1 Social Ties and Microfinance

Predictions for Group Lending

On a cool morning in a midsized village in rural China, I sat with a thirty-six-year-old woman surnamed Lu in the courtyard of her home, which had been built with help from other members of the village, using a rammed-earth technique. She brought out two tiny stools for us to sit on while we spoke. Lu told me matter-of-factly about how the microfinance loan she had gotten (and repaid) was both good and bad. She wasn't sure; she didn't care that much. She had been initially glad to receive the money but found the interest she had to pay a burden. The tiny loan didn't help her with a profit-making enterprise but ended up decreasing her assets overall:

> I repaid by selling my chickens. The loans are good and bad, I guess. It wasn't really very good for us, actually. I didn't do anything with the money, and then I had to pay interest . . . When we had the loans, my sons were small, so I had no extra time to try to do something new. I just used the money for daily purposes or whatever (*suibian yong*).
>
> *(June 8, 10 a.m., field notes)*

Lu's experience confounds the expectation that a microloan leads to increased profit for the borrower. And her response was not unique. Borrowers' reports to me of their experiences with microfinance did not have the characteristics of people empowered. A better description would be indifferent or irritated. Lu didn't know what to call it. Good and bad, she guessed. But not really very good for her, actually.

Ordinary villagers had difficulty repaying the 1,000 RMB ($125) loans, because the mandatory repayment of 60 RMB ($7.50) every two weeks was troublesome. It did not allow for adequate time to make profits from raising livestock (a common venture for the area), since the more profitable animals took months to raise before they could be sold. Social inequality also complicated the program; the influential villagers (those with the most resources and power already) received bigger loans with more flexible repayment schedules. Still they were not making much in profits either. There just are not many options for new enterprises in the villages.

In addition to being practically unhelpful, the program also had what was to Lu an unnecessary and burdensome requirement for borrowers to meet together, according to schedule, as small groups in the village. The meetings had actually been mandated with the goal of increasing the flow of information among borrowers, but in the village, information already traveled as quickly as lightning. The people in her group were her friends and relatives, whom she had lived and worked alongside for many years – they already talked about the loans, and everything else. Even if she had realized that program designers were expecting her to pressure other borrowers to repay their loans (so that the lender would save some of the resources normally spent on monitoring and sanctioning), she would think it a strange presumption. It was not likely she would want to explicitly find fault with a fellow borrower in the village and risk setting off a series of negative reverberations in her own network of social relationships.

According to the microfinance literature, borrowers make profits, people have to be persuaded to repay their loans, and borrowers readily sanction their neighbors when sufficiently incentivized. What I observed ran contrary to these expectations: the borrowers were not making money; rather than needing incentives to repay, most (or all) borrowers repaid, but not because of sanctions; and borrowers simply were not sanctioning each other.

CULTURE AND MICROFINANCE

This book is about what people did with microfinance.

Borrowing Together is a study of what happened in a field site in rural China when there were attempts to have people borrow money, then repay it "together" (using social collateral, pledging their popularity, so to speak, as security for the loan) for the purpose of alleviating their poverty and boosting economic development in their communities. Microcredit, so named for its very small loan amounts, is the best-known type of microfinance and was first launched in China in the 1980s by the United Nations within a larger context of global trends. These loans are granted to very poor people. Although there are many variations, the basic model, made famous by the Grameen Bank, is that the borrower puts the money toward some kind of profitable activity (for example, she buys a sewing machine to set up a tailoring business), keeps most of the profit generated, and uses the rest to repay the loan plus a modest interest. This is thought to both empower borrowers and make them more resourceful, since it demonstrates more respect than a handout. Borrowers get financial rewards (more loans) if all the others in their local group also repay their loans, so people are expected to engage in peer sanctioning to get the loans repaid. It was once a favored solution for those trying to solve the problem of poverty in rural areas but has since led to disappointing results.

