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# Commercialization and Microfinance Interest Rates: Usury or Just Prices?

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Prevailing microfinance interest rates can be very high (20–30 percent on average and well exceeding 100 percent in some cases). The number of faith-based (especially Christian) organizations in the field, biblical injunctions against charging interest to poor people, and increasing commercialization present acute ethical tensions. In conjunction with contemporary research, the authors examine biblical passages and reflect theologically, employing a narrative-ethical approach to the issue of interest rates in contemporary microfinance. They conclude that while prohibitions against usury are still appropriate, a broad condemnation of high interest rates in microfinance is presently unwarranted.

During the past decade, microfinance (a.k.a. microcredit) has been heralded as a revolutionary tool in alleviating poverty. The concept has attracted broad-based support, in part, because it is driven more by a market, rather than a charitable, orientation. In theory, extending small loans to "unbankable" poor people (roughly 2–3 billion people) empowers the startup or expansion of tiny enterprises and subsequently aids recipients in lifting themselves out of poverty. Furthermore, because the loans are paid back with interest, the funds can be recycled and costs recovered, leading to an economically sustainable poverty intervention. Based on this type of promise, the United Nations dedicated a year to microcredit in 2005, and, in 2006, a shared Nobel Peace Prize was awarded to Dr. Muhammad Yunus and the Grameen Bank.

More recently, however, the field has come under increased scrutiny. Some critics believe microfinance serves a neoliberal agenda more than it does the interests of poor people.[1] The increasing influence of commercial interests, client debt levels (and reports of resulting suicides in India), lack of pricing transparency, and the bursting of several microcredit "bubbles" have also raised the level of scrutiny.[2] Moreover, initial rigorous studies have yet to find evidence to support the early promise.

Amidst (and to some degree underlying) these controversies has been a contentious moral debate regarding the prevailing rates of interest charged to clients.[3] Stated rates average between 20 and 30 percent annually and can well exceed 100 percent in some cases. While charging interest of any amount to poor borrowers may seem morally questionable, increasing commercialization adds a new dimension. Earning money from interest no longer serves only the objectives of covering costs and/or funding growth—now it also goes toward private gain. The latter strikes some as "profiting on the backs of the poor."[4]

This issue seems to be especially appropriate for Christian ethical reflection. Given the Bible's direct moral injunctions against charging interest to vulnerable people, usury is one of the most contentious issues within the Christian tradition. For example, John Jewel (1522–1571), a former Bishop of Salisbury, cites Ambrose, Chrysostom, and Augustine while condemning interest on loaned goods and/or money as "filthy gains and a work of darkness" that originate from the same source as "the works of the devil and the works of the flesh."[5] Jewel and many other canonists and theologians sought to draw distinctions between immoral usury and legitimate compensation for the lender.

Christian ethical reflection is also important considering the size and influence of organizations involved in microfinance that operate as faith-based (Christian) entities (e.g., Opportunity International, World Vision), were started as such (e.g., Compartamos), or were founded with personal faith as a motivating factor (e.g., Kiva). Although the majority of faith-based organizations are chartered as nonprofits and have generally not been directly connected to recent controversies, many charge at or near market rates of interest. They may also have for-profit chartered banks within their networks and/or accept private investment funds. Many globally minded Christians have also channeled funds to microfinance through charitable giving, such as "peer to peer" loans through organizations (e.g., Kiva) or other investment vehicles. Microfinance can also be considered a forerunner to growing applications of business/enterprise approaches (e.g., Base of the Pyramid [BOP] Business, Social Enterprise, Impact Investment, et al.) to alleviate poverty. Evaluating some of the tensions inherent in navigating multiple bottom lines may provide useful insights to the larger issue of whether or not profits and development goals can be attained simultaneously.

In what follows, we examine whether current interest rate charges in the commercializing world of microfinance should be condemned as usurious, should be cautiously accepted, or should be defended as just prices. We will utilize a narrative approach to Christian ethics in conjunction with the exegesis of key biblical passages, the examination of theological perspectives, and the contemporary research into microfinance institutions and clients. Prior to our analysis, we will provide some important background on the evolution of microfinance into an industry. While the terms have sometimes been used synonymously and their distinctions blurred, we will refer to *interest* as charges above the principle loan amount that must be repaid by a borrower for the privilege of the intertemporal transfer of future income to today. In contrast, *usury* will refer to a level of interest motivated primarily by greed that exceeds legitimate compensation to the lender and is thereby unjust and immoral.[6]

## Microfinance: From Pilot Projects to an Industry

The concept of loaning small sums to low-income people for enterprise purposes has a long history. However, the advent of modern microfinance has been credited to several pilot projects that occurred roughly simultaneously. Most famously, Muhammad Yunus' experiments with microcredit in 1976 started with $27.00 from his own pocket and eventually became the Grameen Bank.[7] Since then, microfinance has grown rapidly. Grameen, technically a for-profit enterprise but operated more like a member-owned co-op, now has over 8 million client members and has loaned a cumulative amount of about $10 billion.[8]

Still, Grameen is only one of several microfinance institutions (MFIs) that serve several million clients.[9] Globally, the Microcredit Summit estimates that as of 2009, over 190 million poor people had received microloans and that over 3,500 institutions were engaged in microcredit lending.[10] MFIs regularly report loan repayment rates in excess of 95 percent, which are higher than repayment rates in traditional banking. Through its successes, microfinance has drastically changed long-held assumptions about the ability of economically poor people to handle credit. Many MFIs are also moving beyond credit to emphasize the broader dimensions of finance. For example, some institutions offer savings accounts to help people manage "economic shocks" and accumulate useful "lump sums." Micro insurance to protect clients from natural disasters, crop loss, and death in the family is also in its nascent stages.

