Chapter 3

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THE COVID-19 CRISIS AS AN OPPORTUNITY TO BREAK WITH THE FAILING GLOBAL MICROCREDIT INDUSTRY

The Covid-19 crisis is putting the future of the global microcredit industry at serious risk. Among other factors, this is because the poor are increasingly unable to repay the large volumes of microcredit that they have accessed in recent years. Since the international development community believes that the microcredit model has made a hugely positive impact in addressing poverty and can do so going forward, the global microcredit industry has begun to receive significant financial support in order to continue to operate. However, with even mainstream economists now accepting that the microcredit model has in fact failed to address global poverty, this article argues that these emerging bailout efforts will amount to nothing more than "throwing good money after bad." There is now an opportunity to plot a new trajectory towards community-owned and controlled local financial institutions. Economic history shows that these alternatives have a vastly better track record of addressing poverty, economic development and inequality, as well as usefully promoting greater democracy and participation in society. I illustrate my argument by pointing

to just one of the several appropriate models for all to learn from and adapt to the current Covid-19 crisis conditions: the New Deal reconstruction of the rural financial system in the US that arose as a response to the Great Depression. If the Covid-19 crisis is to be successfully addressed in the Global South, a similarly radical all-encompassing approach to the restructuring of local financial systems urgently needs to take centre stage.

INTRODUCTION

The microcredit model is a financial innovation that, since the 1980s, has been widely promoted in the Global South to combat rising poverty, joblessness, inequality and gender disempowerment. Defined as tiny loans – microloans – that are used to establish or expand an informal microenterprise or self-employment venture, the mainstream belief since the 1980s is that microcredit has been very successful in its assigned mission. However, the Covid-19 crisis has now created an unprecedented worldwide crisis, and the global microcredit industry is likely to be one of its many institutional victims. The incomes of the global poor are in free fall right across the Global South. The poor will likely be unable, and perhaps also unwilling, to repay the very large quantity of microcredit they have racked up with the world's microcredit institutions (hereafter MCIs).[1] As a result, many MCIs have been quickly plunged into serious difficulty. Accordingly, rescuing the global microcredit industry has become one of the paramount objectives of the international development community as it responds to the rapidly deteriorating situation in the Global South. Financial and other forms of support are already arriving not only to assist many of world's MCIs directly, but also to support the commercial banks and global investors that

[1] As of 2018, it was estimated that the volume of microcredit debt held by formal MCIs was around $US124 billion spread over 140 million borrowers (Microfinance Barometer 2019).

finance their operations. If, as is now expected, the Covid-19 crisis extends well beyond 2020, considerably more financial support is also to be expected. If all goes according to plan, the vitally important global microcredit industry will be saved from collapse. It will then be able to play a central role in helping the poor cope for the duration of the Covid-19 crisis, and then in rebuilding their lives and communities in its long aftermath.

The entire effort to rescue the global microcredit industry is based on the unshakeable belief that microcredit has been a very successful anti-poverty intervention to date. It therefore seems entirely logical in these difficult times to want to continue to provide microcredit to the global poor. Summing up this very widely held feeling was the UK's *Economist* magazine, which proclaimed "nursing the (microcredit) industry back to health will give a big bang for the buck" (Economist 2020a). It also follows that there is no sense in making any major changes to the structure and operations of the global microcredit industry. Why tinker with what is widely believed to be a winning formula?

But what if the long-standing belief in the power and impact of microcredit is misplaced, and microcredit, in fact, doesn't actually work? This would undermine the rationale for wanting to rescue the global microcredit industry. Sadly, this is indeed the sour reality that has emerged in recent years. Today, even one-time leading microcredit advocates now accept that microcredit has essentially had zero impact on global poverty. Even worse, a growing number of economists working in the heterodox tradition have demonstrated that the microcredit model has quite seriously frustrated the fight against poverty in the Global South. Rescuing the global microcredit industry today is, therefore, not a straightforward issue at all. Bailing out a major financial institution that has actually failed in its assigned mission to date would surely be the textbook definition of "throwing good money after bad."

In the context of the most serious economic and social calamity since the Great Depression, I argue that propping up the existing

global microcredit industry is the very worst way to assist the global poor. What is urgently needed instead is a radical new approach to local finance. This approach involves an effort to begin to rebuild local finance in the Global South through the programmed conversion of historically ineffective and now-failing MCIs into a variety of community-owned and controlled financial institutions. Specifically, I argue for the conversion of MCIs into one of three formats: credit unions, financial cooperatives or community development banks (CBDs). Unlike in the case of microcredit, these three local financial institutions have amassed a very impressive track record of successfully addressing poverty and promoting sustainable and equitable development everywhere in the world. Importantly, this success has very often been achieved against a background of economic and social crisis not dissimilar to the current situation. A key reason for this historic success is because of the aim of such community-owned and controlled financial institutions. Rather than operating to *extract* wealth from the community to be enjoyed by a narrow financial elite (one that is increasingly located abroad in "tax-efficient" or low-regulation jurisdictions),[2] most community-owned and controlled financial institutions exist to *recycle* wealth back into the community to be used and invested by successive generations. In addition, being built on principles of democracy and participation, it is important to note that community-owned and controlled financial institutions have historically played an important role in consolidating and extending democracy into the wider fabric of the local community.

