

Microfinance and rural non-farm employment in developing countries

Expansion of microfinance to rural areas may reduce credit constraints, helping non-farm sector growth, employment, and development

Keywords: microfinance, non-farm employment, developing countries

ELEVATOR PITCH

The rural non-farm sector plays an important role in diversifying income for rural households in developing countries and has the potential to emerge as a major source of employment. In some cases it has outgrown the agricultural sector, in part due to the expansion of credit through microfinance institutions that are supported by governments, donor agencies, and businesses. However, future expansion of the rural non-farm sector requires increased flexibility in credit contracts, as well as decreasing the cost of credit and the delivery of complementary inputs, e.g. skills training.

KEY FINDINGS

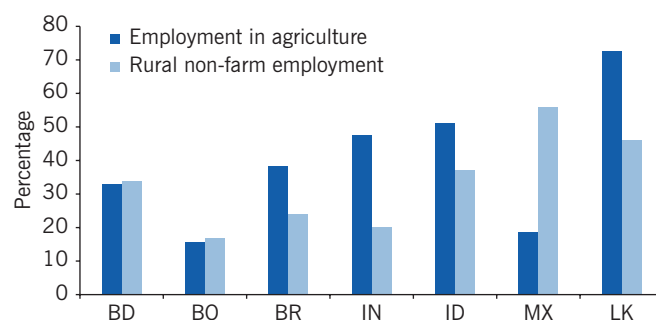
Pros

- ⊕ Rural non-farm enterprises can help absorb growing labor forces in many developing countries.
- ⊕ Rural non-farm enterprises can be very profitable; injections of new capital often result in high returns.
- ⊕ Evidence suggests a strong association between rising rural non-farm employment and a decline in poverty.
- ⊕ Expansion of microfinance alternatives that do not require collateral for loans and target poorer households may help the poor to engage in rural non-farm employment.

Cons

- ⊖ In the absence of credit and other complementary services, rural non-farm employment is often of low productivity.
- ⊖ Owners of rural non-farm enterprises, especially female owners, frequently use unpaid family labor, which may lead to overstated profits.
- ⊖ The non-farm sector is heterogeneous in terms of productivity and quality of employment; its expansion may increase inequality.
- ⊖ Microfinance can be inflexible, requiring frequent (e.g. weekly) and almost immediate loan repayment.
- ⊖ Microfinance institutions typically charge high interest rates and may not offer credit to men.

Employment in agriculture and rural non-farm sectors



Source: ILO. Key Indicators of the Labour Market database. Online at: <http://www.ilo.org/global/statistics-and-databases/research-and-databases/kilm/lang--en/index.htm>; [1].

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AUTHOR'S MAIN MESSAGE

Public policy should support expansion of the rural non-farm sector as a means of combating poverty. This sector—often neglected by policymakers—helps absorb growing rural labor forces in developing countries by providing employment to the rural poor. A policy option for stimulating the rural non-farm sector is the provision of credit through microfinance institutions and commercial banks at reasonable interest rates to the rural poor. Complementary services, such as targeted training programs and linkages to urban markets can further enhance efforts to expand the sector.