Microfinance, once the domain of NGOs, has evolved into a global industry. In recent years, various forms of commercialization have taken place, including the transformation of nonprofits to chartered banks (e.g., BancoSol), the direct entry of for-profits (e.g., Pro-Credit), and the involvement of Wall Street institutions (e.g., Citibank, Standard & Poor's, Sequoia Capital).[11] In 2006, a

Mexico-based microfinance institution, Compartamos, originally founded as a faith-based nonprofit, held an Initial Public Offering (IPO) of stock, raising over $400 million. Similarly, in 2010, SKS in India, founded as a for-profit backed by global investors such as George Soros, had an IPO that raised $350 million.

Some see these changes as causes for celebrating once excluded clients who have proven themselves to be bankable on a commercial basis and are free from depending on aid or charitable subsidies.[12] In fact, some believe it would be desirable if no distinct "microfinance sector" existed in the future because this would signify the full mainstreaming of underserved people into standard banking channels.[13] Commercialized institutions (versus nonprofits) also offer a number of possible direct benefits, including ready connection to country or regional financial payment systems and the legal ability (as regulated banks) to accept deposits and engage in financial intermediation without special provisions from governments.

More importantly, mainstreaming is seen as desirable because it ensures the sustainability of the industry and allows for expanded outreach. Microfinance initiatives that do not at least recover operating costs and loan losses are dependent on donor subsidies. Government subsidies and private charitable funds are insufficient to reach the billions who lack access to formal financial services. Creating an industry by offering competitive returns to attract investment through global capital markets remains the only known way to access sufficient funding.[14] The use of commercial funds has the additional benefit of freeing up government and charitable monies for other purposes.

Critics of increased commercialization fear the profit motive will lead to exorbitant interest rates and aggressive promotion of loan products.[15] In turn, borrowing in excess of capacity and "multiple borrowing" may occur.[16] "Mission drift" is another worry as poorer clients, who are very expensive to serve, may be abandoned in the quest for institutional sustainability and profit.[17] While all microfinance institutions, regardless of tax status, are susceptible to these types of pressures, the profit motive seems to magnify them. In fact, Yunus believes that some institutions have now become like the exploitative informal money lenders that microfinance originally sought to replace.[18]

## Interest, Usury, and the Bible

Within the context of these recent developments, we now turn to our central task: ethical evaluation. We will begin by examining key sections of the Bible that address usury and interest.[19] In order to comprehend the means by which Judeo-

Christian Scripture speaks into current interest practices, it is first necessary to understand what the passages meant in their own time and place.

## Exodus 22

The first instance of a prohibition against interest occurs in Exodus 22:25–27:

> If you lend money to any of my people with you who is poor, you shall not be like a moneylender to him, and you shall not exact interest from him. If ever you take your neighbor's cloak in pledge, you shall return it to him before the sun goes down, for that is his only covering, and it is his cloak for his body; in what else shall he sleep? And if he cries to me, I will hear, for I am compassionate.

This specific section of the Hebrew civil law focuses on the social harm that interest can inflict on the widows and orphans.[20, 21] They would likely be borrowing money under conditions of desperation such as meeting their most basic needs. Thus, the author begins the passage by urging the Israelites to avoid subjecting vulnerable people to a slave-like status.

With this notion of avoiding affliction in mind, the author continues by addressing the ways in which lending to the poor ought to be conducted without harming them further. The Hebrew word for lend is *lavah*; it can be translated both as "to borrow or lend" *and* "to be joined." Of the twenty-seven times the word occurs in Scripture, the word is most often translated as "join" (ten times) or "lend" (seven times).[22] Thus, etymologically speaking, the Scriptural view of lending from this passage carries covenantal significance—a loan establishes a relationship between parties and thus reinforces a sense of joined community.[23]

Therefore, the notion of interest runs contrary to the communal goal. In fact, *neshek*, the Hebrew word interchangeably used for interest or usury is etymologically related to the word for *bite*; it infers that interest operates like a snakebite as it starts small and swells to unmanageable proportions.[24] While biblical instruction remains neutral regarding the general issue of lending to the poor, a loan with the bite of interest seems to run contrary to the covenantal relationship, especially when it afflicts those who are already marginalized.

## Deuteronomy 23

Keeping in mind that ancient Israel existed as an agrarian and communal society, Deuteronomy 23:19–20 states:

> You shall not charge interest on loans to your brother, interest on money, interest on food, interest on anything that is lent for interest. You may charge

> a foreigner interest, but you may not charge your brother interest, that the LORD your God may bless you in all that you undertake in the land that you are entering to take possession of it.

The word *ach*, translated as "brother" in this passage can also be translated as "relative," "kinship," or someone from the "same tribe." Thus, in these verses, "brother" refers both to familial relationships and tribal kinship.

In contrast, interest on loans to foreigners was permitted. Gerhard Von Rad suggests the following:

> Since Israel even as late as the time of Deuteronomy was almost exclusively a nation of peasants, it was really only foreigners who acted as traders and merchants (cf. Neh. 10:31; 13:22). Occasionally the word "Canaanite" (Zech. 14:21; Prov. 31:24) means simply traders.[25]

In other words, loans with interest to foreigners are permitted because they function outside of the community *and* they engage in businesses where interest represents a legitimate cost to the lender, and the additional income created for the borrower can be used for repayment.[26]

## Nehemiah 5

As part of what is perhaps the largest Old Testament passage dedicated to usurious practices, Nehemiah the prophet speaks harshly against those profiting by interest taken from the poor (5:10–12):

> "Moreover, I and my brothers and my servants are lending them money and grain. Let us abandon this exacting of interest. Return to them this very day their fields, their vineyards, their olive orchards, and their houses, and the percentage of money, grain, wine, and oil that you have been exacting from them." Then they said, "We will restore these and require nothing from them. We will do as you say." And I called the priests and made them swear to do as they had promised.

