

# [Ethics: micro finance](https://assignbuster.com/ethics-micro-finance/)

[Finance](https://assignbuster.com/essay-subjects/finance/)

For Profits: The Unethical Side of Micro-Lending The original principle of micro lending is to provide start-up or expansion business loans to people living in less advantaged or impoverished countries who are unable to apply for traditional loans due to lack of credit history and/or collateral. Micro-financing is a great tool to create venture capital for those who would have no other means to secure it. The primary goal of micro lending, as established by Muhammad Yunus, the godfather of microcredit, is to eliminate poverty by means of giving all the opportunity to be self-sustaining with long term solutions.

The principle of micro financing is the mutual benefit of relationship between microfinance institutions and the improverished, however one must note that there is a distinct difference in the for-profit and not-for-profit lenders moral standing when regarding profits. For-profit micro lenders maxmize shareholder wealth while non-profits use the profit to grant more micro-loans. Here is where the ethical dilemma lies not in the principle of micro-financing, but rather in the implementation, operations and profit distribution of for-profit micro-financing.

Does for-profit micro lending widen the socioeconomic distribution among communities? Is it ethical to charge the least advantaged high interest rates, when they are the most in need of the loans? The theoretical principle of Utilitarianism a form of Consequentialism, asks society to maximize the good of the whole and states that the action is determined by the outcome. If we first look at the outcome of for-profit micro lending, we see that the high rate makes it more difficult for people to pay back the loan.

For-profits generally charge a higher interest rate for loans and claim that it is because the risk is higher, however the microcredit loan repayment is 95-97%, with only a 3-5% default rate. A side-to-side comparision of two of Mexico’s top micro-financing instituions show that for-proit companies could be charging much lower rates. Compartamos, a for-profit company is charging upwards of 100 percet per annium on there loans while Al Sol, a non profit firm, is charging half of that of Compartamos while their retained profits from there borrowers both hover around 41% (Mix Market).

This leads one to question the morality, authenticity, and ethics of the high risk rate when the default rate for these loans is so low. As a result of for-profit micro lenders charging exorbitant interest rates, one could say that this is not maximizing the utility of the whole, but rather holding society back. If we, as a community, are able to aid the least advantaged and level socioeconomic standing on a global scale, we could potentially eliminate tax dollars that would be used for charity and non-profits.

With less money being spent on aid to individuals because those individuals are able to take their micro loans, develop businesses and be self sufficient, we would be maximizing utility and all of humanity would benefit. For profit micro lending profit is used to benefit the shareholders, while non-profits use profit to reinvest in their company and grant new loans. Based on this we can deduce that for-profit micro lending is unethical because it does not maximize the net gain or profit to benefit the whole but only rather benefit the shareholders wealth.

It could be said that unlike for-profit micro lending, non for-profit micro lending is Pareto Superior because it in itself is not causing harm to anyone. Government subsidizes are allocated based on regulations, people who donate to the non-profits do so of their free will and recipients have the capability to better their living situation. Non-profit micro credit will benefit the whole of humanity because it assumes that if it can help all, all will be able to have income and poverty will cease to exist. Rule Utility states that an “ action is ethical if and only if the action would be required by those moral rules which are correct. LECTURE PP Assuming that the moral rules of our society are to respect and honor members in our communities, according to this rule the principle of for-profit micro lending is unethical. Furthermore if we see our community on a global scale rather than our neighbors next door, we should actively help the greatest group in society, therefore giving aid to the poorest and largest majority. It should be noted that micro loans are not granted to people who do not wish to better themselves, but rather bring people out of desperate situations and give them the ability to work for a better life for their family and self.

Micro lending was created with the sole design to aid the less advantaged and bring people out of poverty. Muhammad Yunus, a firm believer that it is a human right to have the capability to work and be able to provide one’s own living. If we follow the basic positive rights granted to humanity such as the right to life, adequate housing, food, clean water and clothing, for-profit micro lenders are denying people’s fundamental rights because of the high interest rates and consequently the unethical gain of profit of these high interest rates.

Micro lending is a global consideration and as human beings or rather rational agents there are certain moral and rational laws that apply to us for simply being human and belonging to this group (LECTURE ref). Yunus’ defined his measurement of success to microfinance as, “ To have graduated have graduated from poverty, a family must have, among other things, a house with a tin roof, clean drinking water, a sanitary latrine, warm clothes for winter, and mosquito netting for summer; about seventy-five dollars I a savings account; and schooling for children (Bruck, Millions for Millions).

