

Lending maturity of microcredit and dependence on moneylenders *

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Abstract

Despite the expanding access to the low-interest credit including microcredit in developing countries, the presense of informal moneylenders still remains substantial and some studies even show that the introduction of microcredit programs increased the borrowing from high-interest moneylenders instead of decreasing it. We show that the short maturity combined with the borrower's consumption smoothing motive can explain the increased borrowing from the moneylender as well as the high sensitivity of the credit demand to loan maturity. Our theoretical model suggests that whether the microcredit programs increases the average borrowing from the moneylender depends on the distribution of the investment returns and the interest rates of microcredit and moneylender, as well as the loan maturity. The simple numerical excercises show that with plausible value of the parameters, the introduction of microcredit actually can increase the average borrowing from the moneylender especially when the distribution of the investment return is not so preferable. We also show that the expansion of the lending maturity will reduce the dependence on the moneylender and increase the uptake rate of microcredit and investment, and the sufficient expansion of the lending maturity will eliminate the case where the introduction of microcredit will increase the average borrowing amount from the moneylender. Our results imply the average treatment effect of microcredit on the informal borrowing will crucially depend on the underlying parameter values, and without clear understanding of the mechanisms, applying the estimated results obtained in one setting to some other settings will be misleading.

Keywords microcredit, flexible repayment schedule, maturity expansion, informal lenders

JEL Classification G21, O16, O17,

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