For historical context, the prophet pronounces these claims in the midst of Israel's drive to rebuild Jerusalem. During this singular focus, many Israelites found it difficult to maintain agrarian production and, thus, a famine ensues. With basic needs in mind, working-class Israelites found it necessary to counteract the famine by borrowing money from wealthier families. Such practices, the prophet argues, turns fellow citizens into slaves or, linguistically, into those who are trampled on.

In short, the Old Testament prohibitions against usury materialize around the fear of injustice. If a poor person has less than the necessary minimum for survival, a loan with interest can increase her poverty as she continues to take new loans to meet basic needs while debt escalates. The Hebrew Scriptures remain unified around condemning this injustice. As a community, Israel must not allow debt to swell like a snakebite in the lives of the poor.

## The New Testament and Interest

Although Palestine in the era of Jesus found itself in communication with the larger economic world, the New Testament speaks very little about interest. In fact, it is mentioned only twice (both occurring as parables in the Synoptic Gospels), once in Matthew 25 under the parable of the talents and the other mention in Luke 19 during the parable of the minas.

In both parables, the master praises the servant who succeeds in business and condemns the servant who fails to invest the master's money. These stories suggest that the servant, at the very least, should have put the money in a bank so that interest could be collected. Interestingly, the Greek word for interest in both passages is *tokos* and may also be translated as "birth" or "the act of bringing forth." While the Hebrew word, *neshek*, exhibits interest in harsh terms, *tokos* portrays interest in a positive light, suggesting that it is a way that "brings forth" more money. While acknowledging that finance is not the focus of the parable, William C. Wood notes,

> It does cite the master approvingly and the parable does not question the existence of credit markets or the master's right to receive a return. It also establishes the rate of interest as a floor rate of return that could be expected even from a lazy servant who would not work to increase his master's capital. [27]

Although both parables seem to indicate that charging interest is an ethical practice, they should not be used as "proof texts." Through these parables, Jesus suggests that people ought to utilize what they receive. Yet, to apply these texts as direct support for charging interest to borrowers is to misapply the passage.

## Theological Perspectives on Current Interest Rates

From a theological perspective, it seems that the underlying concept behind these biblical prohibitions is a condemnation of greed, the value of community, and the protection of poor people from exploitation. Economist Thomas F. Divine elaborates:

> The evil of usury is considered to lie in its origin (or motives) and in its effects. Its origin is greed and cupidity in the heart of the usurer, an insatiable desire of wealth for its own sake which leads to serious violations of the love which every Christian owes his neighbor.[28]

If the prohibition against usury is rooted in the rejection of greed and selfishness and its previously discussed deleterious effect on destitute borrowers, there seem to be general conditions under which charging interest is justifiable. In other words, is it ethical under certain conditions to invest and "make money from money?" Is wealth gained in such a way consistent with the biblical story?

Even in biblical times, the prohibition against usury was not a full-scale condemnation against possessing wealth. Jim Halteman notes,

> While the Old Testament prophets strongly criticized patterns of behavior that broke down the web of protection against poverty, they do not appear to have indicted generalized prosperity. The Old Testament is full of examples of God blessing his people materially. In these cases, however, there is an underlying confidence that, if the law is kept, the social structure will filter out the dangers of wealth accumulation.[29]

In other words, the ban on usurious practices exists not to limit the prosperity of the wealthy but to provide opportunity for the poor to ascend economic classes.

Thomas Aquinas, while maintaining the classical interpretations against usury, admitted that selling items at a just price is an ethical position. If profiting on items is ethical provided it is justly priced, is it possible that loaning with interest functions well under a just rate? Christopher Franks asserts,

> Thomas' understanding of just price and usury are of a piece. In both areas, Thomas seeks to stave off economic practices that threaten to undermine the deference and trusting vulnerability to an antecedent natural order that he sees as crucial to human flourishing and to maintaining justice in human relations of exchange.[30]

Again, the principle behind forbidding usurious practices but allowing just pricing follows the rule of providing equal opportunity for rich and poor. If the poor receive loans at a just rate of interest, it follows that the loan is not usurious.

Interestingly, one of the first prominent theologians in the Protestant tradition to allow interest outright on a loan is John Calvin. Despite acknowledging the so-called biting effect of interest on those unable to repay loans, Calvin likened the payment of interest to the payment of rent for the use of land. Put simply, Calvin found interest to be the cost of using money. Eric Kerridge sums up Calvin's position well when he writes, "All that the rest of Calvin's verbiage amounts to is, genuine interest is allowable." While retaining judgment on those who took advantage of the poor through outrageous loans, Calvin considered a just interest rate to align with Christian Scripture.[31]

Current perspectives echo the sentiments previously discussed. Charging interest, in and of itself, is not prohibited by Christian ethical teaching; it is both the intent of the lender and the impact on the borrower that seem most central. In a document detailing usury in the twenty-first century, the Presbyterian Church (USA) offers a "usury quotient" for those considering the ethics of lending to the poor:

1. Does a practice or a law promote financial relationships that take advantage of the financial distress of those economically disadvantaged?
2. Is a practice or a law structured in a manner that balances the economic benefit for both the lender and the borrower?
3. Does a practice or a law lead to the conduct of financial transactions in a fair and just manner, for example, characterized by truthfulness; nondiscrimination to the borrower; full (and understandable) disclosure; and the absence of coercion?[32]

## Applying Biblical Prohibitions in Contemporary Settings

Despite the plain speaking in the Bible toward a prohibition against usury, the application of these principles in modern settings, given contextual differences, is less straightforward. In ancient Greek and Roman societies, small investment and interest structures existed, but loans were generally given for nonproductive purposes, such as allowing poor people to repay their debt.[33] When the poor encountered a difficult economy or a harsh agricultural season, taxes became a difficult reality wherein harsh consequences such as slavery and/or prison, were possible outcomes of failing to pay. In these instances, taking out a loan with interest functioned as a way to avoid punishment, even if only temporarily.[34] Some scholars also believe that although elements of market economies existed, extractive wealth transfer by Roman and religious authorities worked to concentrate power and resources into fewer hands; hence widening inequality and prompting resentment and suspicion toward the wealthy.[35] Craig Blomberg and Bruce Malina note that people who lived in the biblical era operated under a belief in the "theory of limited good" (equivalent to a zero sum game).[36] These factors contributed to significant doubts about both the legitimacy and the possibility of benefitting from borrowed capital. On the lender's side, operational costs, constant inflation, and exchange risk were likely not significant factors in loaning money.

