Credit, the Employment Relation and the Property Rights Constraint

Lilia Costabile
Italy, Political Economy

Credit, the employment relation and the property rights constraint .
By Lilia Costabile

1. Introduction.

In this paper, I explore one non-standard employment relation which, rather than in the labour market, is established via a debt-credit contract. The story, which is set in the village of Jobra, Bangladesh, in 1974, has been told by Muhammad Yunus, the "poor people's banker", in his book *Vers un monde sans pauvreté* (1997).

My investigation is two-fold: first, I propose to examine the accounts which alternative economic and philosophical approaches (Conventionalism, Libertarianism, Welfarism, and the Capabilities approach) may provide of this employment relation: the purpose is both to derive some useful insights into the nature of this relation, and -at the same time- to understand alternative positions and their respective merits, in the light of their analytical and normative arguments concerning the case in hand. Secondly, in order to investigate the reasons which may have motivated Yunus's decision to take action against the state of affairs at Jobra, I start by proposing my own interpretation of the employment relation which he describes in his book. I then try to illustrate how Yunus used the credit channel, and argue that he turned credit from an instrument of "command" over labour, into a powerful lever serving the related purposes of undoing the employment relation, restoring the autonomy of the subjugated person, and conferring control over the instruments and fruits of her own work.

The implication is that credit may be instrumental to a general project to overcome the "limited access problem", or "property rights constraint", which lies at the root of many employment relations.

2. Sufia's story

In his book *Vers un monde sans pauvreté* Muhammad Yunus tells us the story of Sufia Begum, one of the women whom he met in the village of Jobra, near the University of Chittagong in Bangladesh, during the terrible famine in 1974.

Sufia earned her life by making bamboo stools. Yunus informs us of the specific conditions of Sufia's work: every day she borrowed the equivalent of 22 cents of a dollar from the *paikar*, i.e. the merchant. With this money she bought the raw materials (bamboo) necessary for a day's work. At the end of the day, she sold the stools to the merchant, and earned the difference between the value of her daily product, as agreed upon between her and the merchant, and the value of the raw materials. This difference, the daily compensation for her work, would amount to two cents, barely enough to provide food for one person, but insufficient to feed her family, let alone to provide decent clothing and basic education for her three children (Yunus, 1998, p.19). As Yunus explains, Sufia had not enough money (that is, 22 cents) to buy the straw elsewhere; this circumstance enabled the merchant both to appropriate the stools, and to fix her daily compensation at the level just necessary to cover the price of the raw materials, plus a little amount necessary to keep her alive, and in need of his money.

The first thing to note is that, interestingly, in this story deprivation was not the result of lack of employment, but stemmed from the nature of the contractual relation in which the deprived person was involved. Secondly, the connection between work and credit is worth exploring. The merchant, by providing Sufia with credit, was able to "command" her daily labour and become the owner of its product. Thus, although formally an "independent worker", Sufia was involved in a sub-category of what economists call the "employment relation".

For the purpose of alleviating the situation of poor people at Jobra, Yunus started his micro-credit program, whereby Sufia, and other people like her, were given the credit necessary to buy capital assets (in Sufia's case, the bamboo) in order to start their own business, become independent of the merchants, and achieve a higher standard of living.

In the following sections, I propose an enquiry into the reasons motivating Yunus's decision to act, and his choice of the credit channel as the appropriate instrument. Although they might seem quite obvious at first sight, these reasons are interesting to investigate. Obviously, he was motivated by the notion that there was something unacceptable in the situation discovered at Jobra, something that needed to be changed. But, as we will see, this notion is not so obvious as may seem at first sight: Sufia's situation would have appeared acceptable, or not requiring interference, if judged by the standards of some modern economic and philosophical theories.

To illustrate this point, in next section I propose an exercise in interpretation: the relation between Sufia and the merchant will be explored in the light of the alternative analytical arguments and normative criteria proposed by alternative streams of modern economic and philosophical thought[1]. These alternative approaches will be ranked in ascending order: namely, from those imposing less demanding principles of legitimacy to those founded on more demanding normative criteria, until the approach, or the approaches, able to motivate Yunus's project are found.

2. Conventionalism, Libertarianism, Welfarism, and the Capability approach.

Conventionalism. The weakest among alternative principles of justice is that proposed by conventionalism, which I will explore through the writings of Robert Sugden (1986). The tests of legitimacy imposed by this approach are not very demanding, and Sufia's situation would pass the conventionalist test of legitimacy, both on analytical and on normative grounds.

