



# Impact of Access to Microcredit on the Well-Being of Households and Poverty Change in Cameroon: 2001-2007

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## Abstract

Using data from the second and third Cameroonian household surveys, this study analyzes the relationship between access to microcredit, household well-being, and poverty change in Cameroon. It uses a combination of two methods of analysis: the instrumental variable method for controlling the potential endogeneity of access to increased microcredit by correcting for selection bias; and a method for breaking down poverty change into intra-growth, intra-redistribution, and inter-sector mobility components based on Shapley's value. The latter is based on comparison of evidence-based and hypothetical/non-factual distributions. The key findings reveal that access to microcredit: (i)

significantly and positively affects the level of well-being of households and financial inclusion, particularly through education; (ii) has an impact on poverty change and that this effect is brought about by the redistribution component and primary sector; (iii) positively and significantly influences the intra-sector redistribution component of poverty change through the intra-sector growth and mobility components.

## Introduction

In most cases, developing countries are faced with risks that can affect both economic activity and household behaviour. These risks can be climatic (natural disasters), social (conflicts) and economic (economic crises). In the face of such shocks, households may be exposed to situations of vulnerability or persistent poverty to the extent that loss of employment and interruption of income-generating activities are often inevitable (Dercon, 2002). In such situations, households' incomes and their asset portfolios will decline considerably. As a means of ensuring their socio-economic security, households will seek to maintain their income levels and sustain their consumption over time. They will then develop survival strategies based on, among other things, savings, child labour and credit or borrowing (Fafchamps, 2002). With consumption levels being stable, these strategies will then permit households to maintain their level of well-being.

Among these strategies, credit-based strategy, particularly microcredit, is increasingly being adopted by the poorest households. The various international summits on microcredit have made it possible to highlight the simplicity of their use and their effectiveness, especially regarding collateral issues. Indeed, the poorest segment of the population is very often faced with lack of collateral in their search for credit from conventional banks (Otéro, 1989). In this respect, several developed countries consider microcredits as an innovative and easy-to-implement instrument to combat poverty. These countries have consequently adopted microcredits as a privileged tool to help households cushion their consumption during periods of crisis.

Credit is one of the flagship strategies that can enable households to maintain or smoothen their level of consumption over time and thus protect themselves against poverty. To this end, the policy on credit lending and, more specifically, lending of small amounts of credit (microcredits) to poor households has spread throughout the world. Poverty is understood here as a complex phenomenon generally referring to a lack of resources and a deprivation of choices and opportunities that would offer individuals decent living conditions (UNDP, 1998).

The role played by microcredit in poverty reduction has been the subject of several controversies in the economic literature. Indeed, several studies have shown that microcredits can be effective tools for improving households' living conditions in both

developed and developing countries. In this context, microcredits are an important instrument for achieving the Millennium Development Goals by financing the projects of the poor (Littlefield et al., 2003; International Monetary Fund, 2010). To this end, Roedenbeck (1998) points out that microcredit programmes are successful in the Middle East and Africa. Similarly, many studies have shown, in the case of Cameroon, the positive effect of microcredit on poverty reduction (Tchouassi and Tekam, 2003; Epo, 2013; Sikod and Baye, 2013).

Indeed, formal credit systems through microfinance enable households to engage in small businesses such as handicrafts and provide for the basic needs of their families (Gentil and Servet, 2002). Moreover, informal credit through tontines, for example, often permits women to finance their children's education through quasi-annual savings.

However, income generated from loans is not always used to finance income-generating projects, but rather for consumption (buying of goods, for example) and savings. For instance, Stiglitz and Weiss (1981) described the behaviour of bad borrowers in the credit market. Indeed, banks have incomplete information about the risks associated with the loans they provide. On the other hand, borrowers know perfectly well the probability of success of their projects. To reduce the likelihood of running into bad debt, lenders will offer high interest rates, but these rates may drive away good borrowers. Only the bad customers will stay on the market (anti-selection). In the same way, bad borrowers will take advantage of the information asymmetry of creditors to develop opportunistic behaviour (moral hazard). This can mean that borrowers use their loans for non-investment purposes.

Just like banks, microfinance institutions (MFIs) can also suffer the consequences of information asymmetry vis-à-vis borrowers. These consequences may include the non-use of MFI loans for investment purposes or the inability of the borrower to implement an income-generating project. Such a situation can lead to insolvency of households and, as a result, their resilience in a state of poverty (Falcucci, 2012). Similarly, the absence of securities in MFIs' credit lending policies can drive the poorest households into a situation of over-indebtedness (Morduch and Haley, 2012), as there seems to be a race for this type of credit on the part of these households.

To this day, many countries around the world continue to suffer the agony of poverty. Over the years, this plight has persisted and increased among most of these countries, leading to increased inequalities both within and between countries.