Nonetheless, charging interest to poor people for the meeting of *basic* needs in agrarian and subsistence-based economies still seems questionable. Loans to meet basic necessities seem to be exceedingly difficult to repay if they are not put toward productive uses. Today, then, these prohibitions against usurious practices seem more directly applicable when it comes to people who are truly destitute or are very close to being so. John T. Noonan Jr. adds:

> In a largely agricultural economy, one may infer, the moneylender, making money whatever the weather, was an unpopular figure, and money breeding money was perceived as a social evil. Biblical teaching, patristic commentary, and social hostility to moneylenders united to form an intellectual milieu in which usury was seen as intolerable.[37]

A moneylender who was not only exacting interest but also was perceived to be hurting the poor, additionally, was thought to be doing little work to help the community flourish. Similarly today, if vulnerable people are first and foremost concerned with basic survival, any loan granted to them would seem to carry the greater possibility of infecting them with the poisonous bite of usury.

What about those who are considered to be *marginally* (or moderately) poor? While a popularized "story" of microfinance has it that everyone, including financially destitute people, are potential entrepreneurs, microfinance is geared toward those who are economically active.[38] In fact, some research indicates that most clients actually live closer to the poverty line of their countries and are, thus, better characterized as "moderately poor."[39] Research by Daryl Collins et al. indicates that those who are not destitute poor people are actually astute money managers and that loans with interest are important tools in their financial "portfolios."[40] Thus, an important question to consider is whether or not the biblical prohibition against usury applies equally to moderately poor people as it does to those who are truly destitute.

If an appropriate interpretive framework is defined by the broader narrative of Christian Scripture as opposed to a so-called rule book, the biblical prohibitions against usury point us toward a larger story and become the outline of a deeper principle instead of a universal rule.[41] William Spohn argues:

> The basic command that Jesus gave at the end of the story of the Good Samaritan (Luke 10:37) invites his followers to think analogically: "go and do likewise." The mandate is not to go and do exactly the same as the Samaritan. It is decidedly not to go and do what you want.[42]

He continues, "The challenge for Christian ethics is to think analogically, that is, to be faithful and creative at the same time."[43] Along similar lines, Samuel Wells observes that when ethics is guided by interpreting the Bible through a narrative structure, it can be seen as akin to the script of a theatrical play. Using a five-act play as a metaphor, Wells asserts, "Act One is creation, Act Two is Israel, Act Three is Jesus, Act Four is the church, and Act Five is the eschaton (future)."[44] In other words, the Bible dictates the first three acts of the divine play and we are currently living in act four. As it would be inappropriate for the main characters in a play to continually speak lines from a previous act, to repeat the past is to neglect the importance of the present. While the current act emerges from the previous acts, it is not the *same* as the previous portions of the play. Living into a narrative as opposed to a strict application of principles necessitates improvisation.

Just as it makes little sense to repeat previous acts, however, it is equally absurd to completely ignore the building narrative in the play. Wells argues that acts one through three ought to be used as an improvisational basis for the current performance. Thus, improvisation does not mean complete freedom to drift from the script. Just as a child finds freedom to express creativity in a backyard surrounded by fences, improvisation may only properly take place with the previous portions of the narrative acting as boundaries.

Along these lines, the biblical prohibitions against usury act as a portion of the script in the broader narrative; the prohibitions must be taken into account, but the mere command against charging interest does not necessarily condemn such practices in our current setting. From our earlier exegesis of the passages on interest, it seems to be evident that usury was prohibited when it exploits vulnerable people. Yet the New Testament strongly suggests that creating capital by way of interest can be a positive practice. Given some of this ambiguity, an improvisational ethic must understand these views in the previous acts of the narrative and would bind our present actions accordingly. If the extension of credit bites the poor and interest swells, a narrative ethic would likely condemn its practice. If, however, credit empowers and improves people's lives, interest (even at seemingly high rates) can be seen in a positive light.

One could object to a narrative approach that suggests that such an ethical stance leads to an ends-justify-the-means rationalization. While it is important to avoid marginalizing consequences, a narrative approach does not function from a foundation of consequentialism. Instead, this approach builds from classical Protestant ethical applications. Calvin, in fact, built his social ethics off the principle of equity. Guenther Haas notes, "A commitment to equity in one's relations with one's neighbor is the manifestation of the transformed life flowing from union with Christ. For Calvin equity provides the essential meaning and criterion of justice in the various realms and relationships of life."[45] As such, equity is a guiding factor in an ethical approach to the usury question. The question, therefore, does not exclusively orbit around the consequences of microfinance. In part, with a narrative approach, equity suggests an active relationship with our neighbor, one for which lending at just prices might contribute to our neighbor's flourishing.

## Interest and Current Times

Given the complexities of current economic life, a universal application of biblical prohibitions against usury seems misguided and may even result in reducing the availability of a valuable tool to improve the lives of poor people. When viewing the Bible in a narrative framework, applying verses against usury requires some improvisation or use of "analogical imagination" that is informed by the current context in which loans are extended. As the Old Testament prophets, Thomas Aquinas, and John Calvin have suggested, the passages in question do not denounce interest in general. Instead, these passages specifically speak against taking advantage of the poor and profiting from them. As the Presbyterian Church (USA) states, the question of applying interest rates requires a nuanced quotient that strikes at the root of the lenders' intentions.[46] If the lender charges interest without distressing the poor and offers them a just rate, it is within the Christian ethical framework to allow such loans. Given the shape of the foregoing acts of the script, it is necessary to examine two questions if improvisation works in ways that are in keeping within their spirit: Are current rates fair and just? As asked earlier, how do current interest rates affect the lives of borrowers?

