Bangladesh. J. Agric. Econs XXVII, 1(2004) 37-51

ARE COMMERCIAL BANKS PREJUDICED AGAINST THE POOR?

Khandakar Qudrat-I Elahi

ABSTRACT

Microcredit-microfinance revolution is founded on an overwhelming accusation: Conventional banks are prejudiced against the poor, the poor women in particular. This paper examines this popular accusation and argues that its conceptual foundation is weak. First, because commercial banks and microcredit NGOs have differing mandate and motivation, their social roles are not directly comparable. Second, providing loans to micro-entrepreneurs requires special skills as well as a special frame of mind. Commercial bankers may not have this kind of employees due to the nature of their business. Third, the microfinance theory suffers from academic soundness because it is founded on value-laden terms. Fourth, characterizing commercial bankers as anti-poor is professionally unfair. Fifth, holding orthodox economics responsible for poverty creation in the developing world contradicts the reality. Sixth, the criticisms that the para-statal agencies have failed to 'ignite the tires of subsidised agricultural development' are too hasty. Finally, the distinction that microfinance theory makes between commercial bankers and micro-lenders, concerning profit-maximization, has created a new puzzle in microeconomic theory.

I. INTRODUCTION

Microfinance, described as a revolution in rural-finance theory and policy in the current development discourse, seems to be founded upon a controversial accusation that commercial banks are prejudiced against the poor, particularly the poor women (Remenyi 2000; Yunus 1996, 2001): Poor people, including women, possess different kinds of skills that they can use for generating income through self-employment. Their abilities to create self-employment, however, critically depend upon their access to credit facilities. Yet, commercial banks in the third world (TW) countries severely restrict their access to formal financial resources on the ground that the poor are not credit worthy. This orthodox banking principle creates two social consequences. First, it deprives many poor people from their right to make living through self-employment. Second, it forces them to borrow money from informal lenders at usurious rates of interest. In other words, commercial banks in the TW are apparently contributing to the perpetuation of poverty in these countries.

The author is part time faculty, Department of Economics and Social Science, BRAC University, Dhaka, Bangladesh. Dr. M. Lutfor Rahman, Professor (retired), Department *of* Agricultural Finance, Bangladesh Agricultural University, Mymensingh, Bangladesh, read the initial version of the paper and made several comments, which have significantly contributed to the improvement of the manuscript quality. The author gratefully acknowledges this intellectual debt. He, however, remains solely responsible for the paper's residual imperfections.

This accusation, now a conventional wisdom in the microcredit-microfinance literature, seems controversial, because microfinance programs and commercial banks have very different mandate and motivation. The former are exclusively concerned with poverty alleviation, while the latter are involved in serving the wealthy clients for making profits. Given these differing mandate and motivation, they employ staffs with different educational and social backgrounds and aptitudes. These differing mandate and motivation of the two types of financial programs make the accusation highly controversial.

The main objective of this paper is to examine theoretical soundness of this overwhelming microcredit-microfinance accusation. It has been organized as follows: In the next section, the history of original accusation is briefly recounted along with subsequent explanations and . elaborations. Then the paper describes the microfinance view concerning the relation between conventional banks and the poor. This is foflo%.ed.by a critical assessment of the arguments made against the conventional banking policy. Finally, the paper concludes by pinpointing the main inferences that emerge from the analysis.

11. ORIGINAL ACCUSATION AND EXPLANATIONS

The history of the Current microcredit--microfinance movement is often described as the history of evolution of Grameen Bank in Bangladesh during the late 1970's through early 1980's. The founder of this world-famous rural bank is Muhammad Yunus, the then Professor and Head, Department of Economics, Chittagong University. According to Yunus, the idea of establishing this bank grew up out of tension between him and the management of conventional banks (Yunus 1996, 2001). He tried, without success, to convince conventional bankers to make their financial facilities accessible to the poor. Being convinced himself by his own experience-that the poor are bankable, he opened the Grameen Bank in 1983. The history goes as follows:

After a bloody nine-month-old civil war, Bangladesh, former East Pakistan, became independent in December 1971. At that time, Yunus was teaching at the Vanderbilt University in America and returned home immediately after independence. .

