

## What Makes a Credit Group Tick?

In-group favouritism among microfinance clients



How is in-group solidarity created?  
Photo: Aslak Orre

Microcredit clients are often assigned to credit groups with joint liability for loans. But what makes a credit group work well? What credit groups are likely to generate the internal social dynamics needed for group solidarity to form and repayment to happen? This is a matter of both group dynamics and individual characteristics, as some individuals conform more easily to in-group norms. This brief presents an experiment conducted among microcredit clients in Angola. The results suggest that more educated clients and female clients are more likely to favour members of their credit group over outside demands.

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Poor people often cannot put up collateral for loans. A key idea in the microfinance industry is that social pressure can be used to induce repayment in the absence of collateral. By assigning microcredit clients to credit groups with joint liability, individual clients are given an incentive to repay loans through social pressure from other group members. But credit groups clearly differ in their ability to enforce repayment. Why? One explanation is that some groups are able to nurture norms of in-group solidarity, increasing the inclination of members to give priority to other group members over outsiders. But when are such norms likely

to form? What makes microcredit clients susceptible to norms of in-group solidarity?

In the spring of 2010, CMI in cooperation with Development Workshop (DW) conducted an economic experiment among microcredit clients in Luanda, Angola. Participants were drawn from the client pool of Kixicredito, the largest non-commercial microcredit institution in Angola. Kixicredito clients are organized in credit groups consisting of 10-30 clients, with joint liability for loans. The groups are called solidarity groups, and meet bi-weekly for group

business and to build group cohesion. In total, 539 clients representing 51 solidarity groups participated in the experiment.

The experiment took the form of a dictator game. In this game, each participant (or dictator) was given 500 Angolan Kwanza (about 5.4 USD at the time of the experiment), and told that he could keep the money or give some or all of it to a recipient. The decision was anonymous in the sense that the recipient would not know the identity of the dictator, nor would the dictator know the identity of the recipient. The game was played in two versions. In the first version, the recipient was a fellow credit group member of the dictator. In the second version, the recipient was not a member of the dictator's credit group.

The fact that real money is used in the experiment means that participants face a real decision that affects them personally, as opposed to hypothetical survey questions. The fact that the decision was anonymous means that decisions are not influenced by strategic considerations, such as fear of being punished by the recipient in future interactions.

What do the choices of the participants in this game tell us? Completely rational, self-interested participants would keep all the money, giving nothing to recipients in either version of the game. If a positive amount is given, we can take this as an indication of altruistic or egalitarian preferences, the

participant cares not only about his own payoff but also that of the recipient. If a participant gives more to a fellow credit group member than to an outsider, we can take this as an indication of in-group favouritism or solidarity. In other words, it suggests that a participant places greater emphasis on the situation of a fellow group member compared to a stranger.

What makes microcredit clients susceptible to norms of in-group solidarity?

So what did the participants choose to do with the money? Figure 1 displays the decisions of the participants. The blue bars on the left capture the amounts given to a fellow group member. For each possible amount from 0 to 500 Kwanza (horizontal axis) the bars indicate the number of participants choosing to give this amount (vertical axis). The red bars similarly capture the amounts given by participants to recipients outside their credit group.

The graphs tell us two things. Firstly, a large proportion of participants gave away none of the money in either version of the game. Keeping all the money was in fact the most common decision, taken by 28 per cent of participants in the first version of the game

