

The Relevance and Meaning of Charity in the Context of Micro-finance

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Abstract

Microfinance is a sector which often balances on the business-charity border. In this paper I claim that it is necessary to clearly distinguish between charitable and commercial forms of microfinance. The issue is especially important for (potential) donors to MFIs which rely on fundraising to finance their operations. I therefore propose theoretical parameters for charitable microfinance institutions (MFIs) and for the identification of charitable products: in this proposal, I define such institutions and products based mostly on a so-called normal profit criterion. Due to the difficulty of objectively calculating the level of normal profit, I suggest approximating the level of normal profit in microfinance based on the average prices of products in the commercial banking sector, as well as using other (country-specific) criteria. I also propose a system of product certification for charitable MFIs and charitable microfinance which is aimed at simplifying orientation in the microfinance sector, mainly for donors, but also for clients and other stakeholders.

Key words: Charity in business, charitable microfinance, charitable microcredits, poverty alleviation

Introduction

The failure of conventional financial institutions to provide financial services to poor people is a major reason for the emergence of the microfinance movement. So-called microfinance institutions (MFIs) have enabled access to financial services for more than 200 million people in developing countries (Maes and Reed 2012, 3). The financial services provided by MFIs are loans, saving products, financial transfers and insurance. Some MFIs also provide education oriented to skills necessary for business.

Leaders of the microfinance movement declare that poverty reduction is their mission and that financial sustainability is a key essence for sufficient range of services provided by MFIs (see for example Yunus 2008; Akula 2010). However, many MFIs have been diverted from their declared mission because of the overemphasis on financial sustainability (Hermes et al. 2011; Serrano-Cinca and Gutiérrez-Nieto 2014). Symptoms of mission drift include the provision of services mainly to lower middle-class people and the charging of high interest rates and fees (Karim 2011; Bateman 2010; for conceptualization of mission drift see for example Armendariz and Szafarz 2011)

Drifted organizations often ask the general public for financial contributions and label themselves and their products as being charitable or primarily aimed at benefit-

ing people. Microfinance NGOs which have transformed themselves into openly profit-driven companies after many years of being financed by altruistic donors have also caused controversy: one of the most famous cases is Mexican Banco Compartos (see for example Cull et al. 2009, 1-3). Both situations are unacceptable, therefore it is necessary to distinguish between charitable MFIs which maintain a strong social mission, and other MFIs.

There are initiatives, such as the SPTF network, which measure the social performance of MFIs. Incofin ECHOS©, developed by Dewez and Neisa (2009) and the Social Performance Index, developed by CERISE (see Bedécarrats 2011), are examples of composite indices which measure social performance and are used in academic literature. Microfinance organisations also have internal systems to measure the quality of their microfinance services. However, these initiatives, indicators and systems do not focus primarily on the issue of charitableness. In contemporary mainstream microfinance, the idea of social business is at the heart of discussions. According to a well-known definition from Muhammad Yunus, the objective of social business is to overcome poverty, or one or more problems which threaten people and society. Financial and economic sustainability is also a central theme of social business. Famous proponents of the term *social business* in microfinance, such as the Grameen Bank, refuse any subsidies or gifts. Those social businesses which accept subsidies and gifts aim to reach sustainability and to stop accepting them.

However, some organisations have a much clearer focus on helping the poor and much less (or no) emphasis on reaching financial sustainability. Although these organisations are a small minority in the microfinance movement, they do exist¹, and it makes sense to distinguish them from both commercial and social business microfinance organisations by labelling them *charitable microfinance*. Such a distinction would be useful, especially for altruistic donors.

Methodology

In this paper I propose some basic parameters for a system of product certification for charitable MFIs and charitable microfinance organisations. The aim is to simplify the orientation in the microfinance sector for donors, clients and other stakeholders. The first part of the paper focuses on the history of microfinance, with a special emphasis on the charitableness of MFIs. The relevance of distinguishing a charitable microfinance from business microfinance is also discussed, using the example of MFIs. The second part of the paper defines charity in the context of businesses built on a concept of normal profit. A proposal for framework parameters for charitable microcredits and charitable MFIs, and the basic details of a system for their certification are introduced in the third part. Although the proposal is, in principle, derived from the theoretical discussion in the second part of the paper, it also considers the specifics of microfinance and selected practical issues.