Socio-economic conditions of the new country slid from - bad to worse, which eventually caused an infamous famine in 1974. This sad situation badly affected Yunus. To understand problems of the rural poor, he used to visit villages adjacent to the university campus. In one of his visits to Jobra-Grameen's birth place- he met a woman, named Sufiya Khatun, who was making bamboo stools. Out of curiosity, he started a conversation to know about her work. What he learnt made him very guilty (Yunus 1996). Sufiya told bimm that she earned two US pennies a day by making bamboo stools. The reason for this low income was the condition under which she had borrowed money from a trader to buy bamboos: Sutiya must sell her products to the trader at the prices determined by him. In other words, Sufiya was 'virtually a bonded labor'.

To help the villagers like Sufiya Khatun, Yunus prepared a list of all those who needed loans for self-employment. He found 42 such villagers whose aggregate loan demand was US twenty seven dollars in local currency. Yunus lent this money from his own pocket and asked the borrowers to repay their debts as they could. He was pleasantly surprised to see that everyone repaid his or her loans before the time he anticipated.

This event inspired the idea of the now-famous Grameen Bank. To make some kind of regular arrangement for these people, Yunus met the branch manager of the Janata Bank- one of the largest nationalized banks operating at the university campus. The manager took his request as a'joke' and said that the bank could not give loans to these people, because they could not offer collaterals, i.e., they were not creditworthy. However, the branch manager suggested Yunus to meet the bank's higher officials, which he did but returned with greater frustration. Initially, Yunus started an action research project, the Grameen Bank Project, on rural poverty alleviation and provided loans to the project members by borrowing funds from banks in his own name. In few years, the project was successfully replicated in many villages in several districts. Yet, the bank officials remained `unconvinced' about providing loans to the poor, particularly to poor women. Yunus finally applied for government's permission to open his own bank. The 'Grameen Bank Project' became today's famous 'Grameen Bank' on the 2nd October of 1983. He described his sentiment, when he started his bank, with the following words: "And when I began, I made two accusations against the banking system, that it is designed to be biased against the poor, and it is also designed to be biased against women (Yunus 1996)."

Recently, Yunus has offered additional explanations about his accusation against conventional banks. The theme of his theory was outlined in a joint meeting of the Bangladesh Economic Association and International Economic Association, held in Dhaka in April 1998. In his address, Yunus stated: "In a major way economics is responsible for creating the world that we live in. Interrelations among the individuals, nations and institutions, day-to-day activities of all people are shaped in a large way by the role assigned to them by economics. Economics as a discipline not only attempts to explain what goes on in the sphere of economic activities of people and organizations, but it has also vastly influenced their activities by making people believe in what economics says about who they are and what they should do. Economics text-books create the mindsets, mindsets create the world. I think economics has mistreated this world. It got us into a lot of troubles and many human tragedies. For one thing seeds of poverty are planted firmly in the pages of economics text-books (Yunus 1998a: 1)."

Economics, Yunus says, makes three fundamental assumptions, which create mindsets that disfavour, the poor: (a) credit is a neutral tool, (b) entrepreneurs are select groups of people, and (c) capitalism only concerns profit maximization. First, economists cannot adequately address the social and political dimensions of poverty issue, because they do not understand the social power o1 credit. "In economic theory credit has been assigned the docile, passive role of a lubricant. It is perceived as a neutral tool that stimulates commerce, trade and inaustry. Unfortunately this perception ignores the fundamental fact that credit creates entitlement to resources. A person who wishes to build a factory, purchase inventory, buy a store or undertake any other economic activity can do so provided he could convince a financial institution to grant him a loan. Consequently within a social context, credit plays an extremely important role. Credit creates economic power, which in turn creates social power (Yunus 1998b: 53--54)."

Second. production theory, which plays a very vital role in the analytical framework of economics, treats a typical 'person' as a labourer. The key concept in the production theory is production function, which shows how an entrepreneur makes optimal mix of labour and capital to maximize output under the constraint of a given technology: "This fundamental conceptualisation neglects the possibility (and, in the case of the TW countries, the predominant reality) of the self-employment of the masses. Entrepreneurs are considered to be unusually a gifted group of people. Everyone else involved in the private sector is considered to be a wage labourer working under them. This idea appears to economists to be an innocent piece of abstraction. Yet, it is damaging because the creativity and ingenuity of each human being slowly and subtly eroded. The potential within each individual to turn into entrepreneurs disappears. Wage-employment becomes the only legitimate source of employment for all but a small class of people-usually people who own or have access to large amounts of capital (Yunus 1998b: 56)."

Third, the theory of capitalism is `reliant on profit-maximization': "What I disagree with is the feature of profit-maximization seemingly embedded in capitalism. Economic theory portrays the entrepreneur as one who ensures financial return, ignoring any social dimensions or returns. Somehow we have managed to persuade ourselves that the capitalist economy must be fuelled only by profit maximization. Since that belief is shared by many, it has become a self-fulfilling prophecy (Yunus 19986, pp. 61-62)."