When I began the fieldwork in 2004, microfinance was approaching the peak of its popularity, prominent academics were constructing models of why group lending would work, and I was as optimistic as everyone else about microlending's potential. But not long after arriving in the field, I found that what the borrowers were telling me, what the repayment account books indicated, what the staff remarked, and what I observed didn't make sense according to the models – no matter how much I wanted it all to come together neatly. What I saw and what I had read in the books were like ships passing in the night – they seemed to have missed each other completely.

I thought at first that the specificities of the field had "messed up the plan," so I went into problem-solving mode, focusing on the people and issues I thought were gumming up the works. If we were to eliminate the "mess" – the relationships between people, the status differences, the personal histories, the dependencies people had on one another, the friendships, the disagreements between neighbors, the fact that people were significantly more interested in survival than investment – then we could free up the model to work as intended.

Over time, however, I realized that this way of thinking was the very problem with the models. What I was considering peripheral – pesky exceptions to how microfinance should run – were actually *the* decisive factors in the microfinance program. This meant that I had to figure out what people were doing and why. How did they get through life's difficulties? What did they consider admirable and decent? What made them angry, embarrassed, or ashamed, and what did they expect of one another? It was clear that the repayment or default of their loans pivoted on these things. As a sociologist of religion, I was interested in how microfinance intersected with the moral world in which villagers live their lives.[1]

I also began to wonder what, specifically, might be wrong with the microlending models, and *why* there was a conspicuous absence of real people (with feelings and histories and relationships and dependencies) within them. In order to answer this question, I had to investigate the cultural aspects of microfinance itself – that is, what is considered normal, the widely conceded assumptions about reality that form the backdrop of microfinance and upon which its design decisions are based. The more that things were taken as "obvious" or "universally true" – such as the expectation that borrowers are unlikely to repay a loan unless incentivized by the program – the more likely it was that such an assumption would be evidence of culture.

This book is therefore also about culture.

Specifically, it is about how the *person* is conceptualized.[2] More specifically, how are microfinance borrowers (as persons) visualized in group-lending programs – by donors, by development personnel, by themselves? And what are the consequences of these conceptual associations for the repayment of loans, the sanctioning of peers, and the well-being of borrowers? My analytical approach begins with treating the person not as a naturally given entity, but rather as a historically constructed (and possibly problematic) category.[3] Notions of what a person is have, in fact, varied a great deal across times and places.[4] In this book, I focus on the conceptual construction of the person in microfinance, and I look to see how well it predicts the actions of the borrowers in my field site.[5]

So the present exercise not only looks closely at what transpired in the course of a microfinance intervention, it also reverses the gaze to examine the expectations that brought the program to the site in the first place. It investigates the details of the social relationships among fellow borrowers and between borrowers and lenders, finding that these relationships, contrary to existing microfinance theories, are the key that explains the outcomes.

I suggest an explanation of microfinance based on pragmatist theory, which is uniquely able to comprehend the commonsensical Chinese concept of *guanxi*. In doing so, I present an alternative perspective to that which has ruled the day; I focus on how people relate *through* money *to* each other, and not the other way around.[6] *Guanxi* means "relationships" or "social connections," and this mysterious complication, hidden in plain sight, can deflate microfinance plans that depend upon a prescription of whom participants monitor, repay, pressure, and punish. Although *guanxi* is neither a confessed belief nor an allegiance to a faith or god, and it requires no participation or membership in an organized religious institution, it reflects real and important ideas about the way many people make sense of life. It is the context in which people deal with life's biggest moments (like birth and death). *Guanxi* encompasses a point of view that is the basis of moral decisions and everyday judgments about right and wrong, good and bad. A consideration of *guanxi* can shed light on the question of why microfinance models often prove to be limited in its predictions about its borrowers.