In very practical terms, I would argue that we should look for practical inspiration to the great US President, Franklin D. Roosevelt. In the context of the devastation of the Great Depression, Roosevelt saw the enormous damage being inflicted upon America's rural poor and he understood that the only way to really assist them into the

[2] In Cambodia's large and hugely profitable microcredit sector, for instance, all of the top ten MCIs are now either fully or mainly owned by wealthy foreign banks, investment bodies and the international development agencies (Bateman 2020).

longer term was to restructure the rural financial system almost entirely. Accordingly, beginning in 1933, the Roosevelt administration put into place a new farmer-owned and managed rural financial system. This not only proved successful in quickly addressing poverty in the large number of rural communities left devastated by the Great Depression; it also went on to play a major role in creating an efficient agricultural system in the USA. If the Covid-19 crisis is to be effectively addressed in the Global South today, then an equally bold move should be a priority of the very highest order.

ADDRESSING THE "COLD TURKEY" PROBLEM

Quite clearly it is not feasible to do nothing and allow the global microcredit industry to crash. Forcing the global poor to have their current access to microcredit immediately cut off – for poor communities to go "cold turkey" – would in the short term inflict serious damage. For example, many millions of informal microenterprises and self-employment ventures engaged in simple trading activities would encounter real problems without a daily source of working capital with which to restock their tiny businesses. This is what Michael Schlein, the CEO of one of the world's most influential microcredit advocacy and investment bodies, the Boston-based ACCION, is referring to when warning that, "The financial engine for half the world's jobs will… seize up" if the microcredit sector is allowed to collapse (quoted in the Economist 2020b). Moreover, an immediate absence of microcredit would inflict pain on those using microcredit simply to try to cope with the effects of poverty, many of whom were struggling even before the Covid-19 crisis. Further restricting the ability of the poor to purchase healthcare services, medicine and personal protective equipment (PPE), could also quickly become a life-or-death issue.

In the early stages of the Covid-19 crisis (April-May 2020), people realized that a whole host of financial support measures were ur-

gently needed to allow the global microcredit industry to continue to function (Carstens 2020, Ogden and Bull 2020, Rozas 2020, Zetterli 2020). Leading microcredit advocates Liebermann and DiLeo (2020) were fairly typical in what they advocated: repayment holidays of up to 90 days, emergency funds to inject liquidity into MCIs and to take bad loans off the books, government and international donor bailouts to protect the largest MCIs, and measures to protect global investors. Importantly, Liebermann and DiLeo saw nothing fundamentally wrong with the global microcredit industry that might be usefully addressed through the application of the rescue package they were advocating.

By June-July 2020, however, it became clear that the Covid-19 crisis was not going to be over in a short time period but was likely to deepen and extend much further into the future. This deteriorating situation was reflected in the growing number of reports of delayed repayments, savings accounts being depleted fast, outright defaults beginning to grow, and investors starting to run for cover. To preserve their own liquidity, many MCIs also began to avoid further lending, while pushing and even threatening clients to continue to repay their microloans regardless of the huge problems they were now facing. In India, for example, many MCIs were found to be ignoring pleas for a moratorium on repayment and were instead demanding that clients, especially women clients, continue to repay (Guérin *et al.* 2020). A similar situation was reported in Pakistan (Rhyne 2020). Many other MCIs accepted a three-month or more repayment holiday, but simply rolled up the missed interest and capital payments into a larger microloan that has to be fully repaid when the Covid-19 crisis eases (Joseph *et al.* 2020).

At time of writing (August 2020), it is now clear that the global microcredit industry is facing a potential catastrophe. The debate within the international development community has therefore shifted away from introducing temporary support measures towards a discussion of the design of financial bailout programs that would be large enough to ensure a significant part of the current

global microcredit infrastructure remains intact. Still, however, there has been no real debate as to whether a fundamental *restructuring* of the global microcredit industry itself is also required as a way of better dealing with the unprecedented threat that the Covid-19 crisis represents to the global poor.[3]

ADDRESSING THE "ELEPHANT IN THE ROOM" PROBLEM

As with any financial transaction, before using scarce funds to revive the microcredit model, it would seem sensible to do all the necessary due diligence. In other words, we must be absolutely convinced that microcredit has really worked in the past so that we can be confident that it will work going forward to help those negatively affected by the Covid-19 crisis. It is especially important to be certain that microcredit will do no harm. It would also help if we had an idea of what the alternatives to "more microcredit" are and if supporting them might not be a better strategy.

We are therefore presented with a very serious dilemma: in practice, the microcredit model has *not* worked to date in the manner it is supposed to have done, *so it cannot therefore be concluded that it will work going forward*. Given the almost universal celebration of the microcredit model's supposed effectiveness ever since it arrived on the development scene in the 1980s, for many this will be a simply stunning statement. After nearly 40 years of rapid growth, how can it possibly be true that the global microcredit industry does not work?

In the 1980s, the microcredit model represented a major financial innovation that, it was widely predicted, would robustly address the problem of global poverty and deprivation. As is well known,

[3] Even those analysts supportive of microcredit that appear to have highlighted the need for a 'reform' of the current global microcredit industry, such as Malik et al. (2020), actually recommend only a few minor operational changes that the global microcredit industry might wish to consider.

these claims began with the US-trained Bangladeshi economist and future (in 2006) Nobel Peace Prize recipient, Dr. Muhammad Yunus, who famously claimed at the time that the microcredit model would "eradicate poverty in a generation." As the supply of microcredit rapidly grew in the 1990s and into the 2000s, the international development community began to believe its own publicity that the microcredit model was indeed succeeding. The global poor were accessing more microcredit than ever, so the common-sense feeling was that it simply must be helping them; otherwise why would they want so much of it?