IIL CONVENTIONAL BANKS AND THE POOR: THE MICROFINANCE VIEW

Microcredit and Microfinance

Microcredit and microfinance are two recent development buzzwords. Although these words are often used synonymously, the lending ventures they represent are significantly different in terms of both their motives and means of operation.

Microcredit, which denotes small loans but mainly refers to small-scale private lending ventures-has four features that distinguish it from credit supplied by conventional financial institutions (Grameen Bank 2002). FirsL the loan size is very small, averaging about US $100. This general feature differs from one country to another depending upon the differences in the levels of their socio-economic development. Second, the rural poor, particularly women, are the primary customers of these loans. Third, the purpose of these loans is to create income-generating activities through self-employment in rural non-formal sectors. Finally, these loans are collateral-free, a feature that is normally considered risky by the conventional banks. Besides these common and popular features, there is an important aspect of micro lending that does not exist in conventional banking operations: In micro lending, loaning and savings mobilization functions have been integrated. In other words, while micro-borrowers must regularly save with their lenders in order to qualify both the first and subsequent loans, the borrowers of conventional financial institutions are not obligated by this requirement.

This idea was conceived and experimented in a number of the TW countries during the 1970s. However, as noted above, it became popular through the establishment of the Grameen Bank in Bangladesh. The international donor community- which was frustrated with the dismal performance of the TW's public bureaucracies in using international economic assistancebecame impressed by the tremendous success of the Grameen Bank and similar organizations in recovering outstanding loans (95%) and outreaching the rural poor, particularly the poor women. It eventually adopted microcredit as a key poverty alleviating policy instrument. Currently, major bilateral and multilateral donor agencies have special departments to promote micro-enterprises in the developing countries: Consultative Group to Assist the Poorest, Rural Microtinance and Small Enterprise Development, and Sustainable Banking with the Poor (World Bank); Microfinance (ILO); Special Unit for Microfinance (UNDP/UNCDF); Microfinance (UNESCO); Microfinance Development Strategy (ADB); Rural Finance Strategy (IDB); Microenterprise Innovation Project (USAID); and Microfinance and Microenterprise Development (CIDA).

The microcredit idea has now graduated into the microfinance revolution. Although, the operational methods of the two micro lending ventures are basically the same, they differ in terms of motives and means of their operations. The microcredit movement grew up as voluntary philanthropic private initiatives to help the poor with small loans (Korten 1987). Its major sources of fund include donations from national and foreign governments, national and international non-profit organizations, and above all, different donor agencies. In other words, the main motive of microcredit ventures is humanitarian, while the main means of their operations are financial contributions from various agencies and institutions- both private and public. The microfinance organizations, on the other hand, intend to serve the same kind of financial client, but with very different motives and means of operation. Contrary to the popular perception, microfinance refers to `for-profit' financial ventures, which hope to be self-financing to end their dependence on external assistance: "[...] the conventional wisdom has always favoured the view that banking with the poor cannot be undertaken unless it is heavily subsidized. Microtinance, which is about profitable banking with the poor, challenges this view. Subsidized credit and subsidized banking with the poor are inimical to the `best practice' in microfinance (Remenyi 2000: 27)."

Banking with the Poor

The microfinance literature often subtitles the new finance industry with the catchphrase 'banking with the poor' (Ledgerwood 1999). The purpose of this practice is to underline the main objective of the new industry and the type of financial client it intends to serve. And ordinarily, a short introduction precedes the detailed discussion that focuses on the reasons the new development paradigm has evolved.

The microfinance academia (Adam, Graham and Pischke 1984; Hulme and Mosley 1996; Remenyi 1999; Woller and Woodworth 2001) believes that this financial revolution has taken place over the past decade, because of the failure of the para-statal agencies, including the rural credit institutions, to achieve their objectives. Most of the developing countries, which became politically independent after WWII, shared one very common characteristic- pervasive poverty. This deplorable socio-economic condition indicated that the TW countries lacked appropriate social and economic infrastructures necessary for economic development. Accordingly, the international donor community targeted the economic infrastructures for rural development and helped the 1'W governments to establish para-statal agencies during the late 1950s through the 1970s. More specifically, para-statal agencies were created for providing modern agricultural inputs, including chemical fertilizer, modern irrigation, and improved varieties of rice and wheat seeds, agricultural extension and research, and credit to small farmers. This policy achieved tremendous success, for which the decade of the 1960s used to be described as the golden era of development. In spite of these successes, the problems of poverty persisted, which raised questions about the merits of international aid efforts, and by that, encouraged the international donor community to reverse their aid policies. The agricultural development corporations- created for supplying agricultural inputs- are now being dismantled in many developing countries and their functions are being reassigned to private businesses and the NGOs are being encouraged to serve the credit needs of the poor.

