

## **Microfinance-Credit lending models**

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Microfinance institutions are using various Credit Lending Models throughout the world. Some of the models are listed below.

### **Associations :**

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This is where the target community forms an 'association' through which various microfinance (and other) activities are initiated. Such activities may include savings. Associations or groups can be composed of youth, or women; they can form around political/religious/cultural issues; can create support structures for microenterprises and other work-based issues.

In some countries, an 'association' can be a legal body that has certain advantages such as collection of fees, insurance, tax breaks and other protective measures. Distinction is made between associations, community groups, peoples organizations, etc. on one hand (which are mass, community based) and NGOs, etc. which are essentially external organizations.

### **Bank Guarantees :**

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As the name suggests, a bank guarantee is used to obtain a loan from a commercial bank. This guarantee may be arranged externally (through a donor/donation, government agency etc.) or internally (using member savings). Loans obtained may be given directly to an individual, or they may be given to a self-formed group.

Bank Guarantee is a form of capital guarantee scheme. Guaranteed funds may be used for various purposes, including loan recovery and insurance claims. Several international and UN organizations have been creating international guarantee funds that banks and NGOs can subscribe to, to onlend or start microcredit programmes.

### **Community Banking :**

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The Community Banking model essentially treats the whole community as one unit, and establishes semi-formal or formal institutions through which microfinance is dispensed. Such institutions are usually formed by extensive help from NGOs and other organizations, who also train the community members in various financial activities of the community bank. These institutions may have savings components and other income-generating projects included in their structure. In many cases, community banks are also part of larger community development programmes which use finance as an inducement for action.

### **Cooperatives :**

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A co-operative is an autonomous association of persons united voluntarily to meet their common economic, social, and cultural needs and aspirations through a jointly-owned and democratically-controlled enterprise. Some cooperatives include member-financing and savings activities in their mandate.

### **Credit Unions :**

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A credit union is a unique member-driven, self-help financial institution. It is organized by and comprised of members of a particular group or organization, who agree to save their money together and to make loans to each other at reasonable rates of interest.

The members are people of some common bond: working for the same employer; belonging to the same church, labor union, social fraternity, etc.; or living/working in the same community. A credit union's membership is open to all who belong to the group, regardless of race, religion, color or creed.

A credit union is a democratic, not-for-profit financial cooperative. Each is owned and governed by its members, with members having a vote in the election of directors and committee representatives.

### **Grameen :**

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The Grameen model emerged from the poor-focussed grassroots institution, Grameen Bank, started by Prof. Mohammed Yunus in Bangladesh. It essentially adopts the following methodology:

A bank unit is set up with a Field Manager and a number of bank workers, covering an area of about 15 to 22 villages. The manager and workers start by visiting villages to familiarise themselves with the local milieu in which they will be operating and identify prospective clientele, as well as explain the purpose, functions, and mode of operation of the bank to the local population. Groups of five prospective borrowers are formed; in the first stage, only two of them are eligible for, and receive, a loan. The group is observed for a month to see if the members are conforming to rules of the bank. Only if the first two borrowers repay the principal plus interest over a period of fifty weeks do other members of the group become eligible themselves for a loan. Because of these restrictions, there is substantial group pressure to keep individual records clear. In this sense, collective responsibility of the group serves as collateral on the loan.

### **Group :**

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The Group Model's basic philosophy lies in the fact that shortcomings and weaknesses at the individual level are overcome by the collective responsibility and security afforded by the formation of a group of such individuals.

The collective coming together of individual members is used for a number of purposes: educating and awareness building, collective bargaining power, peer pressure etc.

### **Individual :**

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This is a straight forward credit lending model where micro loans are given directly to the borrower. It does not include the formation of groups, or generating peer pressures to ensure repayment. The individual model is, in many cases, a part of a larger 'credit plus' programme, where other socio-economic services such as skill development, education, and other outreach services are provided.

### **Intermediatories :**

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Intermediary model of credit lending position is a 'go-between' organization between the lenders and borrowers. The intermediary plays a critical role of generating credit awareness and education among the borrowers (including, in some cases, starting savings programmes. These activities are geared towards raising the 'credit worthiness' of the borrowers to a level sufficient enough to make them attractive to the lenders.

The links developed by the intermediaries could cover funding, programme links, training and education, and research. Such activities can take place at various levels from international and national to regional, local and individual levels.

Intermediaries could be individual lenders, NGOs, microenterprise/microcredit programmes, and commercial banks (for government financed programmes). Lenders could be government agencies, commercial banks, international donors, etc.

### **Non-Governmental Organizations :**

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NGOs have emerged as a key player in the field of microcredit. They have played the role of intermediary in various dimensions. NGOs have been active in starting and participating in microcredit programmes. This includes creating awareness of the importance of microcredit within the community, as well as various national and international donor agencies. They have developed resources and tools for communities and microcredit organizations to monitor progress and identify good practices. They have also created opportunities to learn about the principles and practice of microcredit. This includes publications, workshops and seminars, and training programmes.

### **Peer Pressure :**

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Peer pressure uses moral and other linkages between borrowers and project participants to ensure participation and repayment in microcredit programmes. Peers could be other members in a borrowers group (where, unless the initial borrowers in a group repay, the other members do not receive loans. Hence pressure is put on the initial members to repay); community leaders (usually identified, nurtured and trained by external NGOs);

NGOs themselves and their field officers; banks etc. The 'pressure' applied can be in the form of frequent visits to the defaulter, community meetings where they are identified and requested to comply etc.

### **Rotating Savings and Credit Associations :**

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Rotating Savings and Credit Associations (ROSCAs) are essentially a group of individuals who come together and make regular cyclical contributions to a common fund, which is then given as a lump sum to one member in each cycle. For example, a group of 12 persons may contribute Rs. 100 (US\$33) per month for 12 months. The Rs. 1,200 collected each month is given to one member. Thus, a member will 'lend' money to other members through his regular monthly contributions. After having received the lump sum amount when it is his turn (i.e. 'borrow' from the group), he then pays back the amount in regular/further monthly contributions. Deciding who receives the lump sum is done by consensus, by lottery, by bidding or other agreed methods.

### **Small Business :**

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The prevailing vision of the 'informal sector' is one of survival, low productivity and very little value added. But this has been changing, as more and more importance is placed on small and medium enterprises (SMEs) - for generating employment, for increasing income and providing services which are lacking.

Policies have generally focussed on direct interventions in the form of supporting systems such as training, technical advice, management principles etc.; and indirect interventions in the form of an enabling policy and market environment.

A key component that is always incorporated as a sort of common denominator has been finance, specifically microcredit - in different forms and for different uses. Microcredit has been provided to SMEs directly, or as a part of a larger enterprise development programme, along with other inputs.

### **Village Banking :**

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Village banks are community-based credit and savings associations. They typically consist of 25 to 50 low-income individuals who are seeking to improve their lives through self-employment activities. Initial loan capital for the village bank may come from an external source, but the members themselves run the bank: they choose their members, elect their own officers, establish their own by-laws, distribute loans to individuals, collect payments and savings. Their loans are backed, not by goods or property, but by moral collateral: the promise that the group stands behind each individual loan.