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Self-fulfilling prophecy?

In a set of recent interviews with microfinance institutions in the Philippines, we discussed the challenges faced by organizations offering agricultural microloans. One non-profit we spoke with is having particular difficulty, with portfolio at risk over 30% and default at 25%.

This particular organization noted that one of the challenges it faces is that its clients have seen many government programs and NGOs come and go, and they feel little confidence in the longevity of the microloan program. So far, so good. But when asked what they were doing to address this challenge, the organization said that they will continue providing loans and services, even if farmers don’t repay, to build consumer confidence and send the message that they are there to serve in the long run.

On the one hand, the insight that the short-lived nature of anti-poverty programs will lead to a lack of mutual accountability between clients and service providers seems spot on. If small farmers or entrepreneurs suspect that their current lender will move on and a new one will take its place in a few years, they may correctly surmise that the penalties for late or non-payment are low. Most lenders will give them some slack in the short run by accepting late payment or restructuring loans, and by the time they have used up their wiggle room, the slate will be wiped clean by the change in service providers. In the absence of any national credit data – or even information sharing between lenders – how would a new lender know if they have a bad credit history?

On the other hand, responding to a lack of consumer confidence by not enforcing penalties for late payment seems like a self-fulfilling prophecy. Surely showing lenders that they *don’t* have to repay in order to get another loan isn’t the way to decrease delinquency?

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