More scientific evidence to confirm the belief that "microcredit worked" then appeared in the form of a number of influential impact evaluations and studies (Pitt and Khandker 1998; see also the summaries of previous impact evaluations compiled by Goldberg 2005 and then Odell 2010). Much sophisticated econometric analysis produced by leading mainstream economists attached to the main international development institutions also appeared to confirm the validity of the microcredit model as a poverty reduction intervention (for example, see Beck, Demirgüç-Kunt and Levine 2007). With so much high-profile support and validation coming its way, Bernd Balkenhol, former Director of the Social Finance Program at the International Labor Organization (ILO), felt able to report in the mid-2000s that the international development community now saw the microcredit model as "the strategy for poverty reduction *par excellence*" (Balkenhol 2006, 2 - underlining in the original).

If it's too good to be true, it usually is

Just as the celebrations began to peak in the mid-2000s, the first real signs began to emerge that the entire uplifting narrative was fundamentally flawed (see Bateman 2010). While many factors were involved in the radical reappraisal of the microcredit model's impact on poverty and development, I will briefly summarize three of the most important inter-related problems.

First, microcredit has certainly helped a lot of new informal microenterprises get established. But what has always been deliberately ignored in the analysis of microcredit impact, as even World Bank economists now belatedly admit was a serious error (see McKenzie and Paffhausen 2017), is that a very large percentage of these new microenterprises fail very quickly. Failure not just ends any ongoing income flow but can also wipe out any of the assets or savings that had been possible to accumulate prior to failure. It can also lead to the loss of any valuable collateral lodged with an MCI, such as vehicles, housing or, most devastating of all, land (Bateman 2020). Moreover, even when some new microenterprises succeed, they typically only do so by taking clients away from many other existing microenterprises struggling to compete in the same local market. This "displacement" effect hurts competitors who are typically forced to contract and lose any employees. The combined result of failure and displacement, or what is formally termed "job churn" (Nightingale and Coad 2014), is all too often a zero-sum employment outcome. Even worse, the intense competition created in so many communities in the Global South – thanks to the unstoppable microcredit-assisted entry of new microenterprises (and, more recently, so-called "gig" workers) – inevitably helps to push average incomes down to the subsistence level. Put simply, a combination of quite standard labour market pressures tend to ensure that any positive employment and income impacts created by microcredit-assisted new microenterprises are all too often swamped by the negative economic and social impacts of the resulting increased local competition (Bateman 2019a).

A second serious flaw in the operation of the microcredit model became evident from the early 2010s onwards. As it became clear that the microcredit model was associated with limited-to-no net employment and income gains for the poor, the microcredit advocacy community felt that a new goal was needed in order to justify its existence and, more importantly, its continued expansion. Without any fanfare or formal announcement, microcredit advo-

cates began to promote a completely new narrative: that they were involved in a "fight to extend useful financial services to low-income households." The term "financial inclusion" came into being to describe how the global poor should now see microcredit as one of a number of financial tools that would simply help them to better *manage* their poverty (see Collins et al. 2009). This might mean ensuring regular access to basic utilities (water, electricity, etc.) as well as funding housing, healthcare and the education needs of the family. However, this new justification for the microcredit model to continue expanding, which it did, gave rise to the serious problem of over-indebtedness. Beginning in Bolivia in 1999, in all of the countries and regions in the Global South that were to go on to become the most "financially included," we find that household debt began to rise to quite destructive levels (Guérin, Morvant-Roux and Villarreal 2013). The global poor could not fight off what became quite a harmful dynamic. Rising microdebt ultimately diverts income from consumption into debt service, and the immediate economic boost provided by more microcredit has everywhere been swamped by the longer-term outflow of wealth from the communities of the poor (Mader 2015).

A third core problem with the microcredit model is directly related to its commercialization that began in earnest in the 1990s. This move was demanded by key microcredit advocates keen to close what they argued at the time was an "absurd gap" between the limited supply of microcredit and the supposedly massive latent demand for it. The international development community then joined in to support the conversion of MCIs into for-profit bodies. The hope was that the global microcredit industry could be weaned off subsidies and become financially self-sustaining – though, crucially, still retain its social mission. By the mid-2000s, however, the destructive impulses inherent to deregulated capitalism began to take root in many of the largest MCIs. Reckless lending to advance rapid but unsustainable growth goals soon emerged as the defining feature of the global microcredit indus-

try. The CEOs and senior management of the largest commercialized MCIs wanted to grow as large as possible, as fast as possible, in order to be in a position to inflate their salaries and bonuses. Shareholders and investors willfully egged them on so that they could reap growing dividend flows, and then profit even more when their equity investments were later sold off for much more than the purchase price. Inequality also rose as a new "microcredit millionaire" class began to emerge alongside the rapidly growing number of individuals floundering under the weight of their growing debts to MCIs or having lost everything they own on an unwise microenterprise project. In addition, the reckless lending practices of the largest MCIs, combined with the inability of the poorest communities to absorb unlimited amounts of microcredit, led to a growing number of hugely destructive microcredit sector boom-to-bust events. Notable "busts" occurred in Bolivia, Bosnia and Herzegovina, Nicaragua, Pakistan, and then, the largest to date, in Andhra Pradesh state in India (Guérin).