The first part of the paper is based on the literature review. Existing literature related to the researched issue is collected and analysed, such as the historical development of microfinance as a charitable tool. The second and third parts of the paper combine the literature review with logical argumentation (deductive and inductive approaches) and critical discussion. The literature has been collected from multiple media sources, such as academic journals, books, legal documents, government publications, etc. The paper thus contributes to an understanding of the current status of microfinance and charity and identifies some of their problems. Logical argumentation and critical discussion are used to define core concepts such as charity and charitable microfinance and to propose solutions needed in the microfinance industry.

The History and Presence of Microfinance as a Charitable Tool

Bangladeshi professor Muhammad Yunus is often seen as the founder of modern microfinance. In the 1970s, Yunus experimented with the provision of loans to poor people in Jobra village and subsequently founded the famous Grameen Bank. Its systems and its philosophy of financial sustainability was then replicated by MFIs all around the world. But the idea of helping the poor by providing them with cheap loans is much older. It had already appeared in the late Middle Ages and mainly came from the church.

According to Benigni (1913, 535), at the beginning of 14th century the French bishop Guillaume Durand de Saint-Pourçain suggested that city councils should offer loans to their citizens at low rates of interest. The aim of this suggestion² was to protect poor people against loan sharks. In 1361, Michael Nothbug, a bishop from London, provided capital for the founding of an institution which lent money without charging interest. A condition for a loan was that the borrower was able to pawn property with a value at least equivalent to the amount of the loan.

It can be said that Nothbug's institution used a similar concept to that which was later used by the organisation known as Montes Pietatis. According to Menning, Montes Pietatis was defined by its Franciscan founders as a "communal charitable institution" (1993, 207). Benigni defines it as a "charitable institution" which lends money at a low or zero rate of interest against pawned goods, with the aim of protecting people against loan sharks (1913, 534). As a charitable institution, Montes Pietatis only lent money to people who were going through a financial crisis. Any extra revenues created by charging interest or through fees were used to pay employees or to further extend their charitable work (Benigni 1913, 534).

Nothbug's organisation was quite short-lived as its overheads were paid for solely from the original capital provided by Nothbug (Benigni 1913, 535). On the other hand the Franciscans, Nothbug's successors, were able to maintain their financial support for Montes Pietatis. Moreover, interest rates were later established to cover the institution's overheads. Thanks to this policy, the Montes Pietatis network was able to spread all across Western Europe with little modification, and it survived for many centuries (Menning 1993, 27).

It should be noted that contemporary MFIs are influenced much more by Irish Loan Funds (ILFs) than by Montes Pietatis. ILFs operated in Ireland as a network of independent institutions from the beginning of the 18th century until the 1950s. The history of ILFs and society's reaction to them largely mirrors contemporary developments and discussions in the modern microfinance movement.

Interestingly, the first ILF was established in 1720 by the famous novelist Jonathan Swift. It lent money to poor traders without charging interest and was based on social liability. Swift had plenty of successors who financed similar funds, including the Dublin Musical Society (Hollis and Sweetman 2001, 295-296). In 1822, the London Committee for the Relief of the Distressed Irish founded a Reproductive Loan Fund Institution. This led to the creation of approximately one hundred new independent providers of microcredits.

New legislation aimed at regulating the funds' operations was approved one year later. The legislation established tax deductions in favour of the funds and it also allowed them to charge interest. The new rules increased the competitiveness of the funds and allowed them to finance their own expansion from the profits. By the beginning of the 1840s, after two decades of spectacular growth, the funds provided services to approximately 20 % of all inhabitants of Ireland (Hollis and Sweetman 2001: 296-300).

The names of the laws focusing on funds and their services imply that both loans and funds were deemed to be charitable. However, strict debt recovery policies and the high interest charged by the funds fuelled discussions concerning the degree to which their activities were still beneficial for the people. In reality, the funds were a mix of charitable organisations, business entities and loan sharks. For customers this situation was confusing (Clements 1843).