From an analytical point of view, this approach, if anything, has a presumption in favour of inegalitarian property rights, for their asserted superior degree of "salience". The idea here is that established conventions of property emerge as "salient", and therefore as a solution towards which the competing parties are attracted, because they exploit a particular asymmetry between them. More precisely, "they exploit an existing association between claimants and objects. Such conventions inevitably tend to favour possessors, since to be in possession of something is to have a very obvious association with it" (Sugden, 1986, p.89). In other words, in this model, property rights are established on a "first-come, first served" basis[2].

From the normative point of view, no grounds for an intervention in favour of Sufia can be found in this approach. What we find, instead, is a recommendation that the existing property rights are not violated since, according to this view, "conventions by which people resolve disputes come to have the status of moral rights and obligations". Consequently, "any government that tries to overturn these conventions must expect its actions to be viewed as

[1]Other relevant approaches, such as those developed by Alchian and Demsetz, North, Hodgson are dealt with in Costabile, 1998 (see also Costabile 1995).

[2]The illustrating example is the convention, ruling on the Yorkshire coast up to the 1930s, whereby property rights over driftwood were assigned to the first person to go to a stretch of shore after high tide and collect the wood.

morally wrong – as illegitimate invasions of individuals' rights" (Sugden, 1986, p.176). Sugden's conclusion is that "the morality of spontaneous order is conservative" (Sugden, 1986, p.177).

What are the implication's for Sufya's story?

First, conventionalism does not require that the situation is evaluated from an economic point of view. It is irrelevant, for instance, whether the economic system in which Sufia and the merchant happen to live is characterised by feudal or capitalist property rights. Also irrelevant is the nature of the employment relation which binds them together, as well as the structure of the labour, credit and product markets in which they operate.

Secondly, conventionalist ethics is bound by its very nature *not* to object to existing conventions, whatever these might be, because it regards the mere fact that a convention has been established as a sufficient condition for its ascent to the role of a moral norm. Conventionalist ethics is, indeed, relativist: people are expected to follow the rule which everyone else in that community respects, but if a different rule is followed in the community, then everybody is expected to follow this alternative rule. Whatever the initial situation, that situation is the only legitimate point of view from where we are entitled to make moral judgements. Rights and obligations are "matters of convention" (Sugden, 1986, p.175).

Conventionalism does not rely on a consequentialist ethics. It is easy to see that the established convention excludes Sufia and her children from owning anything (except Sufia's ability to work, and the scarce food she can buy with the compensation for the stools). It is also easy to recognise that the initial distribution of assets gives the merchant the power to appropriate the whole product of her work, except for the bare subsistence: Sufia's exclusion from productive assets (the bamboo) also excludes her from access to the means of subsistence, and –by setting her "outside option" at a very low standard (in her case, starvation)- severely limits her bargaining power and, consequently, her distributive share. According to conventionalist ethics, these considerations are irrelevant: what is relevant is: (1) the spontaneous nature of the process establishing the existing conventions of property ; (2) the fact that every individual adopting the established rule has an interest that everyone else does the same (Sufia should be happy with it because the established convention of property protects her from thieves); and, consequently, (3) his/her *right* to demand that every one else respects the convention and acts accordingly.

Finally, it is worth stressing conventionalism's limited appreciation of the scope and meaning of non-compliance with the existing conventions of property, which it identifies with theft. Indeed, conventionalists would expect non-compliance to come only from mavericks and thieves. To these people, on a strict application of the logic of this argument, should be likened non-conventionalist philosophers and economists, as well as any person objecting to the established conventions of property on economic and/or moral grounds[3].

Libertarianism. Procedural justice, proposed by libertarians, implies some more demanding criteria of justice than conventionalist morals. A formulation of the libertarian approach, proposed by Nozick in the 1970s, relies on the notion that the "principle of voluntary exchange" (market transactions) and voluntary transfers (gifts, charity, bequests, etc.) is what makes a distribution of holdings legitimate. The first principle of justice states that "a distribution is just if it arises from another just distribution by legitimate means" (Nozick, 1974, p.151). The basic idea is that what makes the established distribution of holdings legitimate is simply the "just" and voluntary nature of its generating process.

This principle of justice also implies that only an examination of the whole chain of prior transactions can tell us whether the current distribution of holdings is legitimate. But this process of "backward examination" sooner or later brings us to the stage when an "original acquisition" of previously unheld things occurred.