The "fairness" of prevailing rates is difficult to define and measure in the abstract. For example, a proposal by Yunus puts rates above 15 percent over an institution's cost of capital into a profit maximizing "red zone" that should be prohibited by governmentally imposed caps.[47] While well intended, rates have more to do with operating costs than with profit. Tiny loans are expensive (relative to size) to make. Lenders, for example, find it much cheaper to make one $10,000 loan instead of one hundred $100 loans because the latter requires a hundred times the administrative work. A study by Adrian Gonzalez reveals that operating (63 percent) and financial (21 percent) costs make up 84 percent of every dollar of interest collected worldwide, leaving 7 percent to cover portfolio losses, 3 percent for taxes, and 6 percent for profits.[48] Gonzalez notes that eliminating all profit from microfinance would still leave 63 percent of borrowers paying red zone rates.[49] In fact, it turns out that about 75 percent of MFIs (both for-profit and nonprofit) fall within the red zone, so profit does not seem to be the major force behind rates.[50] Therefore, high interest rates in and of themselves are not tantamount to usury. A shocking 70 percent APR, for example, might represent little or no gain to the lender in high-cost contexts.

Other industry experts believe rates are too high, but oppose rate caps, fearing they will reduce the supply of credit by making lending unsustainable. Instead, they prefer competition and greater transparency to drive rates down.[51] Bolivia is a frequently cited case of how competition served to reduce rates from 75–80 percent twenty years ago to around 20 percent today.[52] Markets seem to be maturing and rates trending downward. David Roodman notes that in most countries with substantial microfinance industries and where data is available, "the Herfindahl-Hirschman index is below 25 percent, which is equivalent to having at least four big institutions of equal size."[53] Competition may also be growing in the form of conventional banks moving "down market" to serve previously ignored clients.[54]

As MicroFinance Transparency has pointed out, effective interest rates are often higher than stated rates because of additional charges/fees (mandatory savings, credit life insurance) and flat (vs. declining) interest calculation methods.[55] Thus, pricing data must be adjusted and/or other indicators must be used in order to gain a clearer picture of what clients actually pay. Using data provided by MicroFinance Transparency and adjusting for hidden costs, Roodman optimistically concludes, "about 80 percent of microloans cost 35% per year or less."[56] A Consultative Group to Assist the Poor (CGAP) study of gross portfolio yields (a rough measure of interest rates) indicated that rates had declined 2.3 percent per year from 2003–2006.[57]

The forgoing reasons seem to offer a strong argument on behalf of current interest rates. However, are high (and perhaps higher) rates justifiable if they are also used to provide returns to investors, even if socially motivated? Grameen charges a relatively low rate (approximately 20 percent) to borrowers, who also happen to be the primary owners of the bank. However, the Grameen model may be difficult to replicate. Operating costs vary widely across the globe. Furthermore, Roodman notes that although Grameen clients own 97 percent of the bank, their capital contributions only amount to $7.5 million, or $1.40 per member—far short of the amount needed for capitalization.[58] Grameen received subsidies in its early years but also took many years to achieve operational sustainability.[59] In contrast, many MFIs may need to accept commercially oriented funds and may need to charge higher rates to get to self-sufficiency in a shorter timeframe.

Even if all MFIs could be run under models of nonprofits or co-ops, some data suggests it might not make much of a difference. For example, a recent study finds that taken as a whole, nonprofit and for-profit microfinance institutions are indistinguishable as measured by rates charged.[60] Likewise, data from a CGAP study reveals that nonprofits are even more likely than for-profits to be in Yunus's "red zone."[61]

The studies above look at the entire industry, but individual cases of MFIs that possibly make large profits through usurious rates still need to be examined. The two best known (and most controversial) for-profits present a mixed picture. First, SKS Microfinance, the India-based organization issued a 2010 IPO and charged interest rates of 24 percent (32.4 percent APR), low by global standards and close to the mean charged by India's sixteen largest MFIs.[62] However, SKS's rates had also been steadily declining due to increases in efficiency.[63]

Second, in contrast, Compartamos has charged a rate close to 100 percent (much higher if calculated by APR) once Mexico's value-added tax is included, though their rates have also shown a decreasing trend in recent years, perhaps due to competition.[64] After operational costs and taxes, 22.6 percent of these charges went to profit margins.[65] Comparatively, return on average equity was high relative to other Mexican Banks, much higher than other *Microbanking Bulletin* benchmarked peer group MFIs, and on the high side compared to Mexican consumer lenders.[66] For their part, Compartamos's founders state they remain committed to the organization's social mission and that high interest rates and profit margins were necessary to prove a concept and appeal to commercial investors to fund its rapid growth.[67]

A broader 2011 study indicates that a small number of high-yield, high-return MFIs do exist.[68] However, their margins may be due to reasons other than exploitative interest rates. For example, in Southeast Asia, profits tend to be made by high volume rather than by high interest rates.[69]

As noted earlier, a critical question to ask is: What about the actual impact of loans and high interest rates on clients. Do loans with interest make borrowers worse off by trapping them in greater levels of debt? In theory, higher rates might increase debt burdens while lowering social impact (more money going to repay interest means less goes into microenterprises or to other beneficial uses).