The microfinance literature underlines two basic problems with the para-statal credit programs. The first questions the merits of the state intervention described above. Since the government, not private, agencies were involved with providing these services, the establishment of para-statal credit programs was interpreted as a wrong policy. Second, subsidy is considered as interference in the market mechanism, because it creates inefficiency in both agricultural production and distribution of necessary inputs. Consequently, para-statal financial organizations are accused of distorting the market signals through subsidized operations.

The orthodox donor policies, particularly those concerning rural credit programs in the came under intense criticism during of 1980s. The reasons for these criticisms are often stated quite rhetorically: "They failed to help the poor; failed to ignite the fires of subsidized agricultural development; failed to mobilize rural leakage of scarce poverty reduction resources to non-target groups; and failed to avoid the pitfalls of corruption and moral hazards. The consequence of this litany of failures was disillusionment with government-funded and operated rural credit programs or institutions, and a new-found romanticism in the efficacy of traditional informal rural financial services providers (Remenyi 2000: 29)."

In other words, the microfinance revolution began with the belief that the solution to the poor's credit problems demanded a market-oriented strategy. The emergence of the worldwide microcredit-microfinance movement suggests that the international donor community was successfully convinced to change its policy perspective from disbursing loans to the target groups through public agencies to developing local private financial ventures to serve the poor.

Banking means financial intermediation that involves coordinating the activities of independent savers and borrowers. Banks collect savings from individuals and institutions, and lend the same to others who want them for many reasons, including private profits. Microfinance follows the same principles with two key differences. First, it serves the rural poor who have little access to the financial services provided by conventional banks. Second, it provides a number of services, which are not available from the conventional lending ventures. These services include (i) providing small loans for working capital, (ii) deposit services as an alternative savings option, (iii) insurance against loan default due to misadventure, illness, death etc., (iv) financial services for money management and household financial planning, (v) collateral substitutes such as group guarantees and compulsory savings, (vi) access to repeat and larger loans based on repayment performance, and (vi) advocacy services to bring the poor's need to the attention of national and international policymakers.

Conventional Banks and the Poor

Grameen Bank, the model of the worldwide microcredit-microfinance movement, emerged as a protest against the conventional banking policy of restricted access of the poor to formal financial facilities. To correct this professional bias, a proposition has been made to establish microfinance ventures as an integral part of the developing countries' emerging financial systems. This proposition provokes two questions. First, how does it accommodate the original accusation, i.e., the reason conventional banks are perceived to be prejudiced against the poor? Second, what kind of special knowledge the micro lenders have learnt that would help them overcome the problems conventional bankers face in dealing with the poor`?

The answer to first question is not easy. For, even a superficial survey of the history of international development will reveal that this answer is intimately associated with the age-old laissez-faire doctrine, which has reappeared in the development discourse during the past half century under different names- monetarist counterrevolution, participatory paradigm, neoliberalism, privatisation, structural adjustment etc. However, the main points of the microfinance argument have been well summarized: "The reasons for the failure of modern banking to meet the needs of the poor for financial intermediation services are many, but have been built on prejudice, misconception, lack of motivation, institutional rigidity and ignorance. In essence poor people were perceived in banking and finance circles as a poor market, offering few if any opportunities for `investment', with the implication that there is little opportunity for entrepreneurs in banking and finance to make a profit from `banking with the poor' (Remenyi 2000: 27)."