This observation leads us to the second condition required for a distribution to be "just" in Nozick's sense, namely "the principle of justice in the original acquisition of resources", stating that a system of property rights, established by an act of private appropriation of previously unheld things, is legitimate if "enough and as good is left to others". According to this approach, private property rights are conducive to greater productivity and efficiency, thus enabling the "appropriator" to compensate the excluded persons with an amount of resources at least equal to what they would get in the absence of the appropriation. Hence, private property is legitimate

[3] Conventionalism cannot explain diversity and contestation within a given culture or a given society (Martha Nussbaum's critique of cultural relativism applies here: see Nussbaum, 2000, pp.41-49). Indeed, the idea that conventions come to acquire the status of moral norms, and that, moreover, these moral norms are inviolable, is an undemonstrated assumption.

from a moral point of view; in other words, private property is conducive to greater social welfare.

We can now attempt an evaluation of Sufia's story according to Nozick's "entitlement approach" and related tests of legitimacy. Suppose some illegitimate means (e.g. theft or violence) were adopted by the merchant and/or by any previous owner in the chain of ownership transfers. Under these circumstances, the employment relation between Sufia and the merchant would suffer from an "original sin", and would have to be "undone". By contrast, under the alternative assumption that the merchant's money was acquired by legitimate means, the relationship between Sufia and the merchant would pass Nozick's " principle of justice in the original acquisition of resources".

Nozick's second requirement is the "principle of justice in transfers". Since the relationship under examination is based on a voluntary exchange between the legitimate owners of, respectively, the money and the labour services, Nozick's second test is also respected.

Thus, we seem to be entitled, within the boundaries of the libertarian approach, to deduce that Sufia's rights are not being violated, even if her compensation is at mere subsistence. The consequences concerning the health, education, quality of life of Sufia and her children, in absolute terms as well as in comparison to the conditions of people born in more fortunate circumstances, are also not regarded as sufficient to impose a reconsideration of the "legitimacy argument" in favour of private property. The paradox of the libertarian approach is that, for all its stress on people's rights, it completely ignores welfare rights (Hausman and MacPherson**,** 1996, p.130-131).

The "entitlement approach" would definitely object to any violation to the "principle of justice in the original acquisition of resources ". Under given circumstances, it could even ask for a general "rectification" of the system of property rights, in order to undo past injustices. But, according to this approach, the present reality of the "employment relation" between Sufia and the merchant does not entail any *current* violation of economic or moral principles, given the voluntary nature of the exchange occurring between them. Therefore, it passes the libertarian test of legitimacy.

Welfarism. Economists raised in the welfarist tradition would enquire whether the economy under investigation is Pareto efficient. Their approach may imply a severe condemnation of the relationship between Sufia and the merchant, and may thus lead us to call for far-reaching economic reform. However, as will be argued below, this normative approach suffers from severe limitations.

Under competitive conditions, equilibrium wage and employment levels are on the labour supply curve. This implies that exchanges on the labour market are voluntary, and that workers' utility is maximised. Moreover, in perfect competition, each potential borrower faces an infinitely elastic credit supply, implying that he or she can borrow any desired amount at the current interest rate. The usual interactions between demand and supply bring both the credit and the labour markets to their equilibrium condition.

However, Sufia's situation must imply a departure from perfect competition. A welfarist economist may adduce one of the following reasons, depending on which market is considered as non-purely competitive.

(1) The merchant is a monopolist in the credit market at Jobra. Consequently, in equilibrium, the average cost of lending is lower than its price (the interest rate). This circumstance has a twofold implication: first, the merchant earns a positive profit, or rent, which will not be eliminated by competition; secondly, the equilibrium is inefficient, since the amount of credit granted to the villagers is lower than in perfect competition.

(2) In Bangladesh, as in other less developed countries, the labour supply should be described as a horizontal line with intercept equal to the height of the subsistence wage. At this real wage, the labour supply is unlimited (Lewis, 1953). The merchant maximises profits by demanding Sufia's work up to the point where her marginal productivity equals the exogenously given subsistence wage. By so doing, he earns a positive rent.

(3)The merchant is a monopsonist in the labour market at Jobra. Hence, both employment and the wage level are lower than the corresponding competitive levels. The difference between the competitive wage and the current wage is a measure of "Pigouvian exploitation".