Africa is the hardest hit continent by the poverty pandemic. Like most African countries, Cameroon is suffering the consequences of poverty. Its economic activity has experienced a major slowdown with a decline in wages following the drop in international price of oil that occurred in the 1980s. These shocks were followed by

introduction of the structural adjustment programme, and devaluation of the currency in the mid-1990s. Most enterprises were liquidated or privatized. The Cameroonian state then cancelled subsidies as a matter of policy. The general price level rose and the economic situation in the country caused many households to become unemployed or to cease economic activities. This situation led to a drastic drop in the level of household consumption. However, as economic operators do not like fluctuations in their consumption (Begg et al., 2002), Cameroonian households then turned to the informal sector through small businesses to stabilize their consumption. Moreover, to finance these small businesses, households needed recourse to associations.

Cameroon then initiated fundamental measures such as joining the structural adjustment programme. This was intended to rebuild its economic structure (Chauvin, 2012). Despite this and many other measures, the standard of living of the population continued to deteriorate. However, between 2001 and 2007, the country experienced a reduction in poverty rate from 40.1% to 39.9%.

In the light of this situation, the Cameroonian government, in its Growth and Employment Strategy Paper (GESP), developed a credit-based policy to finance its economy. However, the banking restrictions forced the government to embark on a process of liberalizing the financial sector, which led to a surge in the number of microfinance institutions in the early 1990s. This was followed by a national policy for the development of the financial sector.

The number of microfinance institutions increased from 192 in 2001 to 460 in 2007 (COBAC, 2008). In 2000, the total savings mobilized by microfinance institutions (MFIs) in Cameroon amounted to FCFA<sup>1</sup> 35.9 billion or 6% of the savings collected by the banking sector. During the same year, more than FCFA 25.4 billion was distributed by these institutions in the form of loans, representing 4.3% of the total amount of loans disbursed by the banking sector (COBAC, 2001). Furthermore, according to the Global Findex - Cameroon (2014), 12% of the population has an account in a formal MFI; 2% of the latter have benefited from credit and 8% hold savings in these institutions. At the end of 2010, there were nearly 509 MFIs and 1,500,000 clients. Over the same period, MFIs mobilized FCFA 454 billion in deposits and issued FCFA 240 billion in loans (CGAP-Cameroon, 2017).

Given the description of the situation of Cameroonian households, it emerges that households are faced with the problem of maintaining their level of consumption between two periods: growth period and post-crisis period (oil crises, devaluation of the CFA Franc and adoption of structural adjustment programmes). Similarly, at the theoretical level, the analysis of this type of consumption behaviour is theoretically premised on the life cycle and permanent income assumptions.

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1 Franc – currency of the West African Financial Community.

## Methodology

The theoretical model underpinning our approach is that of the timeless consumption function. Indeed, we hypothesize that households seek credit when faced with crises to maintain their level of consumption over time and ensure their security. The problem that these households must therefore solve is that of maintaining timeless consumption. The theoretical function considered in our model is the timeless consumption function. As noted above, our analysis assumes of life cycle and permanent income. According to Romer (1997), the Hall (1978) model tests this hypothesis. In doing so, Hall (1978) concludes that the consumption function follows a random path. If income is accurate and consumers make rational predictions, it is not possible to predict consumption over time.

## Conclusion and recommendations

In summary, the aim was to empirically assess the relationship between microcredit, household well-being and change in poverty in the case of a developing country such as Cameroon. The impact of microcredit on household well-being was determined using Ordinary Least Squares, Double Least Squares and Double Least Squares Sample Correction. The Double Least Squares method was found to be adequate for studying this relationship compared to the other methods used. The study on household access to microcredit regarding poverty level was carried out based on non-factual analysis using the Shapley analysis with respect to growth, redistribution, and mobility components. Therefore, the results of the study show that microcredits have a positive and significant effect on poverty reduction both in aggregate, and at the level of various sectors of economic activity.

## Recommendations

Based on results obtained from the econometric approach and the Shapley analysis conducted in our study, we recommend the following:

- Microcredit institutions in the country should be promoted for their growth and expansion. The existence of many microcredits should make it easier for even the poorest segment of the population to have access to small loans.
- Given that the primary sector employs individuals who are predominantly from the rural areas, and despite the fact that this sector is much more affected by poverty, it contributes largely to poverty reduction and has a multiplier effect on the other sectors. To this end, a policy promoting the proximity of microfinance institutions should be encouraged in rural areas. Consequently, access to

microcredit for rural actors will facilitate an increase in agricultural production through the acquisition of agricultural inputs and diversification of crops.

- Access to microcredit must also be directed towards the secondary sector to finance groups with common interests, small and medium-sized enterprises specializing in the production and processing of local products. These micro-enterprises will be able to compete with foreign firms and absorb domestic demand.
- Policies aimed at providing access to microcredit must be geared towards the idea of redistributing credit to many poor people by increasing the volume of credit to those who previously benefited from it.
- Support and training policies for the beneficiaries of credit should be promoted to improve their entrepreneurial capacity and enable them to implement projects.
- Policies providing easy access to education and health must also be implemented in rural areas, since these elements are the most favourable factors for the well-being of households.

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