To date, only a few rigorous studies of the actual impact of microfinance have been made public.[70] The studies found that while helping borrowers grow businesses, clients were not "lifted out of poverty," nor were women more empowered. Although the results fell short of the early promise, it would be inaccurate to call microfinance a failure as some headlines claimed.[71] According to the researchers themselves, "studies have shown sound evidence that [microfinance] allows many of the world's poorest people to develop businesses, insure against bad weather and health, maintain employment, and smooth consumption."[72]

To be sure, much caution should be used in generalizing from a handful of studies. The studies were conducted in specific contexts and used time frames that may have been too short to realize the true impact.[73] Moreover, they measured "average" effects, so some clients may have fared quite well. Microfinance may be a victim of the false expectations and hype created by a Nobel Prize and the rhetoric of early pioneers. In fact, some argue that microfinance is more accurately described as helping people "cope" with or "alleviating" poverty, rather than "curing it."[74]

With respect to the specific issue of high interest rates, no specific studies (to our knowledge) have compared outcomes for borrowers who receive higher rates with a statistically identical group receiving lower ones. However, several studies do indicate that microenterprises can often generate very high returns on additional capital.[75]

Another significant issue concerns nonenterprise loans. Several studies confirm that some borrowers apply their loans to "consumption smoothing" purposes such as school fees, medical bills, patching cash flow irregularities, and/or even general consumption.[76] These uses are inconsistent with the dominant narrative of microfinance and the potential for unbalanced risk between borrower and lender is greater.[77] While enterprise loans are more ideal, several practical realities should be acknowledged. Money is fungible, and substitution effects could occur (clients borrow less from other sources) so precise tracking/measurement is difficult.[78] Given the additional expense (MFI staff time) required for monitoring, rates would be even higher. Moreover, cash flow mismatches are common.[79] Thus, consumption smoothing might allow one to eat on a given day and/or treat an ailment, both of which could allow a client to focus on income generating activities. Some researchers question the wisdom and necessity of loan use restrictions as nonentrepreneurial loan uses have been found to be beneficial to clients.[80]

## Conclusion

High interest rates in microfinance, particularly those that serve private profit, present a challenging ethical issue. We have argued that while the broader narrative and principles of the ethical prohibitions against usury in the Bible are still relevant and applicable, they are more accurately applied to contemporary economic life through a narrative framework that requires improvisation or "analogical imagination" rather than as universal rules.

After looking at the factors behind high interest rates, what is currently known about the actual impact of microcredit on the lives of borrowers, a broad condemnation of present rates as "profiting on the backs of poor people" seems well intended but misguided. It seems that in many cases, rates are not usurious. In fact, a condemnation is potentially harmful if it diminishes funding for MFIs that are producing positive outcomes and/or if it reduces the availability of credit to those who can benefit from it. While private profit undoubtedly adds a new wrinkle into the equation, widespread profiteering seems far from the norm. Furthermore, there are currently no documented differences on the whole between the interest rates charged by for-profit MFIs and their nonprofit counterparts.

Rather than a general condemnation, a more cautious, case-by-case basis should be used. Given the combustible mix of financial institutions' seeking to earn income (whether to fund organizational sustainability or true private profit) and vulnerable clients, the potential for exploitation exists. Whether an organization is chartered as a for-profit or nonprofit, interest rates, other "business practices" (such as transparent pricing and client screening practices), and social impact should be examined.[81] That is, what is the net effect of their interest rate charges? Are benefits to the borrower "in balance" with what accrues to the lender? If high interest rates lead to higher levels of profit than conventional banking with an appropriate adjustment for risk and have an overall effect of further oppressing loan recipients and worsening their financial lives, then they can be properly seen as usurious. If, on the other hand, rates are high for legitimate reasons (high costs of delivery, risk, and some level of profit), loan recipients and their communities are better off (increase and/or smooth their incomes, goods and services made available, and so on) and clients can demonstrate high repayment rates without undue hardship, then the interest rates are better seen as just prices for valuable services. We can see, however, situations in which MFIs pursue sustainability and/or profitability could cause them to drift from their stated missions and abandon or mistreat clients who are poorer, as well as more-expensive-to-serve clients.

A much more difficult call is in the cases of the few organizations (e.g., Compartamos) that seemingly can lower their interest rates while still operating profitably enough to attract investor dollars for healthy growth. As of now, these cases are the rare exception but may increase along with the trend toward greater commercialization. Making an accurate assessment of these cases is challenging and requires a number of hypothetical renderings of what level of profits would entice capital markets, what constitutes healthy growth, the availability of alternative sources for funding (e.g., social investors willing to accept lower rates of return), and the desirability of such funding (because subsidized funding can create disincentives to mobilize savings, which seems to have proven social benefits). Yet interest rates of 100 percent or more (with a much higher APR) seem unnecessary and may have been harmful to existing clients.

Reducing interest rates is an objective amongst most microfinance practitioners. Newer efforts (such as the Smart Campaign and those of MicroFinance Transparency) to protect consumers through transparent pricing of loan products and better client screening to prevent adverse inclusion and overindebtedness, are badly needed measures to remedy abuses. Several organizations in India (Basix and Equitas) also voluntarily (and transparently) cap profit (vs. interest rates) by way of a limit on return on assets and/or a return on equity.[82] In conjunction with more frequent and better use of social performance measurement tools, competition, and technology, these practices may well be more promising and less damaging ways to drive rates downward than governmentally imposed caps, which blanket condemnations of high interest rates as usurious may encourage. Undoubtedly, profit seeking can work against the well-being of vulnerable people. Up to this point in the history of microfinance, however, usury seems more an exception than the rule.

## Notes

Scripture quotations are taken from the English Standard Version (ESV) unless otherwise noted.

1. Milford Bateman and Ha-Joon Chang, "Microfinance and the Illusion of Development: From Hubris to Nemesis in Thirty Years," *World Economic Review* 1 (2012): 13–36.

2. See Aneel Karnani, "Microfinance Misses Its Mark," *Stanford Social Innovation Review* (Summer 2007): 34–40, http://www.ssireview.org/articles/entry/microfinance_misses_its_mark; and Jonathan C. Lewis, "Microloan Sharks," *Stanford Social Innovation Review* (2008): 54–59, http://www.ssireview.org/articles/entry/microloan_sharks. See also Chuck Waterfield, "Making Microfinance Prices More Transparent," *CGAP* (blog), August 16, 2011, http://www.cgap.org/blog/making-microfinance-prices-more-transparent.