Rent extraction is not compatible with the long-run equilibrium of a competitive economy. In the latter type of economy, other merchants would compete for extra-profits by demanding Sufia's work at a higher real wage, until these extra-profits are absorbed into higher costs. Similarly, other lenders would enter the credit market, thus establishing a competitive equilibrium which, in a production economy, will normally reflect the underlying forces of productivity and thrift. In the long run, no surplus would survive, and Sufia would reap the whole fruits of her productivity. Since the economy under examination does not satisfy the conditions of perfect competition, poverty, "exploitation" and inefficiency should be remedied by a reform of the credit and labour market, thus ensuring that rents are washed out by the restored competitive process.

The problem with this normative approach is that there is no guarantee that Sufia, the weak trading partner, would be immune from poverty in a restored perfectly competitive economy, where every agent is paid according to the marginal product of the factor that she or he owns. In fact, the market distribution depends entirely on the initial distribution of assets. Because an agent's *income* is the product of that marginal product times the amount of the factor he or she owns (and, moreover, the marginal product of a factor itself depends on the level of output and the initial distribution of assets), a poorly endowed agent would not be safe from poverty and deprivation in a pure competitive world (Varian, 1979, pp.140-141).

Thus, social justice (and even the far more limited objective of preventing one of the agents from starving) may require that the Pareto distributive principle is violated, by redistributing income or resources away from the rich agent and in favour of the poor. By so doing, the rich would be made worse off , but, in a world of limited resources, that is exactly what we want, in order to restore some degree of distributive justice.

The capability approach . By focusing on her standard of living and the quality of her life, the capability approach provides interesting insights into Sufia's condition. Standard of living can be defined as "personal well-being related to one's own life" (Sen, 1987, p.29). The conditions of a person's life, on which her well-being depends, include both the set of her "functionings" and the set of her capabilities.

Functionings are the characters of the lifestyle that a person actually leads, or "different aspects of living conditions" (Sen, 1987, pp.36-37); seen in a slightly different perspective, functionings are what a person actually achieves (Sen, 1993, p.31-33): such as being well nourished, or being decently dressed, or "living a life free from cholera or smallpox" (Sen ,1987, p.104), being literate, reading literature and poetry, "having self-respect, preserving human dignity, taking part in the life of the community" (Nussbaum and Sen, 1993, Introduction, p.3).

No less important than these actual functionings, according to Nussbaum and Sen, are the "real opportunities" a person has regarding the life he or she may lead. It is important to stress that, while in the traditional economic approach only "achievements" (e.g., the levels of utility, or the amounts of goods chosen) would enter an evaluation of the agent's living standard, in this approach the opportunities open to that agent are an essential component of her living standard.

Thus, by making freedom a constituent part of a person's living standard, the capability approach parts company with traditional economic analysis. Moreover, Sen's famous, severe evaluation of Pareto efficiency as a criterion of social justice marks still another significant departure from the traditional welfarist approach, and suggests that we could object to the employment relation between Sufia and the merchant, but not merely on efficiency grounds[4].

The gulf between the capability approach and the other lines of thought discussed above is even wider. Despite the importance that it gives to freedom, the capability approach is very different from libertarianism, since it interprets freedom as *substantive* freedom. In fact, the "enabling" function of freedom (as opposed to its procedural aspects) is now regarded as one of its basic, if not its basic, character. With regard to Sufia's story, for instance, Nussbaum and Sen would probably argue that her capability set is very restricted indeed, since she has no choice but to accept a contractual relation with the merchant, and it merely enables her to achieve the "functionings" of working hard and living in misery with her children. Hence, although both Sufia's and the merchant's procedural rights are respected, she, and the society they both inhabit, enjoy very little substantive freedom.

Finally, Nussbaum and Sen repeatedly object to accepting "traditions" as a foundation for, and guarantee of, social justice (Nussbaum, 2000; Nussbaum and Sen, 1993, p.4). This suggests that the capability approach would not justify Sufia's situation on conventionalist grounds, and would probably advocate that action be taken in order to abolish the conventions causing Sufia's absolute and relative deprivation.

Thus, our analysis of alternative arguments concerning economic justice can be concluded by observing that the capability approach, by taking the standard of living as a baseline, and by

[4] "An economy can be optimal in this sense [i.e. Pareto efficient] even when some people are rolling in luxury and others are near starvation as long as the starvers cannot be made better off without cutting into the pleasures of the rich.[….]. In short, a society or an economy can be Pareto optimal and still be perfectly disgusting" (Sen, 1970, p. 22).

insisting that both absolute and relative deprivations should be removed, is certainly the most severe and demanding approach to social justice among those reviewed thus far.