Although the microfinance movement underwent major development after the golden age of Irish Loan Funds, it seems that in some aspects the movement arrived at the situation already experienced in Ireland after the 1823 reforms. Discussing contemporary MFIs means discussing institutions which view themselves or are defined by the relevant legislation quite differently. Some MFIs are described as 'charitable microfinance institutions' (FINCA 2014; MicroLoan Foundation 2015), some as social business institutions and others as business entities or conventional banks. The leaders of some MFIs are keen to publicly disassociate themselves from the term charity, while others provide microfinance as well as comprehensive charitable programmes (for example Catholic Relief Services). To add more, critics perceive some MFIs as well disguised or poorly disguised loan sharks (see for example Karim 2011; Bateman 2010). Other authors discuss the issue of the 'ethical crisis' in the industry (Hudon and Sandberg, 2015).

The confusing situation described above is surely unhealthy for many stakeholders. Nowadays, charitable institutions with the primary aim of helping poor people and business entities whose main aim is to make a profit are labelled with the same name: MFIs. Undoubtedly, as with an efficient charity, an efficient, profit-driven business can greatly help

poor people. Despite that, the behaviour of the general public and potential donors shows that their willingness to support various institutions is influenced by the primary aims of such institutions. Information about the institutions' primary aims is also important for its clients and employees. The business-charity border matters.

Imagine an example of an extremely poor region, where two projects are proposed. The first project is a *Clothes Manufacture Investment Project*. The project aims to build a clothes manufacturing company in the region. It has a conventional business plan. If implemented, the project will bring new job opportunities. It is planned that employees will receive a salary typical of that paid to the local labour market. Working conditions as required by local laws will be guaranteed to them.

By applying for a job in the manufacturing industry, an applicant implicitly evaluates the employment offered by the manufacturer as being better than his former employment. Therefore, when at least one job offer is accepted by locals, the implementation of the *Clothes Manufacture Investment Project* will lead to an increase in welfare in society (for simplicity, let us assume that no negative externalities will be created by the manufacturer) and more than likely this will also lead to poverty reduction. For this reason we can conclude that the project will benefit poor local inhabitants.

The second project is the *Donate Clothes Campaign*. The *Donate Clothes Campaign* is aimed at distributing clothes to people in poor regions. It is a purely charitable project. If implemented, the project will lead to poverty alleviation and it will therefore increase the welfare of local people.

As briefly argued above, both projects have the potential to help locals. Both projects are also dependent on finance. While it is easy to imagine that a successful charity collection can be organized to support the *Donate Clothes Campaign*, it is hard to imagine that people would be willing to help selflessly the *Clothes Manufacture Investment Project*. This example shows that potential donors are sensitive to the question of whether giving help to people in need is a primary aim or only secondary. They are more willing to support selfless projects where help is the primary aim (that is also one of the reasons for people's reluctance to support charities with high overheads. See for example Uri et al. 2014 or Wong and Ortmann 2016).

Beside donors, a clear charity-business border also matters for clients and customers. People tend to be less cautious if they believe they are interacting with an institution which has charitable intentions. As a result, clients and customers who falsely believe they are to be recipients of charity, while they are in fact only interacting with an institution interested in conducting business, are at a higher risk of accepting a deal which is unfavourable to them.

It is worth noting that charity-business labelling is also important for employees. The microfinance sector is a good example. An employee of an MFI who is responsible for the provision of loans can make different decisions based on the MFI's priorities.

An employee can be instructed to primarily care for the wellbeing of a client or to mainly care about the institution's profits. An MFI with charitable intentions should evaluate the microcredit's potential to help or harm its client. An employee of a business MFI, on the other hand, is expected to evaluate the client's ability to repay the loan. A client being able to repay a loan does not necessarily mean that a microcredit is helpful (see for example Czura 2015; Taylor 2011).

Nowadays the microfinance sector has unclear charity-business borders, and this can cause some confusion and discussions among members of the general public and among professionals. The charity-business border is important for a variety of stakeholders, including potential donors and clients and employees of organisations working with poor people. A proposed location for the charity-business border and a definition of charity in business are discussed in the following part of the paper.

