clients whether they would be interested in entering fellow group members into the lottery drawing. The woman faced the choice of diminishing her individual chances of winning, depending on how many group members she entered, but increasing the chances that someone she knew would win. She was informed that she was the only entrant who could influence these chances.

This exercise measures trust or altruism or some combination of both. To further nuance the results, the research team created and randomly presented two types of lottery prizes to clients. The first was a single Rs 200 (about USD $4) voucher and the second was Rs 200 split into four Rs. 50 vouchers. The first type of ticket could not be divided, while the second ticket containing four Rs 50 vouchers could easily be divided and shared. These two types of vouchers were used to test whether clients entered fellow group members in the lottery because they were being kind or altruistic, or because they expected their group member to reciprocate and give them a share of the voucher. If altruism drives the results, then we would expect no difference in the giving of the single Rs. 200 voucher or the four Rs 50 vouchers; however if clients entered names on the expectation they would share in their group members' winnings, we would expect higher giving of the easily divisible voucher.

Expected Reciprocity Drives Lottery Ticket Sharing

Less than half of clients, both monthly and weekly, approached for the lottery entered group members into the draw. Weekly clients were more likely to send a lottery ticket to a group member than monthly clients, but the difference was significant only when the Rs. 200 prize was easily divisible. This result implies that expected reciprocity rather than altruism drives the ticket sharing and that group meetings may not foster goodwill among members but rather trust and desire to share risk together. Furthermore, VWS clients who had been randomly selected for weekly meetings in both their first and third loan cycles were 70% more likely to share tickets than those who had been shifted from weekly to monthly between loan cycles. Additional predictors of ticket sharing include whether a group member lives nearby, whether they knew them prior to taking a loan, and group leaders were frequent recipients of tickets (perhaps due to their perceived trustworthiness and group position).

Returns of Social Capital – Medium Term Default

Beyond the effects of repayment meetings on trust and reciprocity among clients, analysis of VWS' transaction database revealed medium-term impacts on client default. In the first loan cycle, where new clients were given Rs. 4000 of credit, the frequency of group meetings did not appear to impact default or delinquency. But by the second loan cycle, clients who were part of the monthly repayment meetings during their first loan cycle were 8% more likely to default than those in weekly repayment meetings during the first loan cycle.

POLICY IMPLICATIONS

The repayment frequency project reveals what proponents of microfinance suspect – group lending can build up social capital among clients that can be leveraged for both for clients and for the microfinance institutions. More broadly, the findings suggest that entities, such as the microfinance repayment group, that promote interaction amongst the poor can create trust and reciprocity in a finite period of time. Such social capital could then be leveraged for other joint-liability products and services, both within the purview of microfinance and beyond it. As the principal investigators close in their paper:

"In the case of group lending, by broadening and deepening social networks, microfinance institutions may have an important influence on the growth potential of poor communities and the empowerment of women above and beyond the role of credit provision." (Feigenberg et al pg 28)