In my opinion, Yunus may well have been motivated by a vision similar to that endorsed by Nussbaum and Sen, with regard to the ethical and economic problems plaguing Jobra, the Bangladesh economy and, perhaps, the world as a whole. Nevertheless, I think that we should also focus on some further aspects of Sufia's story. In order to change her living standards, Yunus took actions aiming to allow her to leave the employment relation, and remove the property right constraint which was impeding both her access to the instruments required for production, and her full control over the product of her work. Abolishing absolute and relative deprivation, and establishing a just distribution of capabilities may, in some cases, require that this type of constraint be removed.

Before turning to this analysis, I should add some remarks concerning a serious omission in my review of alternative criteria of justice. The reader may be surprised that no use has been made of John Rawls' theory of social justice, given its extraordinary, enduring influence on contemporary economic and philosophical thought. Moreover, Rawls' "difference principle" is easily adapted to Sufia's case, since it dictates a redistribution of primary goods (including wealth and income) in her favour. Under the "difference principle", people only have a claim to a greater share of the society's resources if they can show that such unequal distribution benefits the least advantaged (Rawls, 1999, p.266). The merchant would certainly have a hard time in mounting such an argument in support of his privileges.

Why, then, did I not deal with Rawls' theory of justice? The fundamental reason is that Rawls' enquiry is wider in scope than the one I have attempted here. Rawls is concerned with the basic principles of social justice that "regulate the choice of a political constitution and the main elements of the economic and social system" (1999, p. 7), to the purpose of investigating "what a perfectly just society would be like" (1999, p.8). It goes without saying that I have not attempted such an ambitious investigation into the basic principles of a just society: My analysis is limited to an exploration of the principles which may have inspired one particular "policy" intervention, such as that devised by Yunus. Dealing with Rawls' theory of justice would imply an involvement in issues of paramount importance, that go beyond the scope of the present article.

Having said this, I would like to add that the analysis developed in the next section, with its emphasis on the issue of remedying the differential control over productive assets, goes well together with the concept of a "property-owning democracy" defended by Rawls (following Meade, 1964), i.e. a system which "tries to disperse the ownership of wealth and capital and thus prevent a small part of society from controlling the economy and indirectly political life itself" (1999, p. xv-xvi).

4. Micro-credit and its reasons

In the days following his first meeting with Sufia, Yunus discovered that forty-two families were indebted with merchants for a total amount of 856 taka, the equivalent of 27 dollars, and worked for them under contracts similar to Sufia's. A whole village was starving for a debt amounting to a total of twenty-seven dollars (Yunus, 1998, p.21).

Yunus explicitly makes clear that the villagers were not poor "because of their stupidity or laziness". On the contrary, they worked all day, performing complex physical activities (Yunus, 1998, p.21). Why, then, did they not have access to the goods and services which would ensure a decent standard of living for themselves and their families? Simply because they did not own the bamboo or other productive assets used for performing their work.

Moreover, they were too poor to obtain credit. In Yunus's own words, people in Jobra were poor because "the financial structures in our country were not prepared to help them in enlarging their economic basis. It was a problem of structures - not one of people" (Yunus, 1998, p.21). In other words, because the villagers were poor, they also faced a severe financial constraint. Since, under these circumstances, they could not own the required capital assets, their constrained, if voluntary, choice was - and could not be otherwise - to borrow from the merchant, thereby entering an employment relation with him, at whatever terms the (implicit or explicit) contracts would fix.

Yunus started his micro-credit project, whereby the villagers were given enough money to buy whatever capital assets they needed in order to start-up their own activities. Some considerations may be drawn from Yunus's investigation and from the rationale behind his credit scheme.

(1) Firstly, what motivated Yunus to start his project at Jobra was the extreme poverty of the villagers, which caused the death of many of them in the extreme event of famine, but was an

endemic condition even in normal times. In other words, famine was linked to poverty and poverty to the institutional features of Bangladesh. In the course of his investigation, he discovered that the causes of poverty were deeply rooted in the specific character of the credit and labour markets, and in the underlying system of property rights prevailing in Bangladesh.

We can interpret Yunus's argument as follows. By excluding some people from the ownership of productive assets, the system of property rights and institutions (including financial institutions) also creates a separation between them and the "necessaries of life". Once this double separation is established, the conditions for the existence of an employment relation are established too, since these peoples' command over the goods and services necessary for their survival and well-being must now be mediated by such a relation. This limits their autonomy, by placing them under the control of others, who are entitled to decide the organisation of work, the product mix, and the distribution of income - possibly within the limits set to their bargaining power by some external constraints (see below). Voluntary exchanges and contracts come in at this stage, to re-establish a link between the (would-be) workers and their means of subsistence.