Charity and Business

Charitable activities are defined by Harrison as "generous actions or donations to aid the poor, ill, or helpless" (2008, 197). Dunn defines charity as "the act of giving money, goods or time to the unfortunate, either directly or by means of a charitable trust or other worthy cause" (2000, 223). For example the US administration perceives charity simply as "something given to a person or persons in need" (US Congress 1994, 53). From the definitions above it is possible to extract a minimalistic definition of charity as a 'gift to persons in need'. Using this definition though, it is important to perceive a gift in its altruistic meaning as something that makes another person fortunate or at least less unfortunate. Such a gift should maximize the utility to the recipient at some expense to the donor. This is not to say that the gift cannot imply a counter obligation. However, reciprocation may only be partial. For example, the donation of an item valued at 100 USD conditioned by provision of small service valued at 20 USD still fits the definition of a gift as used in this paper. If such a gift is given to person in need, then it is possible to label the donation of such a gift with conditions as a charitable act.

It can be deduced from the example above that voluntarily paying more for a service or a product to a person in need who runs a business should be labelled as a charitable act. Alternatively, if somebody is motivated primarily by altruism to buy a service or a product from a person in need (the motivation for the purchase is to help the producer but with no interest in the service or the product itself), then such a transaction can also be labelled as a charitable act, even without a voluntary price increase.

If a businessman reduces the price of a service or a product with the primary aim of maximizing its usefulness to a person in need and by doing so makes a voluntary economic loss, then such a step can be described as a charitable act in business. However, it is necessary to distinguish charitable acts in business from price discrimination. Price discrimination, first described and classified in detail by Pigou (1920), essentially relies on variations in customers' willingness to pay and leads to higher profits rather than to economic loss.

Concepts of accounting profit and economic profit are key elements in discussions concerning the location of the charity-business border. Accounting profit is calculated by the following formula:

$$\text{Accounting Profit} = \text{Total Revenues} - \text{Explicit Costs},$$

while economic profit is defined by the following formula:

$$\text{Economic Profit} = \text{Total Revenues} - \text{Explicit Costs} - \text{Implicit Costs}.$$

While explicit costs are direct payments made to others in the course of running a business (for example wages, rent or materials), implicit costs are any costs that result from any action or project's trade-off. Therefore, if the most profitable alternative project is less profitable than an implemented project, an economic profit can be achieved. If an alternative project is more profitable, then an economic loss is the outcome.

A businessman who decides to reduce the price of a service or a product with the aim of maximizing its usefulness to a recipient is obviously losing something. While this loss is well covered by the concept of economic profit, the same does not apply to an accounting profit. Imagine an example of a businessman who sells a product for 5 USD which has a production cost of 2 USD. As an altruistic gesture, the businessman decides to reduce the price to a poor person by 1 USD. Therefore, the new price of the product is only 4 USD.

For the businessman, the transaction means an accounting profit of 2 USD, because revenue is 4 USD and explicit cost is 2 USD ($4 \text{ USD} - 2 \text{ USD} = 2 \text{ USD}$). To calculate the economic profit, we need to first obtain the implicit cost of the transaction. An alternative to selling the product to a poor person at a reduced price was to sell it for the full price with no price reduction. This would create an accounting profit of 3 USD, because revenue would be 5 USD, while the explicit cost would remain at 2 USD ($5 \text{ USD} - 2 \text{ USD} = 3 \text{ USD}$). Therefore, the implicit cost of selling the product to a poor person at a reduced price is 3 USD. After the deduction of the explicit and implicit costs, we find that the transaction has meant an economic loss of 1 USD ($4 \text{ USD} - 2 \text{ USD} - 3 \text{ USD} = -1 \text{ USD}$) for the businessman,

Zero economic profit is the only level of profit which can be obtained in the long-term in a perfectly competitive market. In cases where the achievable profit would be abnormally high in some sectors, it would lead to the arrival of more competitors and they would push the profit down to the level of zero economic profit. In cases where the achievable profit would be abnormally low, some producers would leave the sector, which would push the profit up to the level of zero economic profit. To sell a product or a service for a price which does not allow the producer to achieve the level of zero economic profit in

such a market would lead to an economic loss for a business. The proposed charity-business border is attached to zero economic profit, also called normal profit. Charity can only start below the level of normal profit; economic loss is therefore inevitable. It is important to add that to call something a charitable act, economic loss must be caused by a *voluntary* decision led by the effort to maximize the utility of poor customers.