Why did no one see this coming?

There exists a long succession of impact evaluations and serious studies carried out by recognized specialists that, as noted above, were said to have provided an abundance of empirical evidence that microcredit works. Sadly, it is now recognized that almost all of these impact evaluations were seriously flawed and willfully biased in favour of claims that microcredit produces a positive impact. Put simply, careers are not generally advanced by challenging the official pro-microcredit ideology of key governments (especially the US government), prestigious foundations (e.g., the Gates Foundation) or the international development agencies, notably the World Bank (see Duvendack and Maclean 2015). Instead, one learns how to skillfully provide the positive narratives and required impact evidence that one is largely expected in advance to find, if not explicitly paid to produce. Sadly, even recent high-profile winners of the Nobel Prize in Economics winners appear not

to be immune to this temptation.[4]

The fundamental error committed by uncritically supporting the ineffective global microcredit industry is very profound indeed. An unprecedented investment of financial resources, technical support, political capital, academic research and institutional commitment has been largely wasted on supporting an intervention that, it is now increasingly accepted by one-time leading advocates (Roodman 2012: Altman 2014, Waterfield 2020), has actually had zero impact on poverty. The growing disillusion was best captured by Morduch (2017), advisor on microcredit to many international development agencies and co-author of *The Economics of Microfinance* (a standard university textbook), who bravely admitted that:

Yunus's vision – and the assumptions it rests on – is coming apart. Microfinance has proved fairly robust as a banking idea, but not as an anti-poverty intervention....Aid agencies and foundations have been left feeling confused, disappointed and perhaps betrayed – and have started moving on.

Even worse than under-performing against high expectations is that the growth of the microcredit industry has also generated a raft of destructive downsides that have actually helped to *undermine* the ability of the poorest communities to escape their poverty (Bateman 2010; Bateman and Chang 2012; Mader 2015; Bateman et al. 2019). Meanwhile, as many social anthropologists and sociologists point

[4] The 'last word' on the subject of the impact of microcredit was supposedly provided by the six country impact evaluation project headed up by the 2019 Nobel Economics Prize co-recipients Abhijit Banerjee and Esther Duflo, who could only conclude that microcredit had essentially no impact on poverty (see Banerjee, Karlan and Zinman, 2015). However, in order to come to even this tepid conclusion all six of the case studies used weak methodologies, ignored important downside factors ('distortion by omission'), and also apparently indulged in some quite unethical research practises (see Bédécarrats, Guérin and Roubaud 2017, 2019, 2020; see also Bateman 2013). One possible reason for Banerjee and Duflo adopting such problematic tactics was that otherwise their impact results might have rather awkwardly confirmed what the 'harshest critics' of microcredit have long argued – that microcredit has actually had a harmful effect on the global poor – as well as the fact that their own pioneering impact evaluation methodology based on the the Randomised Control Trial (RCT) had actually failed over many years to pick up on this rather important development.

out, the default form of employment that microcredit was established to validate and expand – the informal sector – simply cannot be divorced from the rising poverty, inequality, precarity, deprivation, crime, ill health and vulnerability that have become the defining features of life today at the "bottom of the pyramid" (see Davis 2006).

Further exacerbating the problem here is the fact that, largely as intended, the trumped-up effectiveness of the microcredit model was widely used by the international development community to further marginalize and discredit all collectively organized, locally owned and controlled financial interventions. In the era of neoliberalism, the idea that the global poor should seek to deploy their "collective capabilities" through their own financial institutions simply had to be destroyed. All such financial institutions were ignored and marginalized. Where possible, they were converted into conventional investor-owned financial institutions. Given the effectiveness of community-owned and controlled financial institutions across so many locations in achieving more than what the global microcredit industry can legitimately claim to have achieved anywhere, this was a fundamental error. But it is an error that can now be corrected.

ADOPTING A ROOSEVELTIAN APPROACH TO RECONSTRUCTING LOCAL FINANCE

An entirely new approach to the impending rescue of the global microcredit industry is urgently required. This approach must use the expected financial support and bailout funding to insist on the construction of a new and improved local financial system. The guiding principle is that of the need to build back better, a simple moral imperative that is rightly informing very many international organizations and governments at this unprecedented historical juncture (for example, see OECD 2020). Rescuing the local financial system by building back better' has two quite reasonable goals:

- It must assist in resolving the immediate objective of helping the community to survive the Covid-19 crisis;
- It must also create the core institutional foundations necessary to build a much more pro-poor, democratically owned and managed, and explicitly *developmental* local financial system capable of promoting bottom-up growth in the post-Covid-19 era

In terms of the sheer extent of economic decline and social disruption, the most relevant parallel to the Covid-19 crisis today is the Great Depression. The Roosevelt administration's response is widely seen as a great success. It is therefore an obvious example to study. The most relevant aspect to consider is the rural financial system, which was driven to the point of collapse. However, rather than simply reconstruct or bail out the existing ineffective rural credit structure – which was what the banks, established elites and Republican politicians were demanding – Roosevelt opted for a very dramatic change.[5] This came with the passing of the *Farm Credit Act* of 1933, which represented the first step in constructing an entirely new farm credit system. Through an executive order, all existing agricultural credit bodies were put under the supervision of a new agency, the Farm Credit Administration (FCA), prior to the recapitalization and restructuring of very many of them. More importantly, the FCA established twelve Banks for Cooperatives (BCs) and a number of production credit associations (PCAs) that combined to provide crucial low-cost long-term and short-term loans to the ailing agricultural sector. Roosevelt also pushed through the *Federal Credit Union Act* of 1934. This greatly enhanced the existing credit union network by creating a network of chartered member-owned credit unions to support individuals in the hardest-hit communities.