Remenyi has listed seven factors why these `prejudice, misconception, lack of motivation, institutional rigidity and ignorance' have developed in the conventional banking circle. First, lending to the poor is very risky, because they are unlikely to have business plans and rarely maintain financial records. The poor, who are mostly illiterate, may not have reliable addresses. Second, the transaction costs of making small loans, collecting small regular repayments, or handling small savings deposits and withdrawals are normally very high. Third, the enforcement of contractual financial obligations, which is quite costly, may far exceed the value of loans. Fourth, the poor cannot supply tradable collaterals against which lenders might spread the risks of repayment defaults. Fifth, conventional bankers know very little about the financial markets in which the `economics of survival' plays a major role. Sixth, there are institutional and official biases against informal lending to the poor, which often find expressions in official harassment and attempts to impose unaffordable and excessive regulations. Finally, the conventional financial service providers hold biased opinions against the poor, which are mainly fuelled by misinformation, fear of poverty, and the popular image promulgated in the media that pertains poverty with the unscrupulous, the unreliable and the hopeless `basket case'. The popular perception in the banking circle is that `the world of the poor is an environment of chronic uncertainty, vulnerability to violence, widespread exploitation, an ardent readiness to succumb to opportunities of moral hazard, and fear born of rampant corruption and crime'.

Concerning the second question, microfinance practitioners claim that they have comparative advantages over the conventional bankers in serving the poor 's credit needs. They have already proved that the poor are bankable. In other words, the conventional contention that the poor would break away with loans, and could not be caught, because the loans were collateral-free, has been effectively disproved. Besides this success, two sets of argument have been advanced to show their advantages in meeting the poor's credit need. Firstly, the microtinance organizations have learnt six key lessons by which they can contain costs and reduce risk and to treat their clients as active partners in conducting their businesses: (a) accommodating collateral substitutes as an effective basis for client selection, (b) using selfinterest to manage risk and to maintain near-perfect on-time repayment rates, (c) minimizing the cash costs of making small loans and collecting small savings, (d) mobilizing peer pressure and social mores to enforce contractual obligations, (e) designing and delivering finance `products and services' that meet the needs of the poor, and (f) segmenting the market to keep focussed on the poor, yet targeting the well motivated.

Secondly, the comparative advantages that the micro lenders enjoy over the conventional bankers, can be demonstrated with two criteria- competition and savings mobilization. The micro lenders are more competitive than the conventional banks and other financial institutions, because they are better able to meet the needs of poor households. They can `internalise' transaction costs, for, they have access to better information about community social capital that helps them better assess the integrity of potential clients and `externalise information dissemination to deposit collection transaction costs'. Additionally, the micro lenders can keep default costs down and on-time repayments high, although they take no tangible collaterals to screen and monitor borrowers. Taken together, borrower screening and monitoring constitute the largest share of the operating costs of microfinance organizations.

In the savings mobilization, micro lenders can perform better, because they work closely with poor households and therefore, are more familiar with their clients. Regular contacts make both withdrawals and deposits easier, which conventional banks cannot do, as their branches are located in distant places. "Moreover, there is general understanding among village residents that their voluntary savings with the MPI will be recycled back into their own communities. Banks, on the other hand, do not recycle savings back into the village (Remenyi 2000: 45)."

IV. ECONOMICS OF BANKING OUTPUT

The original accusation, as noted above, is that conventional banks do not provide credit to the poor, because the poor are 'not creditworthy', i.e., they cannot offer collaterals. This seems an oversimplification of the reasons why banks are shy in serving the poor. The bank lending policy- the economics of banking output- is much more complicated than the problem of granting ; loans simply based on collectible collaterals! Then it was an accusation from a very patriotic person who was deeply disturbed by the fact that the poor suffer because they must borrow from exploitative informal lenders due to the lack of their access to formal financial institutions. The banks refuse to give loans to poor arguing that these loans are less likely to be collected and the transaction costs are too high. In the context of Bangladesh, these arguments made little sense for at least two reasons. First, all banks at that time were public property. This means they had responsibilities that the private banks normally did not have. Second, their loan recovery records were dismally poor.

However, the recent microfinance proposition has made the accusation a subject of' curious academic investigation. To contribute to this curiosity, the economics of banking is briefly reviewed below.

Bank is a financial organization that accepts deposits, makes loan, pays checks, and performs related services for the public (Fitch 1990). It primarily acts as a middle person between suppliers of funds and users of funds. Funds are received from three main sourcesdemand deposits, savings and time deposits, short-term borrowing from other banks, and equity capital- which are made available to prospective borrowers.

All banks earn profits by investing their liabilities in different kinds of enterprises and assets. but the commercial banks make profits principally from making loans to prospective businesses and investors.

Financial intermediation is, thus, the bank's main business. To do this business profitably, it conducts credit analysis before extending loans, which involves the assessment of the ability and willingness of a borrower to repay the requested loan in accordance with the terms of the loan contract. "A bank must determine the degree of risks it is willing to assume in each case and the amount of credit that can be prudently extended in view of the risks involved. Moreover if a loan is to be made, it is necessary to determine the conditions and the terms under which it will be granted (Reed et al 1976: 159--160)."

