Socio-Economic Differences and Deployment of the LDC Micro-Finance Bottom-Up Approach in DCs

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ABSTRACT

Microfinance (MF), after showing great success in poverty-relief in less-developed countries (LDCs), is experiencing rapid growth and interest in developed countries (DCs). However, current DC MF literature gives the impression that survival concerns are diverting DC MF from its original poverty-relief intent. As e-technology evolves, further threats and opportunities are created for MF by changing cost structures and relationships. This study uses descriptive analysis to infer that DC MF needs redesigning for DC socio-economic conditions or it will continue gaining a reputation of being too poorly focused, ineffective, and inefficient for use in DCs. After showing that LDC poverty is harsher than DC poverty, this paper reviews current-performance concerns of DC MF, links those issues with the effect of regulatory and other socio-economic factors on micro-enterprise, discusses how MF can relieve poverty in DCs, and concludes that MF needs refocusing before DCs investing in further developing/adapting MF infrastructure.

Keywords: Developed Country, Lesser-Developed Country, Microenterprise, Microfinance, Poverty, Regulation, Socio-economics

INTRODUCTION

Microfinance (MF) has a long history of success in lesser developed countries (LDCs). However, MF has many different meanings, from micro-credit to insurance and income protection to social enlightenment (Burkett, 2003). This diversity is conceptualized in this study into seeing MF as a set of tools, approaches, and strategies developed in LDCs to provide bottom-up poverty relief via a *hand-up* to people trapped in poverty by an exclusion from mainstream financial services (Dixon et al., 2006). Buckland and Dong (2008), note that financially-excluded people rely almost entirely on non-mainstream and informal financial services. The well-documented profound success of MF, in helping many LDC poor escape poverty, has sparked debate on its use in developed countries (DCs; Servon, 1997, 2006;

The literature, on DC MF projects, gives a general impression that MF in DCs is failing to achieve its financial and poverty-relief objectives and attributes these difficulties to high administration costs, nonperforming and/or defaulted loans, adverse-selection of clients, cost-recovery issues, difficulty developing appropriate administrative tools, and confusion over its client base and social role. However, this study suggests these issues are symptoms and the progression of DC MF setbacks will continue until the cause is discovered and resolved.

The study seeks to show that the causes of poverty differ from LDCs and DCs and those differences affect the design and deployment of MF in DCs. This study is organized into: a background discussion on how MF works, a contrast of socio-economics in LDCs and DCs, a review of DC MF performance concerns, consideration of the cost-effectiveness of DC MF, and a conclusion that MF needs refocusing to DC conditions.

**BACKGROUND**

**How Does Microfinance Work?**

Micro finance works best with those whose inability to access main-stream financial services either holds them in poverty or puts them at risk of becoming poor. A non-exhaustive selection of poverty at-risk-groups in DCs is given in Table 1.¹

Thus, for MF to work in DCs: 1) difficulty accessing mainstream-financial services must be a cause of poverty; 2) access problems of at-risk groups must be targeted; and 3) the process must be sustainable. If these attributes are absent, DC MF may become an innovative welfare variant and/or boondoggle (mostly benefiting MF providers via employment, power, and status). However, socio-political issues can be as important to those funding MF, as poverty relief. Helms (2006) found that three-of-four common MF-program-funding providers in LDCs are very strongly interested in social development and the fourth is likely to promote itself as having such an interest via government requirements (Goodwin-Groen, 1998; Pitt et al., 2003; Dunford, 2006; Pitt et al., 2006; Deaton, 2009).

**The Effect of Socio-economic Differences on MF in LDCs and DCs**

Understanding the socio-economic differences between LDCs and DCs is vital to understanding why MF is having difficulty adapting to DCs. As noted later, individuals in LDCs often have much higher social capital than people in DCs (Banerjee & Duflo, 2007)—much of this social

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**Table 1. Poverty-at-risk-groups in DCs**

<table>
<thead>
<tr>
<th>Isolation Issue</th>
<th>Examples/description</th>
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<tbody>
<tr>
<td>Culture, history, religion and/or ethnicity,</td>
<td>European Gypsies, Australian Aborigines, Canadian 1st Nations, US Native Americans, multi-generational-welfare families, and new migrants with language issues. Also, ageism (50+ or young adults) or sexism.</td>
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<tr>
<td>Educational challenges</td>
<td>Illiterate, innumerate, inarticulate, unskilled in a trade or profession.</td>
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<tr>
<td>Few employment prospects</td>
<td>Unaccredited and/or inexperienced in the work-force (often directly closely related to the educational challenges above).</td>
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<tr>
<td>Ill-health, disability, or disfigurement</td>
<td>Mental or physical difficulties arising from disease, accident, age, or congenital issues.</td>
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<tr>
<td>Family obligations</td>
<td>Single parent households, the role of wife in a traditional extended family, adult children with disabled parent(s).</td>
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A Web Service Architecture for Revenue-Earning Information Products
www.igi-global.com/article/web-service-architecture-revenue-earning/1502?camid=4v1a