This radically new cooperatively owned farmer credit system involved the investment of significant financial resources from the state. But this investment was well spent. The new financial system

[5] The following account is drawn from the comprehensive Living New Deal website. See https://livingnewdeal.org (accessed July 2020).

quickly rescued the US agricultural sector from collapse, and so reduced poverty in the rural communities. It also created a solid institutional foundation that decisively underpinned its future success. Moreover, in spite of numerous revisions, the still broadly cooperatively owned farmer credit system put in place by Roosevelt remains today the single biggest provider of farmer credit in the USA. Importantly, it is widely recognized that these initiatives would probably not have been possible in "normal" times. The sheer magnitude of the Great Depression, plus the thorough discrediting of the previous financial regime that effectively caused it (see Galbraith 1955), allowed Roosevelt to outflank those who combined to try to block what they erroneously saw as an attempt to bring socialism to America. A root-and-branch restructuring of the local financial system was the result. Such a Rooseveltian approach to local finance is, I would argue, urgently required today and also manifestly feasible. Defining and implementing such an approach, moreover, is an urgent requirement before scarce financial resources are wasted.[6]

TWO PRACTICAL OPTIONS FOR PROGRESSIVE CHANGE TODAY

A feature of the neoliberalized financial sector that emerged after 1970 is the extent to which ownership changes were encouraged in only one direction: away from public and collective ownership forms and towards private corporate investor-driven forms. The classic example is the UK's ultimately disastrous de-mutualization of its hugely successful saver-owned building societies (see Elliot and Atkinson 2008). Another related feature of recent history is the use of financial support and bailouts to provide "no-strings" financial support to the many private financial institutions that began to fail from the 1970s onwards. It was always expected that the main beneficiaries of such

[6] The global banking and financial elites appear to have already been able to profit handsomely from the government's financial support designed to mitigate the economic impact of the Covid-19 crisis (see The Washington Post 2020).

deals would be the key stakeholders in a struggling financial institution: the CEOs, senior managers and shareholders. As noted by many economists (for example, Stiglitz 2019), this effectively ushered in a period in which the financial sector was able to enjoy significant financial rewards during the good times, but then look to government and the general public to absorb the costs when things begin to turn sour. The most spectacular recent example of this new trend was evidenced during the global financial crisis that erupted in 2008. A large number of financial bailouts were undertaken to save key US, European and Asian financial institutions but without any attempt to change the unstable (neoliberal) model of finance that had actually created the problems in the first place (Mirowski 2013, Tooze 2018). As a result, with even fewer and bigger banks than before 2008, another financial crisis, perhaps even larger than in 2008, is almost inevitable (Hudson 2015, Keen 2017).

What I am proposing in the context of the current Covid-19 crisis is thus the very opposite to what transpired after 2008. Rather than bailing out the CEOs, senior managers, investors and corporate financiers that now own and control the global microcredit industry (very many of whom have enjoyed spectacular financial returns in recent years), public financial support and bailout funding directed towards the rescue of the global microcredit industry should instead be used to effect a major Rooseveltian-type change to the local financial sector. This will involve the conversion of for-profit MCIs into a range of community-owned and controlled financial institutions that have a far better track record of promoting local economic development, including under very difficult conditions. Above all, this will involve the recycling of wealth back into the local community as a whole, rather than its concentration into the hands of a narrow local elite or, even worse, taken outside of the community into the hands of global financial elites located in "tax-efficient" or low regulation locations.

Even before the Covid-19 crisis, many similar proposals had been put forward to reform the local financial system in order to facilitate sustainable and equitable local economic development. Some of the

most cohesive arguments along these lines have been put forward by those attached to what might be called the “community wealth building” movement (for example, see Jackson and McInroy 2017, Guinan and O'Neill 2019). Moreover, these ideas and concepts are also seen as one of the best ways to address the immediate dangers of the Covid-19 crisis (Guinan et al. 2020).

However, the changes proposed here represent quite a radical change to the current ideology and ownership structures relating to local financial institutions in the Global South. Inevitably, as after 2008, they will not be supported by the neoliberal-oriented international development community, nor, for obvious financial self-interest reasons, by the global microcredit industry itself.[7] But as Roosevelt understood, and do so many others today (for example, Bernards 2020), extraordinary times demand extraordinary measures. This is the essence of what is meant by building back better.

There are two general options for the ideal types of institutions that an MCI may be converted to as a condition for bailout funding and other forms of support. There are overlaps between these various types – most commonly the case where a financial cooperative also adopts a community development banking function. However, the ownership structure and social mission are taken as the key defining features that distinguish these institutions from MCIs.