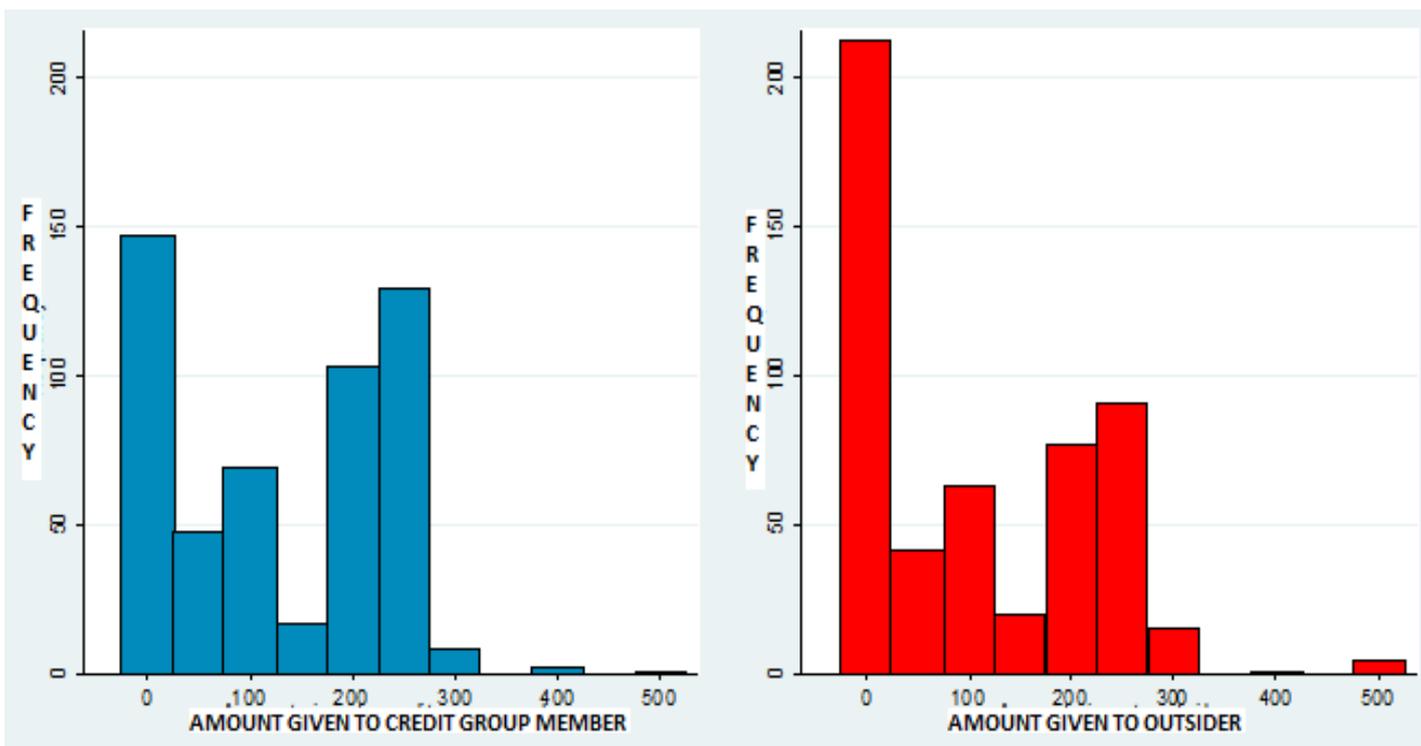


Fig. 1. Amounts given in the dictator game



Female entrepreneur  
selling food in Luanda  
Photo: Arne Wiig

and 41 per cent in the second. A substantial share of the participants can hence be characterized as self-interested. The rest, however, gave away some or all of the money, exhibiting altruism or egalitarianism. The second most common decision was to give half the money to the recipient, a not uncommon pattern in these types of games.

Secondly, comparing the blue and red graphs tells us that participants gave away more money to fellow credit group members than to outsiders. The average amount given to a fellow group member was 131 Kwanza, whereas the average amount given to an outsider was 107.5 Kwanza. This suggests that participants have an in-group bias, they tend to treat members of their credit group more favourably than non-members.

There is considerable variation in the degree of in-group favouritism exhibited by different individuals, however. Some of this variation is explained by differences between credit groups, likely reflecting their composition and dynamics. Individual characteristics also affect the degree to which a participant favoured in-group members, sometimes in surprising ways.

More highly educated participants favoured in-group members to a greater extent. The more years of education a client has, the greater was the amount given to a fellow group member compared to the amount given to an outsider. This is a striking result, as education is often believed to broaden the perspectives of people, making them less

likely to favour their own narrow social group. We find the opposite to be the case. Whether this is a finding that generalizes beyond the Angolan context is an open question. It is possible that the large economic and social inequalities in Angola have generated a schooling system which highlights in-group considerations. But this needs further study.

Women favoured their own credit group more than men. The results indicate that this difference is large. The difference between amounts given to fellow group members and to outsiders is on average 50 Kwanza greater for female participants than for male ones. This is in line with results from other studies suggesting that women are more susceptible to in-group norms than men.

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Family background and social networks are also related to the degree of in-group favouritism shown by participants. Participants whose father spoke more languages, and who had access to newspapers in the home during childhood, showed

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less in-group favouritism. It is possible that this reflects family socialization, where growing up in a home with more universalist inclinations rubs off on a person. Participants who knew the manager of a local NGO also demonstrated less in-group favouritism. This may again reflect socialization, having access to a social network of this kind may influence views in a universalist way. However, our methodological approach does not permit us to conclude that the effects of family background and social networks are causal effects. For instance, the relationship between knowing the manager of an NGO and in-group preferences may reflect reverse causality, where a person with universalist perspectives is more likely to seek out and be accepted into a network of this kind.

What does all this tell us about which credit groups become closely knit? Group composition and/or dynamics matter. However, controlling for group differences, we also find that some individuals are more susceptible to norms of in-group solidarity than others. More educated clients and female clients prioritize in-group demands more strongly over outside demands. There are also possible effects of family background and social networks which need to be explored further.

## On the Mechanics of Microfinance

Knowing how credit groups work, what makes them tick, is important to make microcredit programmes effective in addressing poverty. Microcredit institutions can benefit from increased knowledge on client selection and group integration.

The joint CMI-DW project provides an important starting point for addressing these issues, which will be further analyzed in a second round of cooperation in the period 2011-14.

In addition, the dynamics of microcredit is the topic of a large research programme recently granted funding by the Research Council of Norway.

This programme, called On the Mechanics of Microfinance, is a collaboration between researcher at CMI and the Norwegian School of Economics and Business Administration.

FOR MORE INFORMATION VISIT  
THE CEIC-CMI COOPERATION  
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