That microloans are not turning out as expected is not news. The innovation of group responsibility appealed to donor sentiments, and the apparent no-cost collateral of social pressure appealed to lenders. Optimism was high from the late 1990s to the mid-2000s. It peaked in the late 2000s and then began to plummet approaching 2010. The microcredit climate remains cool today.[7]

Some of the more devastating critiques of past microcredit efforts accuse lenders of actual harm to the already disenfranchised. Some have shown that, in a drive to produce high repayment rates, the Grameen Bank and other microfinance organizations in Bangladesh appropriated honor-and-shame language against women borrowers – making them an object of oppression.[8] Suicides by borrowers in India caused the government in Andhra Pradesh to all but shut down the microfinance industry in 2010 (writing off almost all microfinance loans and issuing strict regulations).[9]

Activity in microfinance, however, has lately been revived, as industry experts have become more careful about profit incentives for lenders and more thoughtful about outsized dreams of mass entrepreneurship. Even so, studies have shown, people are using the cash influxes to smooth out income fluctuations and ensure sufficient daily food and other basic requirements. Microfinance, therefore, is still falling short of its goal to make poor people economically self-sufficient. It instead enters the mix of wages, semiformal or formal loans, and savings and borrowings from family and friends – all funding sources being used to pay for necessities and to weather life's storms.[10]

The number of people living in China on two dollars (or less) a day is approximately 400 million, and approximately 130 million of them live on no more than one dollar a day.[11] Most of them live in rural areas, which do not get the press coverage of the rapidly developing cities. The numbers alone justify close examination of poverty-alleviation efforts in rural China. In addition, this case is also applicable around the globe. People in China live within a power structure where personal ties are both consequential and negotiated, and they practice traditions that feature family and an extended community, including ancestors. This places them in good company with a good portion of the world.[12]

As the title of the book suggests, people cultivate their social ties in microfinance programs. This book is not about how microfinance can change people's lives, but rather, how microfinance is incorporated by people into their networks of social relationships.

CULTIVATING SOCIAL TIES: A PRAGMATIST THEORY OF MICROFINANCE

In group lending, borrowers are expected to repay if they have financial incentive, and predicted to sanction defaulters in pursuit of these financial incentives. Drawing on John Dewey's essay, "The Moral Self," I build an alternative theory of microfinance that takes social relationships into account.[13] Taking a pragmatic turn would mean that we expect repayment instead to depend on what it does to one's *relationships* (does it improve one's ties?) and what it does to the *self* (is one being a good neighbor?). Three contrasting predictions about how borrowers repay and sanction in microfinance are covered below.

1. Borrowers repay when repayment strengthens important social connections. To understand group lending, the question to ask is how microfinance intersects with a borrower's web of relationships.[14] In rural China, people consciously orient their lives around their relationships (*guanxi*). People's *guanxi*, the social relationships they have cultivated and the networks they are embedded in, define who they are.[15] Social life is therefore not based on agreements and contracts between preexisting entities, but instead, those entities are defined and shaped by the relations between them. We cannot envision "interests" as "the adjustments of isolated selves," Dewey wrote, where "social arrangements were considered to be secondary and artificial."[16]

Social ties (*guanxi*) involve both material obligation and "human feeling" (*renqing*) toward other human beings.[17] Anthropologist Yunxiang Yan writes that *guanxi* constitutes "a total social phenomenon" in the sense that it "provides one with a social space that at once incorporates economic, political, social, and recreational activities."[18] Someone who is good at *guanxi* is someone to be admired. It is a mix of admiration that the person has created and maintained such relationships by treating her friends and family right, but also that she is able to organize it all to the benefit of herself and others, too.[19]

A borrower therefore asks, which of my social ties (*guanxi*) will be affected by my repayment or default?[20] To predict microfinance outcomes, we need to examine the relationships that the borrowing and lending involve. Are there status differences? If the microfinance repayment or default decision touches upon relationships where there are status differences, people will do what they need to do in order to strengthen those connections. Repayment and default will depend on what kind of relationship (*guanxi*) is involved, as well as what kind of relationship the borrower would like to have.

2. Borrowers repay when repaying makes one a good person. Dewey argues that "action manifests and forms the self."[21] Instead of assuming that borrowers are always looking for ways to default, a pragmatist theory of microfinance predicts that the likelihood of default depends on whom the money is going to and what kind of person the action of repaying makes them. Relationships (*guanxi*) are central to the *kind of person* one is. A good son, a good person, takes care of his parents.[22] A good life includes good relationships (good *guanxi*) with parents and children as well as friends and neighbors.