The specific contractual relations which these voluntary exchanges bring into existence may vary: in fully developed market economies, wage contracts prevail. By contrast Sufia, formally an independent worker, is tied to the merchant by a debt-credit relation. She has no access to bank credit because the bank is not interested in the only "collateral" she could offer as a guarantee: her ability to work. By contrast, the merchant is ready to offer her his money, since he is interested in commanding the specific product of her work at a minimum price, thus maximizing his returns over the capital advanced. Under these circumstances, the merchant, a monopolist in the credit market, faces a very inelastic demand curve, given the lack of substitutes and the workers' absolute necessity to borrow. If he borrows the money from the banking sector, his cost curve reflects the passive interest which he pays on these borrowings. Alternatively, he may lend Sufia part of the proceeds from the sale of her stools, at virtually zero cost to himself. In either case he earns the difference between the price of credit that she pays and the cost of credit to himself. Total profits absorb virtually the whole value of the borrower's product, except for the share of her wage, set at the level necessary in order to keep the "wheel" of exploitation spinning. Sufia must adjust her work effort in order that the value of her product enables her to pay for the bamboo, the merchant's share, and to keep herself alive.

In spite of the different contractual relations, the underlying motivations are the same in Jobra as in developed market economies: the employers' purpose is to control the employees' work-effort and the value of their product; for the workers, the purpose is to re-establish a link between their work and the instruments of production, in order to gain access to the "necessaries of life". Thus, a voluntary exchange between labour and capital occurs because, as Joan Robinson (1983 [1962], p.46) appropriately noted, there is one thing worse than being exploited by a capitalist: not to be so exploited by any.

(2) Secondly, once the employment relation is actually established, the workers' access to the necessaries of life becomes possible, but – given that they lack direct control over productive assets - it also becomes dependent on the contracts that they are able to strike with their contractual counterpart. This brings us towards the realm of bargaining theory, with bargaining powers set unequal by the unequal degree of command over productive assets.

Within these limits, the parties' bargaining power may find further determinants in the economic and institutional features of the country in which they happen to live. Thus, for example, in the conditions described by Yunus, the villagers' bargaining power is so restricted – it is practically nil - that their compensations are at the mere subsistence level. The reason why Sufia and her fellow villagers cannot get a higher compensation for their work is that many other people would be willing to take their place if they were to refuse the conditions dictated by the merchant, since everybody's next best alternative is to starve. Under these circumstances, they have no bargaining power and, consequently, wages –according to Yunus's appropriate remark- are just sufficient to keep workers alive and in need of the merchants' money. Under these circumstances, wages are determined by pure market forces.

By contrast, in more advanced economies - like many western economies - workers' bargaining power may be enhanced, even at less than full employment, e.g. by unemployment benefits, which raise their "outside options". Under this or similar institutional arrangements (like minimum wages, etc.), the lower limit to wages is higher than in the "pure market" solution described above. Consequently, western economies – to the extent that they regulate their labour markets with institutional arrangements of this type - create the conditions for less inequality in income distribution. In these economies, there is some scope for improvements in workers' standard of living.

(3) Our third consideration is that - in spite of this further major difference - "backward" and "developed" economies share some basic elements in the structure of property rights: as was stated above, by assigning different "bundles of rights" over productive assets to different people - these systems also establish the necessity of the "employment relation", as an intermediary between some agents and the means of their subsistence and well-being, thus limiting their autonomy.

Yunus's story brings to the forefront the issue of the differential control of productive assets. Any existing inequality in the distribution of income between workers and their "merchants" is the product of this more basic inequality.

(4) Our fourth consideration concerns changing property rights. How do property rights change? Again, different schools of thought provide different answers. According to some authors belonging to the "spontaneous order" school, property rights, like other institutions, change as the result of spontaneous evolution; other authors predict that they change if and when they come to conflict with economic efficiency, or if the underlying system of costs and benefits changes. However, some may argue that property rights may also change as a result of rational choice and, in some cases, as a result of an ethical project. The very fact that Yunus started his project, as well as his efforts to devise a rational poverty-relief scheme, may be regarded as evidence that the latter approach to institutional change inspired the lines along which he acted.