Lending officers take many factors into consideration in analysing loan applications. These factors are normally referred to as the five C's of credit- capacity, character, capital, collateral, and conditions (economic). Capacity to borrow refers to the applicant's legal and economic background showing their ability and willingness to repay the loan, while character refers to their personal attributes such as honesty, integrity, industry and morality. Capital, or the ability to create income, is another important condition in accepting the loan applications. This C of credit depends upon such factors as health, education, skill, age, stability of employment and resourcefulness. Collateral is the asset pledged as a security to ensure payment or performance of an obligation. In bank lending, it is generally something of value owned by the borrower.

Finally, economic conditions are the environment within which business units and individuals operate. "Borrowers can have good character, an apparent ability to create income and substantial assets, but economic conditions may make the extension of credit unwise. It is here that the loan officer must become an economic forecaster (Reed et al 1976: 163)."

The Grameen Bank has developed its own method for assessing loan applications, which it calls the three C's of credit- character, capacity and capital (Grameen Bank 2002). The character of the Grameen Bank member, with respect to further borrowing, shows how they handled their past debt obligations. In other words, the honesty and reliability of repaying further loans are determined from the member's past credit history and personal background. The member's capacity to borrow refers to the amount of credit they will be able to handle comfortably. In this respect, their income situation and legal obligations are taken into consideration. Finally, capital signifies currently available assets, savings and investments, which the Grameen Bank may seize in case the member fails to repay the debt. This last C suggests that the Grameen Bank takes tangible assets into consideration in making out loans to its members, although it does not require, like the conventional banks, the assets to be mortgaged out.

It is, thus, evident that the ability to supply collateral is only one C of credit. The conventional banks are not shy about lending to the poor, just -because they are unable to supply collaterals. There are many other reasons, which diminish the poor's viability as potential bank customers. Moreover, the term, creditworthiness, has become susceptible to criticism, because of way it is interpreted in the microcredit-microfinance literature. This term is formed by combining two words, credit and worthiness. Credit, comes from the Latin word, credito, which means trust or faith, while `worthiness' means deservingness. Therefore, the word, creditworthiness, ordinarily implies the deservingness of faith or trust. This general meaning is also applied in conducting banking businesses. It is a general qualification for borrowing from the bank that the loan officer must somehow be satisfied about the applicant's willingness to repay the loans. In other words, the applicant deserves bank loans only if they appear trustworthy to the loan officer. This is, however, just one criterion that enters conventional banks' selection process to determine their willingness to lend. The other selection criteria, which the bankers take into consideration in this respect, are uncertainty, credit risk and the margin of acceptability (Galbraith 1963).

V. THEORETICAL MERITS OF MICROFINANCE VIEW

The foregoing analysis suggests that the original accusation against the conventional banks carries little credibility: Ability to support one's qualifications with collaterals to obtain bank credit is only one criterion to make out commercial loans. There are many other factors, which the conventional bankers must consider before approving a loan application. Thus, the accusation that the poor are deprived from conventional banking facilities because they cannot supply collaterals is oversimplified. However, arguments offered by the microfinance academia deserve critical evaluation. For, the reasons with which the microcredit programs were promoted in the developing countries are very different from those for which microfinance is being proposed as an integral part of their emerging financial systems.

The microfinance proposition suffers several theoretical difficulties. First, from the commercial banking perspective, microcredit presents two insurmountable problems. In terms of profitability, these loans are too costly and in terms of security, they are tangibly insecure. These features discourage the conventional banks from being involved in the activities popularly known as the banking with the poor. Besides this commercial consideration, there are two other reasons, which might constrain conventional bankers from extending microcredit. Firstly, granting collateral-free loans not only violates the established business principles and practices, but also turns them into discriminatory institutions: If the poor are eligible for collateral-free loans, then, there are little logics for asking collaterals from the rich. Secondly, providing loans to the poor requires a special skill and perhaps a special frame of mind. The micro-entrepreneurs, because of their very situation in the society, need to be discovered and encouraged to explore their creativity. This suggests a kind of social work for which the traditional bankers have neither training nor incentive. The conventional bankers do not normally seek out prospective entrepreneurs; interested individuals submit projects to banks, which are approved if, found satisfactory on critical considerations.