3. See Elisabeth Rhyne, *Microfinance for Bankers and Investors: Understanding the Opportunities and Challenges of the Market at the Bottom of the Pyramid* (New York: McGraw-Hill, 2009).

4. Muhummad Yunus, "Sacrificing Microcredit for Megaprofits," *New York Times*, January 14, 2011, http://www.nytimes.com/2011/01/15/opinion/15yunus.html?_r=0.

5. John Jewel, "Commentary on 1 Thessalonians 4:6 and 'A Paper on Usury,'" *Journal of Markets & Morality* 15, no. 1 (Spring 2012): 287.

6. For further discussion of definitional issues, including historical perspective, see Eric Kerridge, *Usury, Interest and the Reformation* (Burlington: Ashgate, 2002).

See also Constant J. Mews and Ibrahim Abraham, "Usury and Just Compensation: Religious and Financial Ethics in Historical Perspective," *Journal of Business Ethics* 72 (2007): 1–15.

7. Muhummad Yunus, *Banker to the Poor* (New York: Public Affairs, 1999).

8. See http://www.grameen-info.org.

9. SKS, ASA, and BRI are some of the other large organizations. Each serves four to six million clients. BRI has an outstanding loan portfolio of approximately $6 billion. For more statistical information about microfinance organizations, see http://www.mixmarket.org.

10. Larry Reed, "2011 State of the Microcredit Summit Campaign Report," *Microcredit Summit Campaign*, 2011, http://www.microcreditsummit.org/SOCR_2011_EN_web.pdf.

11. See Rhyne, *Microfinance for Bankers and Investors*.

12. Michael Chu, "Profit and Poverty: Why It Matters," *Forbes*, December 20, 2007, http://www.forbes.com/2007/12/20/michael-chu-microfinance-biz-cz_mc_1220chu.html; Michael Chu, Richard Rosenberg, and Muhummad Yunus, "Is It Fair to Do Business with the Poor?" (transcript) *World Microfinance Forum Geneva* (October 2009).

13. Elisabeth Rhyne, interview in *Microfinance Distance Learning Course* by Heather Clark (New York: United Nations Capital Development Fund, 2002).

14. Chu, Rosenberg, and Yunus, "Is It Fair to Do Business with the Poor?"

15. Yunus, "Sacrificing Microcredit for Megaprofits."

16. Karnani, "Microfinance Misses Its Mark."

17. Brigit Helms, *Access for All: Building Inclusive Financial Systems* (Washington, DC: The World Bank, 2006).

18. See Yunus, "Sacrificing Microcredit for Megaprofits."

19. While the weight and relative authority granted to the Bible (usually in conjunction with church tradition, reason, and human experience) varies across subtraditions and denominations, the vast majority of Christians look to Scripture as either normative content, form, or both for ethical guidance. The proper use of the Bible in Christian ethics is one of lengthy debate and is far beyond the scope of this article. For more on this debate, we suggest: Richard Hays, *The Moral Vision of the New Testament: Community, Cross, New Creation, A Contemporary Introduction to New Testament Ethics* (New York: HarperOne, 1996); R. C. Sproul, *Scripture Alone: The Evangelical Doctrine* (Phillipsburg: P&R Publishing, 2005); or for a broad overview,

Kevin Vanhoozer, ed., *Dictionary for Theological Interpretation of the Bible* (Grand Rapids: Baker Academic, 2005).

20. To be certain, few biblical scholars would support a position that civic laws given in the Old Testament are directly binding today in their given form. However, most would acknowledge that Old Testament laws and commands reflect and/or illustrate broader principles and/or a larger story/moral orientation.

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22. James Strong, *The New Strong's Exhaustive Concordance of the Bible* (Nashville: Thomas Nelson Publishers, 1990), 614.

23. Childs, *The Book of Exodus*, 451.

24. Childs, *The Book of Exodus*, 479.

25. Gerard Von Rad, *Deuteronomy: A Commentary* (Philadelphia: Westminster Press, 1996), 148.

26. Benjamin Nelson, *The Idea of Usury: From Tribal Brotherhood to Universal Otherhood* (Chicago: University of Chicago Press, 1969).

27. William C. Wood, "Subprime Lending and Social Justice: A Biblical Perspective," *Journal of Markets & Morality* 11, no. 2 (Fall 2008): 192.

28. Thomas Divine, *An Historical & Analytical Study in Economics & Modern Ethics* (Milwaukee: Marquette University Press, 1959), 27.

29. James Halteman, *Market Capitalism and Christianity* (Grand Rapids: Baker Book House, 1988), 40.

30. Christopher A. Franks, *He Became Poor: The Poverty of Christ and Aquinas's Economic Teachings* (Grand Rapids: Eerdmans, 2009), 104.

31. Kerridge, *Usury, Interest and the Reformation*, 32.

32. Presbyterian Church USA, "A Reformed Understanding of Usury for the Twenty-First Century," 2006, p. 5, http://www.pcusa.org/site_media/media/uploads/_resolutions/usury.pdf.

33. Moses Finley, *The Ancient Economy* (Berkeley: University of California Press, 1973), 141, cited in Craig Blomberg, *Neither Poverty nor Riches: A Biblical Theology of Material Possessions* (Grand Rapids: Eerdmans, 1999), 90–91.

34. See Blomberg, *Neither Poverty nor Riches*, 91.

35. Edd S. Noell, "A 'Marketless World'? An Examination of Wealth and Exchange in the Gospels and First-Century Palestine," *Journal of Markets & Morality* 10, no. 1

(Spring 2007): 85–114. See also, K. C. Hanson and Douglas E. Oakman, *Palestine in the Time of Jesus: Social Structures and Social Conflicts* (Minneapolis: Fortress Press, 1988); and John R. Schneider, *The Good of Affluence: Seeking God in a Culture of Wealth* (Grand Rapids: Eerdmans, 2002).