However, it should be added that it is difficult to identify the level of normal profit for sectors, individual companies and products in the real world as it is characterized by imperfectly competitive markets. Imagine an example of an antique dealer who is going to sell flawed but valuable antiques with an accounting profit of 1000 USD. She/He believes that the best alternative is to ask a restorer to repair the antiques. This would approximately double the price of the antiques, but it would also lead to a dramatic increase in costs. The result would be the same accounting profit of 1000 USD. Therefore, the dealer believes that the outcome of selling the antiques is a normal profit. However, if the dealer found that there was a well-skilled and cheap restorer in a different region and that their restoration would allow her/him to triple the price of the antiques, she/he would find that she/he actually incurs an economic loss.

Based on the discussion above, I define a charitable act as a gift which benefits a person in need. The gift must lead to an economic loss, but not necessarily to an accounting loss. It is important to note that this means that businesses practising charitable transactions only can be financially sustainable. Charitable activities in business can therefore be independent of external support and do not have to be subsidized by other non-charitable business activities. It is obvious that it is very hard to measure economic profit and to find a normal profit in the real world characterized by an imperfectly competitive market. In the following section all these findings will be applied to the microfinance context, and framework parameters for charitable microcredits and MFIs will be suggested.

Charitable Microfinance

It is difficult in practice to identify the level of normal profit and it is also necessary to distinguish charitable from non-charitable microfinance services, so there is a need to find a different way to identify charitable microfinance, one which approximates the criterion of normal profit and which is applicable in practice.

Distinguishing between charitable and non-charitable MFIs is important for their clients, employees and especially for donors, who often support MFIs based in and providing their services in different countries. This fact and the universal attitude towards charity described in the part *Charity and Business* is why I propose the establishment of internationally recognized criteria of charitableness in microfinance and of an internationally recognized microfinance authority. Such an authority can be established either by an organisation founded as a confederation of organisations (similar to the European network of NGOs called CONCORD), or it can be established as a cooperating organisation technically independent of those organisations (as was the case of MFTransparency in context of

microfinance). Theoretically, proposals for criteria can also be done by already existing microfinance initiatives such as CGAP or Mixmarket. However, these initiatives are dominated by people and organisations with a neoliberal background and are focused on the promotion of social business, which is not fully in accordance with the idea of charitable microfinance.

In terms of the certification of charitable MFIs or products, the microfinance movement can find inspiration in the Fair Trade system. In the case of Fair Trade, whole institutions are certified by the World Fair Trade Organisation (WFTO) and individual products are certified by Fairtrade Labelling Organizations International (FLO). Similar to microfinance, Fair Trade also balances on the business-charity border. One can argue that Fair Trade businesses are voluntarily generating economic loss by helping to provide better conditions for poor producers in an attempt to maximize their benefits. By accepting this perspective, we can view Fair Trade as a charitable activity. Critics of labelling Fair Trade as a charity usually argue that Fair Trade only ensures fair terms of trade, and therefore Fair Trade only leads to the improvement of badly set-up conventional trade, which is not a question of charity, but rather a question of being just and honest (see for example Nicholls and Opal 2004, 5).

However, there is no doubt that some customers perceive Fair Trade as a charity and that they also buy Fair Trade goods for altruistic reasons (for deeper discussions of customers' behaviour see Andorfer and Liebe, 2011; Salvador et al., 2013). Such customers cause themselves to incur a voluntarily loss in order to help others. For this reason, Fair Trade can be perceived as a charity (at least from the point of view of these customers).

Fair trade certification enables customers to identify those products whose purchase contributes to a 'good cause' and this therefore enables customers to be charitable. However, the same conditions as provided by Fair Trade companies can also be offered by organisations unwilling to pay for the certification process and thus do not have the Fair Trade label. I propose the creation of a similar certification system for charitable microcredits. The microcredits which met the established criteria would be denoted as 'charitable microcredits'. As with the Fair Trade system, those MFIs unwilling to undergo the certification process would be unable to use the *charitable microcredits* label.