Second, the microfinance theory seems to be founded on value-laden ideas- `prejudice, misconception, lack of motivation, institutional rigidity and ignorance'. These are subjective words with negative value connotations. However, theory in social science, which explains as well as predicts, is developed through objective analysis and explanation of facts and events. Accordingly, the foundation of the microfinance proposition appears deficient in objectivity.

Third, conventional bankers constitute a social group, whose distinguishing feature is that they are involved in financial intermediation as a source of making the means of their living. In general, they are professionals who work for financial institutions- public or private. These people are being characterized with negative words for the business policy they pursue as a matter of professional principles as well as protecting and promoting their institutional interests. This characterization raises two questions. Firstly, conventional bankers manage a social infrastructure that is pivotal to economic growth in capitalism. Therefore, if these people are considered prejudiced against the poor, the whole system of capitalism is to be condemned. Secondly, average bankers are employees of a financial institution. Consequently everything they do are inspired by professional and personal considerations. If loans they grant turn out to be bad debts, their careers will be in jeopardy. Thus, in performing their professional responsibilities, they are not supposed to view the loan applicants as belonging to any particular group; they examine their credentials as potential profitable clients. In other words, bankers examine the credentials of prospective clients mainly for their professional and career concerns.

As noted above, the principles of orthodox economics are held responsible for forming these negative values. This explanation appears problematic. First, the economic prosperity of the North, which has been propelled by the conventional banking system, is due to capitalism. Thus, the accusation that orthodox economic principles are responsible for the developing countries' pervasive problems, cannot be justified. Then the Marxist literature offers a very different explanation about how human motivations are formed. The essence of this explanation may be understood from the following quote that pinpoints Marx's conclusion about his famous social theory, historical materialism: "In the social production which men carry on they enter into definite relations that are indispensable and independent of their will; these relations of production correspond to a definite stage of development of their material powers of production. The sum total of these relations of production constitutes the economic structure of society- the real foundation, on which rise legal and political superstructures and to which correspond definite forms of social consciousness. The mode of production in material life determines the general character the social, political and spiritual processes of life. It is not the consciousness of men that determines their existence, but on the contrary, their social existence determines their consciousness (Marx 1963: 379)."

Fourth, microfinance is currently described as a revolution in the rural finance theorv and policy. This revolution- that involves 'creating customer centred microfinance institutions'- is claimed to have entered into its second phase (Woller 2002). The first phase of the revolution was concerned with `innovations in methodologies' to overcome structural barriers to providing credit and savings facilities to the poor, which include information asymmetries, lack of collateral, high cost, high risk, systematic market bias etc. In other words, the establishment of the microfinance industry in the developing countries is being suggested as an important answer to their pervasive poverty problems.

It is well understood that microfinance is not a panacea, because many other measures need to be undertaken to cure the third world's poverty disease. However, the way the microfinance academia criticizes the para-statal credit agencies, raises a question of consistency in their argument: The para-statal credit institutions are merely lending agencies, which suffer the same kind of infirmity that other government agencies do. Why should, then, these agencies be specially singled out as failing to `ignite the fires of subsidized agricultural development, to mobilize rural resources to the modernization efforts, to bridge the gap between rich and poor, to avoid the pitfalls of corruption and moral hazards'?

Finally, a puzzle exists in the microfinance theory concerning the distinction it makes between conventional bankers and micro lenders (Elahi and Danopoulos 2004). This distinction is founded on the motives of operations of the two groups. The conventional bankers are assumed to be profit-maximizers, while the micro lenders are described as social consciousness-driven capitalist entrepreneurs (Yunus 1998b). The logic is described as follows: In the orthodox economics, private entrepreneurs are assumed to optimize the resource allocation to maximize profit. This assumption ignores any social consideration that some entrepreneurs might have in setting the rates of return on their investments. Thus, an alternative is to assume that entrepreneurs maximize a bundle consisting of two rates of return: (i) financial return or profit and (ii) social return. This axiomatic assumption creates three groups of entrepreneurs. First, there are traditional capitalists who maximize only financial profit. Second, philanthropic organizations, which include the traditional microcredit NGOs, maximize only social return. The third group consists of entrepreneurs who combine the two rates in making their investment decision, i.e., besides private profit motives, they have social considerations in pursuing these financial activities. This group includes the microfinance enterprisers who are to be treated as `socially concerned people' and microfinance is to be treated as a`social consciousness-driven capitalistic enterprise'.