Option 1: Financial cooperative or credit union

This first option involves a move to convert a struggling MCI into a credit union or financial cooperative. A credit union is a member-based savings and loan organization servicing a particular

[7] After the UK government bailed out what was at one time the world's largest bank, the Royal Bank of Scotland (RBS), there were serious proposals, including by one member of the UK Parliament (see Thomas 2016), to convert it into a mutually owned bank with a social mission to promote economic development as well as provide quality and affordable financial services for customers in lower-income segments. Powerful ideological and financial sector resistance to such a measure, plus the Conservative government's desire to get hold of the funds generated by returning RBS to the private sector, ensured that the proposal was blocked.

group, such as the population of a specific geographic area or a set of company employees. A financial cooperative provides similar services to a larger group of members, but it can also have non-members as clients. Both financial institutions exist to provide quality low-cost services, while also recycling any profit back into improving and diversifying member services and providing a regular financial bonuses or dividends. Crucially, quite unlike today's MCIs, the goal of such local financial institutions is *not* to grow at a breakneck pace but to serve the needs of existing member/savers. Because they are unwilling to operate aggressively and exploit clients and employees in order to maximize profits, at times this has meant that financial cooperatives and credit unions are less competitive compared to investor-owned financial institutions. Deregulation can also sometimes open up the door for unscrupulous individuals within a financial cooperative or credit union to abuse and defraud their own institution.[8] Nonetheless, history shows that they "work" to improve the lives of the poor.

In Italy, for example, financial cooperatives have been a major part of the financial sector for more than a hundred years, especially in the north of the country. Suffering greatly in the 1930s on account of their collective foundations, after 1945 they flourished once more and played a major role in the reconstruction effort. While after 1945 the private investor-driven banks preferred to support through imports the renewed conspicuous consumption habits of Italy's still-wealthy elites, the financial cooperative sector played a vanguard role in promoting sustainable economic development and poverty reduction (Bateman 2007). After restructuring and re-capitalizing to repair the war damage, the financial cooperatives went on to play quite a decisive role in rebuilding the region's formal small and medium enterprise (SME)-based industrial sector into one of the world's leading examples. Japan's mutual (*sogo*) banks

[8] Probably the most spectacular instance of this led to the collapse of the credit union sector in the US in the 1990s (see Black 2005).

and the credit banks (*shinkin*) formed out of the larger pre-war credit unions played a key role in the post-war period by financing those small enterprises capable of integrating into the supply chains of the leading companies. Crucially, as Girardin and Ping (1997) emphasized, robust oversight by local governments and the central Zenshiren Bank helped to (re)build local trust and ensure minimal fraud and speculative activity using depositors' money. And in the Global South, it is often overlooked that financial cooperatives have played a quite crucial role in supporting equitable economic development, notably in southern Brazil (Jacques and Gonçalves 2016) and many parts of Colombia (Fajardo Rojas 1998).

Financial cooperatives and credit unions naturally have their own problems, including the extra complication of being run more democratically. However, history shows that they tend not just to be far more effective at addressing poverty and promoting equitable and sustainable development, but are also much more resilient when it comes to coping with wider macroeconomic fluctuations and supporting the poor in the aftermath of a crisis of one sort or another (Goglio and Alexopoulos 2012, ILO 2013, McKillop et al. 2020).

Option 2: Community Development Bank

The second option available to those providing a bailout to a struggling MCI is to facilitate its conversion into a community development bank structure. While many community development banks (CDBs) offer conventional financial services to members of the community, their main role is to proactively encourage economic and social development. A CDB can do this in many ways: by promoting new enterprises in general, supporting specific new sectors of high-growth enterprises, facilitating technology transfer, promoting innovation, and encouraging horizontal networks and clusters of local enterprises in order to reap collective economies of scale and scope. In more recent times, CDBs have been specifically highlighted in connection with the provision of "patient" (long-term) capital that might help the local enterprise sector to sustainably expand

(in numbers and average size), upgrade technology, diversify and export. CDBs are owned and controlled by the community, typically involving some element of public management by the local government overseen by an independent supervisory board of individuals drawn from the wider community.

Like financial cooperatives and credit unions, the concept of the CDB has a long pedigree of success. Many banks in Europe not specifically referred to as CDBs nevertheless function as CDBs. In Germany, for instance, the savings banks (*Sparkassen*) are owned by the local town or other administrative body. They have very successfully promoted local economic development through two mechanisms: first, through their lending activities (they provide as much as two thirds of the lending required by Germany's famous *Mittelstand* [medium-sized] companies); second, through the relationships and networking activities they see as a management responsibility to be performed within the community (Audretsch and Lehmann 2016, 106-7). In addition, the *Sparkassen* are more efficient than their counterpart private sector banks, earning a significantly higher return on capital than the wider private banking system in Germany as well as paying much more in taxation to local and federal levels of government (Brown 2019, 152). In Spain, as noted above, two of the most successful financial cooperatives – the *Caja Laboral Popular* (now known as *Laboral Kutxa* after a merger with a local credit union) and *Cajamar* – are essentially quasi-CBDs, charged by their membership to promote local solidarity and cooperation by acting as a CDB in order to promote the wider economic development of the region (see Bateman 2019b). In the US, the state-owned Bank of North Dakota serves as a CDB in many respects and has played a critical role in developing the state's economy in an equitable and sustainable manner (Brown 2014). Much of Asia's rapid economic development in the post-1945 era can be attributed to the bottom-up development impetus that was orchestrated and funded by a variety of proactive local financial institutions that essentially follow the CDB model. This began with Japan after 1945,

followed by South Korea, Vietnam, Thailand and others, and especially a decentralized China in the 1980s and 1990s (Bateman 2019c).