While in the case of the Fair Trade system only the organisations unwilling to undergo the certification process are eliminated from the option of using the respective label, there would be also a second round of elimination in the case of *charitable microcredits*. As can be derived from the section *Charity and Business*, a charitable microcredit is a microcredit which increases the utility of a person in need. At the same time the provision of such a microcredit means a planned economic (but not necessarily an accounting loss) loss for the MFI. Because it is very difficult in practice to measure economic profit or loss, it is necessary to approximate this criterion somehow. A normal profit approximating criterion must be set in such a way that would stop the situation in which the *charitable microcredit*

label would be given to a microcredit which creates a normal or higher than normal profit. This stringent requirement for an approximating criterion can also lead to the elimination of some microcredit that create lower than normal profits.

I recommend setting the maximum price of *charitable microcredits*, either by binding their maximum annual percentage rate of interest (APR) below the average APR in the banking sector of the respective country to a segment of small loans or relatively close to the central bank's interest rate. To call a business transaction a charitable act, economic loss must be caused by a *voluntary* decision led by an effort to maximize the usefulness of the loan to a poor customer. This should be verified by the evaluation of an MFI's system of decision-making concerning the provision of microcredit to a client. Such a system should initially take into account any potential long-term positive effects of the microcredit on the living standards of a client and not only the ability of the client to repay the loan (i.e. for example investment loans should be preferred over consumption loans). To help identify a poor customer the international poverty line; a national poverty line set by the government, or a non-income indices of poverty such as the increasingly popular asset indices (see for example Ezrari and Verme 2012 or Cardozo and Grosse 2009) can be used.

Beside the three main criteria (low price of microcredits; provision of microcredits based on potential effects on living standards of a client; provision of microcredits to a poor client), the inclusion of other criteria can be considered. It can be, for example, mandatory to evaluate the effects of the charitable microcredits on its clients or to evaluate the provision of microcredits used only for investments and not for consumption. However, it is important to note that every extra criterion means a more expensive certification process. This also reduces the probability that MFIs which provide charitable microcredits only can achieve an accounting profit. The ability to achieve an accounting profit by such MFIs will also be greatly influenced by the exact determination of the maximum price of microcredits.

Certification can be applied not only to microcredits, but also to other microfinance products and to all MFIs. A certification of microsavings and microinsurance should be based on the same principles as the certification of microcredits. Certification of all MFIs should be conditioned not only by the provision of the charitable microfinance products exclusively, but also by other criteria relevant to the whole organisation rather than to the individual products. The criteria for *charitable MFIs* can also include being a non-profit organisation, because such a legal status indicates that the priority of the organisation is to help people rather than to generate a profit. Other criteria which should be considered for inclusion are ensuring good working conditions of the employees and an emphasis on the democratic governance of the MFI.

Conclusion

In this paper I focused on the issue of relevance and the meaning of charity in the context of microfinance. I highlighted the historical roots of microcredits, as far back as the Middle Ages, and also drew attention to the discussions which arose from the diversity within the microfinance movement. While some MFIs claim they are a charity, others claim they are entrepreneurs or social entrepreneurs. Contradictions in the perception of MFIs as a result of this diversity has already been well documented in Ireland from the 19th century and is also present today. The distinction between charity and entrepreneurship in the microfinance sector is important for (potential) donors and also for clients and employees of MFIs.

In this paper I argue that beside distinguishing between conventional and social business, we should also distinguish between social business and charitable microfinance. The simplest definition of charity is ‘a gift to a person in need’ and with the concept of normal profit this was used in the discussion about charity in a business context. It was stated that the term ‘gift’ can be used in a broader meaning as something that makes another person fortunate or at least less unfortunate, and that brings utility to the gifted person at the expense of the donor. Loss for a giver implies that the giver must end up in economic loss. Charity in business is therefore restricted to zero economic profit, also called normal profit. As economic loss does not imply accounting loss, this definition of charity in business allows charitable activities to be financially sustainable and therefore independent of external support and other profit-making activities of a charity provider.