This proposition seems problematic too. It is not clear, intuitively or otherwise, how these social consciousness-driven entrepreneurs are to be identified, unless it is assumed that the stated objectives of the microfinance ventures also reflect the intentions of their owners or organizers. Since national and international public authorities are Supposed to supply funds for helping them start their businesses, the point is critically important for designing international development policies. Then the idea is value sensitive. Those who pursue economic and/or financial enterprises for profits are being characterized as having little social considerations- a proposition that is inconsistent with the economic system of the non-communist state, capitalism. If capitalism does not serve social purposes, then it cannot be the economic system of the democratic system, currently considered the fairest political theory of civil society. Here, it should be noted that microfinance itself is a capitalistic enterprise. Lastly, the proposition is irrational in characterizing individuals. Suppose, after graduating from college, a young woman chooses to pursue a banking career. Very luckily, she gets two lucrative offers- one from a commercial bank and the other from a microfinance firm. If she accepts the offer from the microfinance firm, she will be lauded as a socially concerned person. If she chooses otherwise, she will be seen as having little social considerations. Yet, both are private undertakings and have profit making as their ultimate motive.

VI. CONCLUSION

The main objective of this paper was to examine the overwhelming accusation that the conventional banks in the TW countries are prejudiced against the poor, particularly the poor women. This accusation, which originally came from Mohammad Yunus, the founder of the famous Grameen Bank, appears less than satisfactory on critical examination. But, academically most curious aspect of this investigation concerns the controversy that the recent microfinance literature has created by vindicating his theory. The foregoing analysis suggests the microfinance proposition, which recommends for an overwhelming transformation of the microcredit movement, is founded on questionable conceptual premises.

However, it may be underlined that the justification of microcredit programs hardly depends upon the role of commercial banks in the economy, simply because they have completely different mandate and motivation. Microcredit is an NGO, meaning that it has no profit motive. The commercial bank, on the other hand, is a private business venture that runs with profit motive. Naturally, commercial banks serve those who appear profitable to them, while NGOs have evolved to serve those who cannot qualify for services from the commercial backs. Therefore, given the mandate and motivation, microcredit programs and commercial banks have little conflict. But, this logic cannot be extended to microfinance ventures, because they have characteristics similar to those of commercial banks.

REFERENCES

Adams, D. W., Graham, D. H. and Pischke, J. D. V. (1984).*'Undermining Rural Development with Cheap Credit*. Boulder: Westview Press.

Elahi, K. Q. and Danopoulos, C. (2004). "Microfinance and the Third World Development- A supply-Side Analysis". *Journal of Political and Military Sociology*, 32(1).

Fitch, T. (1990). *Dictionary of Banking Terms*. New York: Barron's.

Galbraith, J. A. (1963). *The Economics of Banking Operations*. Montreal: McGill University Press.

Grameen Bank (2005). "The official website of Grameen bank," http://www.grameen-info.org/

Hulme, D. and Mosley, P. (ed) (1996). *Famine against Poverty*- Volume 1. London: Routledge.

Korten, D. (1987). "Third Generation NGO Strategies: A Key to People-Centred Development" *World Development* 15 (Supplement): 145-160.

Ledgerwood, J. (1999). *Sustainable Banking with the Poor: Microfinance Handbook- An Institutional and Financial Perspective.* Washington D.C.: The World Bank.

Marx, K. (1963). "Contribution to the Critique of Political Economy", in J. Somerville and R. Santoni (eds), *Social and Political Philosophy.* New York: Anchor Books, Doubleday & Company, Inc.

Reed, E. W. et. al. (1976) *Commercial Banking*, New Jersey: Prentice-Hall Inc.

Remenyi, J. (2000). "Is there a 'State of the Art' in Microfinance?" in J. Remenyi and B. Quinones Jr. (eds), *Microfinance and Poverty Alleviation- Case Studies from Asia and the Pacific.* London: Printer.

Woller, Gary (2002). "Introduction,"*Journal of International Development*, 14 (3).

Woller, Gary and Warner Woodworth (2001). "Microcredit: A Grassroots Policy for International Development," in D. Snow, G. Woller and T. Buss (eds), *Microcredit and Development Policy.* Huntington, New York: Nova Science Publishers Inc.

Yunus, M. (1996). "The Empowerment of the Poor," An address to The State of the World Forum, San Francisco, October.

Yunus, M. (1998a). "Towards a Poverty Free World," A paper presented to the joint conference of the International Economic Association and the Bangladesh Economic association, Dhaka, April.

Yunus, M. (1998b). "Poverty Alleviation: Is Economics Any Help? Lessons from the Grameen Bank Experience," *Journal of International Affairs*, 52 (2).