Consistent with his finding that Sufia's poverty was the result of her employment relation, what Yunus did was to help her to quit: she would thus be freed from the necessity to make a contract with the merchant, and offered an alternative way to earn the "necessaries" of life. What was obstructing this freedom was her lack of ownership of the capital assets (the bamboo). Yunus tried to remove this obstacle by enabling her to buy the required means of production. Starting on a small scale, he was trying to introduce some element of change in the existing system of property rights.

His solution was different from those recommended by other schools of thought, some of which would have recommended that the spontaneous order of established conventions should not be interfered with or, alternatively, would have made changes subordinate to the proven inefficiency of existing property rights. What motivated Yunus to act was not Pareto inefficiency (indeed, weakening or abolishing the merchant's control over Sufia's labour certainly made him worse-off), but a concern with both the standard of living and the autonomy of the working population.

(5) Our final point concerns the role of credit as a means of redistributing capital assets and changing property rights. In order to analyse this point, it is helpful to recall some basic features of the model of the economic circuit, where credit plays a fundamental role. I will refer mainly to Augusto Graziani's version (1980, 1984, 2004) which, for my present purposes, I define the "classical" circuit model.

Firstly, in a market economy with production, different social groups may be distinguished by their differential access to bank credit. By virtue of their access to bank credit, entrepreneurs command an amount of purchasing power which is independent of their income; by contrast, workers' purchasing power is constrained by, and equal to, their incomes. Entrepreneurs open up the monetary circuit by "buying" labour in exchange for the money that they receive as credit from the banking system. By contrast workers are not in a position to express any demand until some firm decides to hire them.

Secondly, given that workers' budget constraint is determined by their money wage and by the price level of consumption goods (which, in turn, is determined on the goods market), it follows that the maximum amount of consumption that workers can attain is equal to the amount of consumption goods produced by the firms in the opening phase of the circuit (though workers may decide to consume less). Thus, entrepreneurs' autonomy also extends to the composition of output and, through this channel, to the determination of real wages (though workers may defend real wages via the instruments of "social contracting").

The "opening phase of the circuit" is in many ways the fundamental one. This is so because, as we have just seen, this is the stage when firms decide the level and composition of final output, thus also setting the stage for income distribution. But, perhaps more fundamentally, it is at this stage that a trilateral relationship comes into existence: a debt-credit relationship between the firms' sector and the banking sector, and a buyer-seller relationship between firms and workers in the labour market.

Now the question is: can we interpret the relationship between Sufia and the merchant, as well as Yunus's micro-credit scheme, in the light of these insights from the circuit model? My answer is yes, for the following reasons.

What the entrepreneur and the merchant at Jobra have in common is their being "mediators" between the worker and the materials needed for production. Their role as mediators is made possible by their command over purchasing power, which they use to command labour either directly in the labour market, or indirectly through lending. The similarity between them becomes clearer if we assume, for argument's sake, that the merchant, like the entrepreneur in the circuit model, acquires his command over purchasing power via the banking system. Under this assumption, both the circuit model and the Bangladesh economy work with a tripartite class scheme (banks, firms and workers).

In the classical circuit model, this tripartite class scheme is adopted in order to provide a description and an interpretation of the working of market economies. This purpose also explains why the model concentrates on the principles of conventional banking, whereby credit is only granted to some categories of people: presumably, those who own wealth to serve as collateral.[5] But, setting aside this interpretative purpose, the circuit approach does not imply any *logical* necessity why we should assume either a tripartite class structure or conventional banking principles. In principle, credit may be granted to any category of people, whether or not they own collateral to serve as a guarantee. Similarly, in Yunus's approach, there is no *logical* necessity or *practical* reason why banks should apply conventional principles, thus re-producing such a tripartite class-structure. Yunus decided to lend money to poor people not owning any collateral, thus enabling them to exit any inconvenient employment relation.

In the "non-conventional circuit" model, which I am proposing, the bank lends credit directly to the producers, i.e. to people using their own work effort to make goods and services. With this credit, they are enabled to buy the materials and start their production processes, finally selling their products and paying back the loan and interest to the bank. This is exactly what the

---

[5] Even though the circuit approach is not explicit on this point, there must be some reason underlying the asymmetry referred to at the beginning of this section. The circuit approach must either implicitly adopt an explanation based on the owning of collateral, or assume some other selection process (e.g. a random one).

Grameen Bank did in Bangladesh and, later, in many other countries[6]. The credit channel was not used for the purpose of re-producing the employment relation, but for the opposite end of abolishing it. Thus, while workers' autonomy is established by virtue of this scheme, also a bigger share of the fruits of their effort accrues to them.