The definition of charity in business is also applicable to microfinance products. As it is difficult to calculate or estimate the level of normal profit in microfinance, I propose approximating the normal profit using the price of the microfinance products. In the case of microcredits, the price of a loan as expressed by APR should be used. The average APR in the segment of credits in a local banking sector or a local central bank's interest rate can be used as a benchmark for setting the threshold for the charitable microcredits label. Other criteria must also be met for the microcredit to be labelled as a charitable microcredit. A system of microcredit provision decision-making must first take into account the potential long-term effects of the microcredits on the living standards of a client. Only people living below the international or national poverty line should be the recipients of charitable microcredits.

As with the Fair Trade systems of certification, all organisations can be labelled as charitable. Such a certification of MFIs would be conditioned only by the provision of charitable microfinance products and also by other criteria. The ability of charitable MFIs to achieve an accounting profit will depend not only on the quantity of the criteria, but also on their stringency, especially in the case of the designation of the maximum price of microcredits and other products. Although this issue is beyond the scope of this paper, it is important to note that the maximum price must be set in such a way that will stop a situation where

the charitable product label is given to any product which creates a normal or higher than normal profit. The principal advantage of criteria based on the maximum price derived from the level of normal profit is that it is independent of the issue of profitability of the individual products or of the individual MFIs. Therefore, loss-making caused by the ineffectiveness of MFI cannot be falsely passed off as charitableness.

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Notes

¹ Amongst them are for example Czech NGOs Fair z.s, Shinebean z.s. (both implementing their activities in Kenya) or Maendeleo (implementing its activities in Tanzania).

² It is not known whether the suggestion was implemented.

³ The original aim of the committee was to raise a general subscription to relieve the famine in Ireland caused by crop failure. However, after the famine was over the committee was left with a considerable amount of money and no clear mandate what to do with it. It was decided to use this money as basic capital for a new loan fund.

⁴ For example: Charitable Loan Fund Act (Dillon 1899), Charitable Loans Societies Act (Atkinson 1898), Charitable Loans Act (Hemphill 1900).

⁵ Since then the Microfinance movement has been greatly influenced by such cooperatives as Raiffeisen and Schultz-Delitzsch and by agricultural development banks.

⁶ For example, Yunus (2008, 205-269) describes charity as an ineffective tool to help the poor.

⁷ For a complex discussion of the relationship between profitability and the poverty alleviation effects of MFIs' operations, see Morduch (2000) or Mersland and Strøm (2010). Also, profit-driven businesses are (unlike charities) key drivers of economic growth, which positively influences levels of poverty and human development (see for example Harmáček et al. 2016 or Schlossarek et al. 2016).

⁸ Term 'person in need' includes all categories of people mentioned in Harrison's and Dunn's definitions: poor people, ill people, helpless people, and unfortunate people.

⁹ Such a person does not equate the product or service bought from a person in need to the price paid. Reciprocation for money paid to a person in need for his/her services or product is therefore, from a customer's point of view, only partial.

¹⁰ Implicit costs are also called opportunity costs.

¹¹ A perfectly competitive market is a hypothetical market where competition is at its greatest possible level.

¹² In such cases, economic profit reached by sectoral producers would be higher than zero, which would mean that all alternatives would be less profitable for them.

¹³ In such cases economic profits achieved by sectoral producers would be lower than zero, which would mean that at least one alternative would be more profitable for them.

¹⁴ An imperfectly competitive market is, for example, a market characterized by consumers with imperfect information or by barriers to producers entering and leaving the market.

¹⁵ In fact, deciding about the charitableness of an organization competing in an imperfectly competitive market based on profitability would be inappropriate. Imagine the situation when an efficient MFI creates a profit and charges a lower rate than an inefficient MFI which finds itself operating at a loss. Based on profitability criteria, we would - ironically - award the charitable label to the MFI that is costlier for clients.

¹⁶ The exact formula could be country-specific and based on the decision of local committees of a certifying organization. The author is aware that in many countries including Bangladesh, there is an imposed cap on interest rates and an extensive regulation of the sector by either banking authorities or separate microfinance regulatory entities. However, for charitable microfinance, regulations can be much stricter, as the only "punishment" for MFIs unable to adhere to them would be the inability to obtain a certificate of charitableness.