Group versus Individual Liability: Long Term Evidence from Philippine Microcredit Lending Groups

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Abstract

Group liability in microcredit purports to improve repayment rates through peer screening, monitoring, and enforcement. However, it may create excessive pressure, and discourage reliable clients from borrowing. Two randomized trials tested the overall effect, as well as specific mechanisms. The first removed group liability from pre-existing groups and the second randomly assigned villages to either group or individual liability loans. In both, groups still held weekly meetings. We find no increase in default and larger groups after three years in pre-existing areas, and no change in default but fewer groups created after two years in the expansion areas.

Gender Connection | Gender Focused Intervention
Gender Outcomes | Women’s access to credit
IE Design | Clustered Randomized Control Trial (Clustered at microfinance center level)

Intervention

Group liability in microcredit purports to improve repayment rates through peer screening, monitoring, and enforcement. However, it may create excessive pressure, and discourage reliable clients from borrowing. Two randomized trials tested the overall effect, as well as specific mechanisms. In the trial, half of a microfinance bank’s existing group-lending centers were randomly converted to individual liability. In the second trial, the bank expanded into new areas. Villages were randomly assigned to be either group liability centers, individual liability centers, or centers that would phase-in individual liability. Note that all loans are given to women.

Intervention Period | 2004-2008
Sample population | In the first study, the sample includes 169 microfinance centers handled by 11 credit officers in 6 branches. In trial 2, the bank opened 124 centers, 43 with group liability, 41 with individual liability and 40 with phased-in liability. 3285 clients were active borrowers before the experiment started.
Comparison conditions | The first study compares people who continue to have group lending to borrowers who switch from group to individual lending. The second study compares new borrowers from centers that only have group, individual or individual-phase-in lending.
Unit of analysis | Borrower Level
<table>
<thead>
<tr>
<th><strong>Evaluation Period</strong></th>
<th>2004-2008</th>
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<tbody>
<tr>
<td><strong>Results</strong></td>
<td>The first trial finds no change in repayment rates for centers converted to individual liability. There is also higher client growth and less monitoring of each others loans. Those with weaker social networks prior to the conversion are more likely to experience default problems after the conversion to individual reliability. In the second trial, there were no statistically significant differences between the repayment rates across any of the three groups. Credit officers were less likely to create groups under individual liability.</td>
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<td><strong>Primary study limitations</strong></td>
<td>The elimination of group-based contracts got rid of the contract structure, but the social norms around the contract may have remained in tact.</td>
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<tr>
<td><strong>Funding Source</strong></td>
<td>World Bank Research Committee, The national Science Foundation CAREER SES-0547898, Bill and Melinda Gates Foundation Financial Access Initiative</td>
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<td><strong>Microdata</strong></td>
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