THE KEY RATIONALES FOR SUPPORTING CONVERSION

There are at least four key overlapping justifications for using potential bailout funding to promote (where possible) the conversion of struggling MCIs into community-owned and controlled financial institutions. The latter are:

1. Better at promoting sustainable economic development and growth: History shows that community-owned and controlled financial institutions are far more capable of promoting sustainable economic development and poverty reduction compared to the average MCI. It helps that the average community-owned and controlled financial institution tends to be a functioning part of the local community and local society, often born as a result of past struggles and difficulties. With its democratic structure, it is also more likely to be held to its mission to promote development into the future.
2. Better at providing for the reinvestment of any surplus: One of the earliest reasons for community-owned and controlled financial institutions to emerge in the 1800s was to facilitate the recycling of locally generated wealth (profit) back into the local membership or the wider local community. This higher reinvestment attribute can also be facilitated by law, such as in Italy.[9] In other words, community-owned and controlled financial institutions are not *extractive* institutions, a term that would correctly describe the operations of most

[9] As with most cooperatives in Italy, financial cooperatives receive certain taxation benefits in return for agreeing to reinvest back into the cooperative a high percentage of their surplus. This legal measure is intended to ensure that the cooperative is better placed to create more sustainable local jobs, raise productivity in order to increase wages, and improve services to members. The cooperative is monitored by the taxation authorities to ensure compliance.

medium-to-large MCIs operating today in the Global South.

3. Better at using fintech for the benefit of the entire community: The Covid-19 crisis has seen the very rapid deployment of financial technologies, or "fintech" by MCIs as a way to avoid contact with potentially infective cash (Haidar 2020). Fintech has enormous potential to deliver benefit to society, but it has become clear already that it has created more problems for the global poor than have been resolved. Two stand out: First, fintech is beginning to exacerbate the problem of over-indebtedness that was raised above. With access to microloans "at the touch of five buttons on your mobile," large numbers of the global poor have already been plunged into quite astonishing levels of unrepayable debt (for the example of Kenya, see Donovan and Park 2019). Second, fintech is helping MCIs (and banks) to tap into the billions of daily tiny financial transactions of the poor and, by taking take a small cut of the value of each transaction, poor communities are effectively being drained of much of their wealth (Bateman, Duvendack and Loubere 2019).[10] However, fintech nonetheless offers a unique opportunity for community-owned and controlled financial institutions to streamline and lower the cost of their operations, as well as retain and recycle locally generated wealth within the community (particularly if subject to democratic oversight).
4. Better at promoting equality: A community-owned and controlled financial institution helps to build equality in the community in two important ways: (1) internal constitutional prohibitions strictly limit the value that elected officials and senior managers can extract as salaries and bonuses from their own financial institution, and (2) internal constitutional requirements dictate that any profit generated is either rein-

[10] For example, thanks partly to its ownership of the iconic M-Pesa mobile money platform, Safaricom is now Africa's most profitable company, earning a Wall Street-sized $US747 million in 2019-20 (see Ngugi 2020).

vested back into the financial institution and/or passed down to individual members in the form of dividends, bonuses and other member reward systems. The problem of the "microcredit millionaires" that has emerged in many locations around the Global South, caused by CEOs, senior managers and so-called "social investors" in an MCI often quite legally diverting its earnings into their own pockets (Sinclair 2012), is much less likely to arise.

KEY PRACTICAL ISSUES TO CONSIDER IN FACILITATING CONVERSION

In terms of the legal, institutional, organizational and other practicalities of converting MCIs into either of the desired new formats, dealing with these issues would naturally require a much longer treatment than space permits here. However, I will introduce several of the practical issues that will likely be important to resolve through negotiation when considering the conversion of a struggling MCI.

First, what type of community-based financial institution is best for the community in question? Small communities may be best suited to a credit union format that provides a limited range of financial services to saver-members and loans mainly for working capital purposes. A larger and more diverse community in terms of employment might be better served with a financial cooperative open to all local people. It would work on savings mobilization and establish a lending capacity geared to identifying and promoting more sophisticated and sustainable employment creation and other projects of value to the local community overall (e.g. cooperative development, renewable energy, local supply chains servicing local consumption needs). The financial cooperative format would be particularly appropriate for communities that receive large remittance inflows, which can become the financial base for much careful lending activity. The CDB format might also be appropriate,

especially in cases where none exist already, and where there are major economic problems, or opportunities to be exploited responsibly, that require coordinated institutional action backed up by "patient" financial support. A consultation exercise with an MCI's clients and other local stakeholders will be required to assess what might work best.