The final result of this lending scheme depends upon the banking sector's objectives and what it decides to do with the interest payments on its lending. The Grameen Bank (as other microfinance programs) devotes its distributive share to the purpose of expanding the area of independent work at the expense of direct or indirect employment relations[7].

One final remark: some readers may consider that this paper merely concentrates on distributive issues, thus underrating the problem of raising productivity: in other words, rather than focusing on the mechanisms that induce a growth in the pie, it discusses how a given pie is, and should be, distributed. Although my argument does not deny the importance of raising productivity, it privileges the notion that we should pay some attention to the distribution of the pie, and also to the ingredients we put in it. We may require that productivity growth should be maximized subject to the constraint that the yeast does not include intoxicating substances.

---

[6] It has been argued by one of my readers that the Grameen bank may simply have eroded the monopolistic position of the merchant, and that, consequently, the change it has induced is entirely within the boundaries of orthodox economic analysis. I do not disagree that perfect competition is superior to monopoly, but I think that a multiplicity of banks acting on the principles of conventional banking, i.e. requiring previously accumulated wealth as collateral, may not have done much to improve Sufia's conditions.

[7] Morduch (1999) and Woolcock (1999), among others, are extremely useful references concerning the problems of incentive compatibility, motivational factors, and financial sustainability involved in micro-credit programs. In this article, I have not been adopting the "win-win" rhetoric discussed by Morduch, since I have been interested only in the borrower's well-being. To adopt Morduch's suggested terminology, I have been adopting the "socially concerned" rather than the "Wall Street" point of view.

REFERENCES

Costabile, L. (1995), "Institutions, social custom and efficiency wages models: alternative approaches", *Cambridge Journal of Economics*, October, pp. 605-623.

Costabile, L. (1998), "Ordine spontaneo ordine negoziato? Conflitti e risoluzione dei conflitti nella nuova teoria economica delle istituzioni", in A.Amendola (ed.), *Istituzioni e mercato del lavoro*, Naples, ESI.

Graziani A. (1980), "Malthus e la teoria della domanda effettiva", Introduction to L.Costabile, *Malthus. Sviluppo e ristagno della produzione capitalistica*, Turin, Einaudi.

Graziani A.(1984), "Moneta senza crisi", *Studi Economici, n.24*.

Graziani, A. (2004), *The monetary theory of production*, Cambridge, Cambridge University Press.

Hausman D.M. and M.S. McPherson (1996), *Economic analysis and moral philosophy*, Cambridge, Cambridge University Press.

Kymlicka, W. (1990), *Contemporary political philosophy: an introduction*, New York, Oxford University Press.

Lewis A.W. (1953), "Economic Development with Unlimited Supplies of Labour", *Manchester School of Economic and Social Studies*, May.

Morduch, J. (1999), "The microfinance promise", *Journal of Economic Literature*, XXXVII, 4, December, pp.1569-1614.

Nozick R. (1974), *Anarchy, State and Utopia*, New York, Basic Books.

Nussbaum, M. (2000), *Women and human development. The capabilities approach*, Cambridge, Cambridge University Press.

Nussbaum, M. and A. Sen (1992) (eds.), *The quality of life*, Oxford, Clarendon Press.

Sen, A. (1970), *Collective choice and social welfare*, Holden Day, 1970.

Sen, Amartya (1987), *The standard of living*, The Tanner Lectures, Clare Hall, Cambridge 1985, with contributions by John Muellbauer, Ravi Kanbur, Keith Hart, Bernard Williams, Cambridge, Cambridge University Press.

Sen, Amartya (1993), "Capability and well-being", in M. Naussbaum and A. Sen (eds.), *The quality of Life*, Oxford, Clarendon Press.

Sugden R. (1986), *The economics of rights, co-operation and welfare*, Oxford, Basil Blackwell.

Varian, H.R.(1979), "Distributive justice, welfare economics, and the theory of fairness", in F.Hahn and M.Hollis, *Philosophy and economic theory*, Oxford, Oxford University Press (originally in *Philosophy and public affairs*, vol.4, 1974-5, pp.223-47).

Woolcock, M.J.V. (1999), "Learning from failures in microfinance: what unsuccessful cases tell us about how group-based programs work", *American Journal of Economics and Sociology*, vol.58, pp.17-42.

Yunus M. in collaboration with Alan Jolis (1997), *Vers un monde sans pauvreté*, Edition Jean-Claude Lattès; Italian translation: *Il banchiere dei poveri*, Milan, Feltrinelli, 1998.