MFI's clients borrowing strategies and lending groups financial heterogeneity under progressive lending: Evidence from rural Mexico

- **OBJECTIVE:** Do borrowers necessarily borrow the maximum amount they are allowed along credit replications?
- **THEORETICAL BACKGROUND:** Economic theories generally assume that borrowers of microfinance institutions are credit constrained

Dynamic incentives according to which borrowers repay their loan in order to access a larger loan may be powerful

- **CONTEXT:** Remote rural villages in southern Mexico- Oaxaca State- attended by a Microfinance Institution. Borrowers are mainly coffee producers
- **METHODOLOGY:**
  - Data: 1462 individual loan observations covering the borrowing history of 91 lending groups living in villages attended by two rural branches
  - Completed by 135 individual (borrowers) interviews

**Step 1:** Statistical comparison of amount borrowed relative to amount that such microfinance institution is willing to lend to borrowers (according to credit cycle, repayment performances of previous loans).

**Step 2:** Look at potential facts that could explain why borrowers are unwilling to obtain the maximum amount of loans that they could possibly obtain.

**Step 3:** Assess borrowing strategies among borrowers of same group lending along credit replication (analysis of a variable we construct that represents the difference between the highest loan amount in the group and the real amount borrowed by each group member)

**MAIN FINDINGS**

Individual level: Along credit replications borrowers tend to request loans that are small relative to those that such MFI is willing to lend to them

- **First credit cycle:** neither the t test nor the confidence interval could reject the null hypothesis that there is a significant difference between the borrowed amount and the amount that the MFI is willing to lend to borrowers
- **Following credit cycles:** the t test significance statistic becomes lower and the confidence interval increases and so does the mean level of the two variables.

- **Control for potential influences on amounts borrowed**

1) Borrowers are not characterized by a large set of projects to finance and are not systematically interested in larger loan amounts. Because of economic difficulties in daily life and low level of income-generating activities opportunities, loans are used to meet daily expenses - rather than for income-generating activities

2) No negative influence of access to any other liquidity sources or coffee prices negative evolution on borrowed amounts

- **Group level:** Increasing heterogeneity among borrowers along credit replications

- Along credit replication, lending groups experience varied borrowing strategies among borrowers, increasing heterogeneity among groups' borrowers from financial needs criteria:

- **Moreover we observe**

  Even "homogeneous groups" experience varied borrowing strategies but financial needs heterogeneity is managed with intra-group renegotiations such as

1) intra-group loans:

- 2) or temporary exit: although attrition rate is quite low: less than 6% per year we observe that some borrowers stop borrowing and borrow again one credit cycle later

- **CONCLUSION**

  Progressive lending scheme is too rigid: borrowers are unwilling to borrow larger amounts along credit replication + groups' members financial needs are heterogeneous thus groups adopt strategies to better adapt MFI's offer to heterogeneous financial needs among borrowers.

  MFFs would have to better adapt lending technology

- Better adjustment would require loan offices to collect more data to analyse client loan-repayment capacity rather than relying on peer group recommendations to determine amounts to lend (Meyer, 2002)
- Repeated loan access is a better repayment incentive (see low attrition rate)
- Group lending financial heterogeneity (different borrowing strategies) can be a source of problems for joint-liability
- Intra-group renegotiations to manage financial needs heterogeneity represents a new source of information asymmetries (moral hazard) for the MFI
- Borrowers have difficulties to understand that they are not obliged to borrow each credit cycle But this questions the commitment to joint-liability with mutual guarantee.