Second, how best to ease out the current owners of an MCI? Especially if large investments were made in recent years and/or the MCI was exceptionally profitable, strictly commercial investors will likely not exit their investment in an MCI without a fight. Inevitably, equity holders will overwhelmingly prefer the sort of "no strings-no change" bailout that Wall Street's banks and bankers received in 2008 – a restructuring process that would rescue an MCI's equity holders by keeping the MCI alive and still under their control. However, if the MCI is on the verge of collapsing, conversion into the desired alternative ownership arrangement might not be too difficult. For example, in return for any financial bailout, a good part of the existing equity held by the current owners and investors could be swapped for an agreed amount of debt to be repaid once the new institution is up and running in the post-Covid-19 period (see also Guinan et al. 2020). The advantage of this debt-for-equity arrangement is that the original equity holders have an incentive to ensure the smooth conversion of the MCI in order that their debt is repaid in full and on time. The fact that foreign investors now own and control a large and increasing share of the equity of MCIs across the Global South further complicates the conversion process. However, it also makes it even more imperative. Foreign investors, including social impact investors, generally have little interest in or sympathy for the countries in which they invest. Even though in the absence of a bailout there may actually be considerably less value attached to the equity they hold, creative techniques will have to be adopted in order to overcome the resistance of equity holders to a change in ownership. Inevitably, the political will to effect such changes, aided by informed community mobilization, will be key.

Third, what form of regulation is required from governments? Democratic ownership and management have many economic, political and social advantages. But it is not a foolproof method of managing an(y) institution and it can often be subverted by narrow elites (both internally and externally) with a determination do so. To ensure that any new institution operates according to the social mission it is assigned, and that it is not hijacked or destroyed by those ideologically opposed to collective action and/or hoping to benefit financially, ensuring robust regulation and (at least initially) local government oversight will be absolutely imperative. In particular, the hugely ineffective forms of self-regulation promoted by the microcredit industry itself (Sinclair 2012), will clearly have to be abandoned in favour of genuine measures to regulate the local financial system in a way that prioritizes the interests of the poor.

Fourth, who or where can we learn from? Financial institutions that work well in one context do not necessarily work well in another. There can be no guarantee in advance that the community-owned and controlled format will lead to local economic and social success. Nonetheless, it is still perfectly possible to learn from and adapt best institutional practices from elsewhere. One obvious and relevant example here is the way that the East Asian "miracle" economies learned from each other in order to create their own pro-poor collectively owned and controlled financial institutions. Beginning with Japan, each of the East Asian states that later achieved economic success did so with the help of a highly efficient developmental local financial model that was built on roughly the same core principles as pioneered in Japan but adjusted to local economic, social and political conditions (see Bateman 2019c). As Akyuz, Chang and Kožul-Wright (1999) have argued, learning from other experiences and adapting good practices to local conditions was the key to East Asia's miracle. To some extent a similar process of learning and adaptation got underway in Europe as a result of the economic destruction caused by the global financial crisis in 2008. In the UK, for instance, European and Canadian experience

has been tapped into in order to form a network of 18 regional cooperatively owned banks, which have as their goal the building of sustainable and equitable local economies (Peck 2020). Furthermore, it is important that many local governments have been successful in re-municipalizing companies that have abjectly failed to supply quality and low-cost services to the public, including many public bodies previously privatized (see Kishimoto, Steinfort and Petitjean 2020). Much important experience of facilitating similar conversions across the local economy now exist.

Fifth, how can clients of an MCI be helped to manage their financial cooperative or credit union efficiently and democratically? This will likely require extensive training, mentoring and on-the-job coaching by skilled cooperative trainers. It helps that much useful experience exists of this type of activity in Europe and elsewhere that can be tapped into by conversion projects in the Global South. For example, the UK's Cooperative College and the Workers Educational Association (WEA) both have experience running training programs and adult learning packages for those involved in setting up a variety of cooperatives, including financial cooperatives and credit unions. In terms of the CDB option, many of the world's most successful national development banks, such as Brazil's BNDES or Germany's KfW, have local units and interact extensively with local governments. As a result, they have the capability to provide training and consultancy to those communities in the Global South wishing to establish CDBs out of a struggling MCI. Germany's *Sparkassen* savings banks have an international development arm (*Sparkassenstiftung für Internationale Kooperation*) that provides advice and assistance to those wishing to replicate elsewhere their very successful cooperative financial model. Finally, there is also Spain's world-famous Mondragon Cooperative Complex (MCC), which has an international development consulting arm that provides advice and training to those who might wish to follow their example. This includes providing advice on how to establish a version of the *Caja Laboral Popular cooperative*

bank, which played a hugely important role in developing the region around Mondragon.

CONCLUSION

The importance of adopting a build-back-better approach local financial systems in the context ofthe Covid-19 crisis simply cannot be overstated. The brief exploration of the issue in this article argues that governments in the Global South, the international development community and local activists must demand that financial support is not used to simply bailout once highly profitable MCIs, but is instead invested in the conversion of MCIs into the most appropriate of three types of community-owned and controlled financial institutions. While the Covid-19 crisis provides the immediate rescue pretext for such a bailout-cum-conversion policy, the fundamental ineffectiveness of the microcredit model as a development intervention provides the crucial rationale for the process to continue thereafter.

While certainly no panacea, history shows that community-owned and controlled financial institutions have a very good track record of providing a genuinely sustainable and equitable pathway for the global poor in order to exit poverty and deprivation. Not least of the advantages these institutions have is the ability to retain wealth generated within the local community and allow it to be used to develop sustainably the economic base and social systems for the good of the *entire* local population, not just for a narrow local elite (still less for a narrow foreign elite). And as the important examples from Europe and Asia demonstrate, community-owned and controlled financial institutions can be a very transformative development model indeed in a post-crisis rebuilding context. A new Rooseveltian approach to local finance in the time of the Covid-19 crisis thus deserves to gain traction today. We might then reasonably hope to see local citizens becoming the masters of the local financial system, and no longer simply its hapless victims.

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