

# Intermediated Loans: A New Approach to Microfinance\*

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Work in Progress: Comments Welcome

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### Abstract

This paper studies a variation on traditional microfinance, where a microfinance institution appoints local intermediaries (traders, lenders or local government representatives) to help select borrowers eligible for individual liability loans. The loans are of longer duration (4 month repayment cycles) compared to standard microfinance loans and are designed to help finance agricultural working capital needs. There is no peer monitoring and it avoids costly weekly meetings or savings requirements. Repayment incentives are provided by linking eligibility to future loans on a larger scale to current loan repayments. Loan intermediaries are incentivized via commissions based on loan repayments. We report from results of a field experiment with two versions of intermediated lending that vary with respect to the agent appointed as the intermediary. In TRAIL a local trader/lender is appointed as a loan intermediary while in GRAIL the local government is requested to appoint the intermediary. The experiment is conducted with farmers in 72 villages in West Bengal, India, with group-based joint liability loans (GBL) serving as a control group. This paper reports on patterns of selection of clients, loan take-up rates and repayment rates in the first year. TRAIL achieved the highest repayment rates (exceeding 95%, significantly higher than under GBL). All three approaches experienced similar take-up rates (exceeding 80%). TRAIL and GRAIL agents tended to exhibit a bias in favor of borrowers with intermediate landholdings, those with whom they have extensive past dealings and those with similar occupation, caste and religion. GBL in contrast was biased in favor of landless households, and did not exhibit any biases based on occupation, caste and religion. We develop and test a theoretical model in order to interpret these results. Relative impacts on borrower cultivation, incomes and assets is deferred to a subsequent paper since the experiment is still ongoing.