Following Kant’s principle of the categorical imperative “ Everyone ought to be treated as a free person equal to everyone else” (LECTURE). For-profit micro lending where profit is given to shareholders goes against Kant’s Formulation of Humanity which says that humans possess dignity and should be treated as so. Kant believes that humans should not be treated as a means to an end, which is oppositely exhibited by for-profits micro creditors are treating the recipients of loans as means to profit because they are turning making revenue off of others hard work.

Furthermore, if we are allowing for-profit micro lenders to benefit off of the poorest of people we are not treating the borrows’ as equal but rather using them as a means. Yunus calls for humans to recognize their duties to society. Yunus looked at gender and as a result believes women are more likely to repay the loan back because of their tendencies to put their family’s needs first and therefore take additional loans after repayment of the first (Cavanaugh, 312). Statistics show that in countries, such as India, there is lower default ate and the loans are more beneficial to the entire family when women manage the funds. Because many of these loan recipients are from impoverished areas generally the women who apply for the micro loans are less educated than their male counterparts, and as a result many of the micro finance institutions provide basic education classes on how to run successful small businesses. Lenders have a duty and a responsibility to ensure that borrowers know and understand the details, rules and potential consequences of the loans.

Acting ethically in this situation would include that sense of duty towards honesty to borrowers, which includes not only telling the truth about all aspects of the loan, but not omitting details, or misrepresenting information. Recently, some governments have enacted policies protecting consumers ensuring that these potentially financially uneducated individuals are not subject to the fine print, or potential manipulation by these micro lending institutions. Some banks act against regulation, as can be seen in Nigeria, and ask for collateral because of credit situations of low income level individuals that apply for these loans.

This extra collateral begs ethical implications that these lenders are implementing because this gives lenders an opportunity to take more from the borrowers if they are unsuccessful in attaining the necessary funds to repay. Virtues/JUSTICE Virtue of charity Virtue of generosity (see and add to paragraph below) The high interest rate takes a personal toll on the individual borrower. Any capital that was going to be reinvested in their small business is now being paid back to the lender. This leaves the borrower financially vulnerable if their business fails, has a medical emergency, or other expenditures.

Although it a business’s goal is to make money, we as a society should govern what we believe are a reasonable rate because 20-30% return lenders are aiming for is simply unethical. (Where did you get the 20-30 percent number? ) The virtue of charity could come into play in this micro-finance problem. Charity can be briefly defined as helping others that are less fortunate than us. Concerning micro-lending, one could say it is a charity by helping those that otherwise would not be able to receive loans. Even hough these people most likely do not have any credit, they have a right to it. These micro loans could help them establish credit for the future and maybe take out bigger and bigger loans to create a better life for them. By being a for-profit model business, they would think less aobut this charity side and look more towards citizens that already have some history of loans and perhaps are not even in poverty, just to help the company be more profitable. The Grameen Bank was started to help those in poverty to rise out of it, and make a good life for themselves.

If these non-profit micro-fancing “ charities” did not exist what would happen? Well other charities would most likely get involved. I have donated to charites before and do not expect anything in return, it just makes one feel good that they could change someone’s life. This reflects the non-profit model. The for-profit can lose site of such a valuble virtue and focus only on profits, which is not why micro-financing even started. The theoretical principle of justice states that the individual should be given what they deserve.

More specifically Distributive Justice theorist, Rawls, believes that “‘ the most common way of producing more wealth is to have a system where those who are productive earn greater incomes’” (SITE: LECTURE). For-profit micro creditors give their profits shareholders in lieu of reinvestment of future loans and if we adhere to Rawls’ principle, it is overtly evident that for-profit micro creditors are denying justice to potential recipients who might better from micro credit. Rawls’ believes that productivity should produce incomes.

If we deny people the right to a living or the capability to a potential living we are indeed denying them what they deserve. Rawls’ justice or fairness aims to benefit the least advantaged members of society and benefiting these members in return will equal the economic distribution of society. In this case non-for-profit microcredit institutions level the global socioeconomic playing fields while for-profit micro lenders unethically keep the economic distribution at its current larger scope. Justice calls for bridging the economic gap, which for-profits do not do.

Rates for microcredit should be higher than that of the risk free rate of a country, but how high is responsible? This begs another ethical question concerning for-profit micro lenders who charge upward to 20-30% interest rates, while non-profits provide the same services but seek subsidizes from government aid or subsidizes internally with their loans by charging clients who have a job and more means to pay the loan a higher rate and subsequently using that interest to subsidize loans where repayment might be harder. It stands in the way of a borrower achieving a better life for themselves.