36. Craig Blomberg, "Neither Capitalism nor Socialism: A Biblical Theology of Economics," *Journal of Markets & Morality* 15, no. 1 (Spring 2012): 208; Blomberg, *Neither Poverty nor Riches*, 90–91; and Bruce J. Malina, *The New Testament World: Insights from Cultural Anthropology* (Atlanta: John Knox, 1981), 71–93.

37. John T. Noonan Jr., *A Church That Can and Cannot Change: The Development of Catholic Moral Teaching* (Notre Dame: University of Notre Dame Press, 2005), 131.

38. Stuart Rutherford et al., "Clients," in *The New Microfinance Handbook: A Financial System Approach*, ed. Joanna Ledgerwood, et al. (Washington, DC: World Bank Publications, 2013), 49.

39. Monique Cohen and Deena Burjorjee, "The Impact of Microfinance," *CGAP Donor Brief* No. 13, July 2003, http://www.docstoc.com/docs/57939016/The-Impact-of-Microfinance.

40. Daryl Collins et al., *Portfolios of the Poor: How the World's Poor Live on $2 a Day* (Princeton: Princeton University Press, 2009).

41. For more on narrative ethics within the Christian theological tradition, see Gordon Wenham, *Story as Torah* (Grand Rapids: Baker Books, 2004); and Bernard Adenay, *Strange Virtues: Ethics in a Multicultural World* (Downers Grove: IVP Academic, 1999).

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49. Gonzalez, "Sacrificing Microcredit for Unrealistic Goals."

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52. See Chu, Rosenberg, and Yunus, "Is It Fair to Do Business with the Poor?"; Helms, *Access for All*.

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54. Robert Cull, Asli Dimurguc-Kunt, and Jonathan Morduch, "Financial Performance and Outreach: A Global Analysis of Leading Microbanks," *Economic Journal* 117 (2007): 517.

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63. Micro-Credit Ratings International, 2011, http://www.m-cril.com/.

64. David Roodman, "Does Compartamos Charge 195% Interest?" *Center for Global Development* (blog), January 31, 2011, http://blogs.cgdev.org/open_book/2011/01/compartamos-and-the-meaning-of-interest-rates.php.

65. Richard Rosenberg, "CGAP Reflections on the Compartamos IPO," *CGAP Focus Note* no. 42 (June 1, 2007), http://www.cgap.org/p/site/c/template.rc/1.9.2440/.

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67. Chu, "Profit and Poverty: Why It Matters"; Carlos Danel and Carlos Labarthe, "A Letter to Our Peers," *Compartamos Banco*, 2008.

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70. In the past, anecdotal and nonrigorous studies had been used as major sources of evidence for the impact of microfinance interventions on the lives of clients. More recently, several well-publicized random control/counterfactual studies were made public. See Abhijit V. Banerjee et al., "The Miracle of Microfinance? Evidence from a Randomized Evaluation," *MIT Abdul Latif Jameel Poverty: Action Lab Working Paper*, 2009; Pascaline Dupas and Jonathan Robinson, "Savings Constraints and Microenterprise Development: Evidence from a Field Experiment in Kenya," Working Paper 14693, *National Bureau of Economic Research*, 2009; Dean Karlan and Jonathan Zinman, "Expanding Microenterprise Credit Access: Using Randomized Supply Decisions to Estimate the Impacts in Manila," *Financial Access Initiative and Innovations in Innovations for Poverty Action Working Papers*, 2009; and Dean Karlan and Jonathan Zinman, "Expanding Credit Access: Using Randomized Supply Decisions to Estimate the Impacts," *Review of Financial Studies* 23, no. 1 (2010): 433–64.

71. See, for example, Drake Bennett, "Small Change: Does Microlending Actually Fight Poverty?" *Boston Globe*, September 20, 2009.

72. Banerjee et al., "Microcredit Is Not the Enemy."

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75. See Karlan and Zinman, "Expanding Credit Access." The researchers examined high interest (200 percent or more) consumer (not true microfinance, per se) loans by a for-profit organization in South Africa and found positive effects on employment, income, and food consumption. See also Abhijit Banerjee and Esther Duflo, "Growth Theory through the Lens of Development Economics," Unpublished Paper, 2004; Christopher Udry and Santosh Anagol, "The Return to Capital in Ghana," *American Economic Review* 96, no. 2 (May, 2006): 388–93; David McKenzie and Christopher Woodruff, "Experimental Evidence on Returns to Capital and Access to Finance in Mexico," *The World Bank Economic Review* 22, no. 3 (2008): 457–82.

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77. For a discussion of "shared risk," see John Jewel, "A Paper on Usury," 308.

78. See Joanna Ledgerwood, ed., "Measuring Financial Inclusion and Assessing Impact," in *The New Microfinance Handbook: A Financial Market System Perspective* (Washington, DC: The World Bank, 2013), 136.

79. As the authors of *Portfolios of the Poor* point out, cash flow mismatches are common. Just because people live on "two dollars a day," does not mean they have two dollars every day. This is an average amount over time. See Collins et al., *Portfolios of the Poor: How the World's Poor Live on $2 a Day* (Princeton, NJ: Princeton University Press, 2009), 2.

80. Karlan and Zinman, "Expanding Credit Access"; Collins et al., *Portfolios of the Poor*.

81. Efforts to measure and report on the social impact of individual MFIs are gaining much traction. A number of "social performance" metrics (including ones developed

by CERISE and Accion) have been developed and a task force with membership representing many organizations has been operating to move the conversation forward. See http://SPTF.info. The Mixmarket also recently began reporting MFI social performance in addition to financial performance.

82. See Roodman, "Does Compartamos Charge 195% Interest?" (blog), January 31, 2011, http://www.cgdev.org/blog/does-compartamos-charge-195-interest.