People aim to be the kind of person they want to *become* as they go about their activities and cultivate their relationships. Since every human choice pertains to a future self, "in choosing this object rather than that," Dewey wrote, "one is in reality choosing what kind of person or self one is going to be."[23] There is no such thing as a "fixed, ready-made, finished self"; instead, one's actions determine the person one becomes.[24] Doing good deeds doesn't *reflect* goodness that is within; by doing good, you create yourself as good person.

Whether the borrower feels that people see him as a decent person is part of how he sees himself, and it can happen instantaneously, like seeing a reflection in a mirror. If defaulting has little bearing on whether the borrower feels like a good person, he or she is more likely to default. However, if defaulting means violating a bond of reciprocity and mutual aid between two people, ignoring the emotional attachment that has been generated (perhaps over the span of many years), and not understanding the importance of obligation and indebtedness, then borrowers are unlikely to default.[25]

3. Borrowers avoid sanctioning peers when embarrassing someone incurs a moral cost. *Being* a person is thought of as *becoming* oneself in pragmatist theory. People wonder as they deliberate whether to embarrass or punish someone, *what kind of person would I become if I did that*? People don't like to feel embarrassed, so a tactful and decent person will avoid placing others in this position. A good person refrains from embarrassing people and helps others save face.[26]

People see their lives as interwoven with others, as their shared experiences and their shared past define who they are. In this way, their identity is situated in the latticework of social relationships that constitutes their person. Every act reinforces or diminishes one's social relationships. Since helping people save face is an important part of cultivating good relationships (*guanxi*), it is unlikely that borrowers in rural China sanction each other easily. People's webs of relationships are powerful and longstanding, but also susceptible to injury. In the "giving" and "acquiring" of face and favor, the ongoing reciprocal exchange is central to the moral ordering of relationships, and therefore one's self as a person.[27] If the loan is considered a relatively trivial matter, those who pressure one another about it would be seen as unreasonable or unkind. Someone who seriously considers the reasonableness of sanctioning in the context of *guanxi* would not be quick to predict success for a social-collateral model based on sanctions.

MICROFINANCE AND SOCIAL RELATIONSHIPS

One of the reasons microfinance captivated the attention of donors was its use of "free" collateral: They were excited about having borrowers use social relationships in the service of gaining money and assets. Three axioms of group-lending microfinance are that financial incentives predict repayment; that repayment is not likely, so incentives must be provided via the imposition of interdependency; and that sanctions are costless to apply. These accepted truths have never been questioned.[28]

Borrowing Together reveals that the outcome of microfinance can depend not only on the financial terms of the loans but also how people incorporate microfinance into their existing social relationships (*guanxi*). Repayment and default then become offshoots of the existing ties; this contradicts the expectations that participants would use their social relationships to acquire more loans. Relying on five types of data gathered over three years – "go-alongs" to distribute and collect cash in the villages, interviews, ethnographic observation, microfinance repayment records, and internal reports of the third-sector organization – this book details intriguing outcomes in repayment and peer pressure.

The Grameen Bank's famed group lending model of microfinance describes a means for achieving poverty alleviation and economic development. Does this recipe, cultivated by the organization, its supporters, and academic writing, correspond with the realities for borrowers in the field site in rural China?[29] The recipe is as follows:

Small Loan + Poor Individuals + Group Repayment Incentive =
Self-Regenerating Entrepreneurship

There were two microcredit programs in the field site I observed in rural China, both of which provided small loans to poor individuals with some type of group repayment incentive.

The Grameen replicator was fashioned after the Grameen model (with villagers grouped together in small groups, interest paid early and often, and no more loans disbursed when the larger group fails to repay in full). It was carried out by the Chinese government. Ordinary (noninfluential) villagers indicated that the repayment schedule of the Grameen replicator was not suitable and that the funds they received were not particularly useful for poverty alleviation, *yet* they repaid on time, scraping together the cash even when unable to make a profit (which was most of the time).

The other microfinance program was developed by a third-sector organization that I'll refer to as Global Hope (GH).[30] It had an altered model (as I'll explain) with the intention of fitting better into the realities of village interactions. Rather than needing to be