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CREATING KNOWLEDGE TO END POVERTY

MICROCREDIT IMPACTS IN URBAN MEXICO

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Credit markets ration loans to people in poverty. In developing countries, credit market inefficiencies mean that poor households are not able to allocate their labour resources optimally. Improved availability of microcredit to poor households should lead to a re-allocation of their labour resources, with implications for their productivity, income and poverty status.

Wider poverty impact

Improved access to credit could also have a wider impact on poverty, if it leads to new employment opportunities among fully or partially unemployed workers outside loan-supported households. Knowledge on the extent to which microcredit can lead to increased employment among extremely poor people is important, particularly in urban settings, as labour often represents the only source of livelihood for them. We conducted a study in three microfinance institutions operating in Mexico City and Tula City, to investigate these issues.

The study contributes to knowledge on microcredit in two important ways. First, we test whether, by lending to vulnerable, non-poor households, microcredit programmes can indirectly benefit poor labourers by generating increased employment. We also investigate the routes through which microcredit reaches people in poverty outside the loan-supported household. Second, we conduct a study to take into account the spatial dimension of urban credit markets in Mexico.

Increase in labour supply

Our findings show that participation in a microcredit programme over time leads to an increase in labour supply. This eventually trickles down to poor labourers outside the loan-supported family. If, by borrowing capital, enterprising households increase production to the extent that they cannot supply the required labour themselves, then the propensity to hire labour increases.

This is illustrated by the green line in Figure 1, which we envisage as a *platform for employment generation*. These trickle-down effects were only observed after loan-supported enterprising households had achieved income levels high enough to afford expenditure on labour. We estimate that

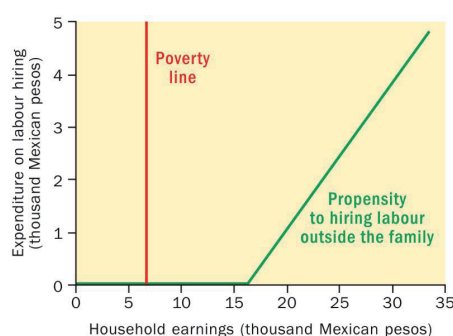


Figure 1: Household earnings and labour-hiring expenditure (2004 prices)

income level to be about three times as high as the poverty line, which is represented by the vertical red line in Figure 1.

Wage differences

Although we found no evidence of labour hiring by the poorest loan-supported households, we did find that one-third of labourers employed by loan-supported households were in poverty.

Important differences were also identified between loan-supported households and their corresponding control group, in relation to the wages paid to poor labourers. The former group paid wages 25 percent above the poverty line, whereas the latter paid wages below the same threshold. Two factors explain wage differences: labour intensity, i.e. more hours at work; and labour productivity. This suggests that efficiency factors were driving up the wage rate. The policy implications of our research results are summarised below.

Key policy points

- Rigid approaches to poverty targeting in microcredit delivery may miss out important trickle-down effects which can indirectly benefit people in extreme poverty.
- By extending credit access to non-poor households, microcredit programmes can indirectly contribute to alleviating poverty in urban markets, by generating increased employment.
- Intra-household allocation of labour resources resulting from improved access to microcredit can have adverse effects, if it increases child labour. Policy devices to maintain school attendance are crucial.
- As well as credit access, the duration of programme participation is important for increased employment generation.

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