

SOCIAL CAPITAL AND CREDIT IN A JAVANESE VILLAGE

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ABSTRACT

The objective of this study is to investigate empirically the influence of social capital on the rural credit in the case of a Javanese village. Estimation results indicate difference impact of social capital on each type of credit. Meeting attendance was found positively influence the amount of formal credit. Meanwhile, number of memberships negatively affects the amount of informal credit. This study also confirms that the rural elites have more accessibility to economic opportunities such as formal credit than non-elites do. Therefore, this study suggests that the implementation of formal credit program in rural areas should consider not only the existing social capital but also the elites in the rural society. This approach perhaps bring improvement on the role of formal credit program as an anti poverty program in rural areas.

Key words: *social capital, rural credit, rural elites.*

INTRODUCTION

Low access to formal credit persists in most developing economies. Poor households usually do not have access to guarantee mechanism, such as non-real estate-based collateral (van Bastelaer 2000). He argues this situation, combined with the overall lack of information about these potential borrowers', creditworthiness, and contributes to a virtual exclusion of this group of borrowers from formal credit markets. According to recent development of social capital literatures, that exclusion could be eliminated by social capital. For examples a study by Grootaert (1999) that address the relationship between social capital and welfare in the case of rural areas of three provinces (Jambi, Central Java and East Nusa Tenggara) found social capital positively influence access to credit.

The objective of this research is to investigate the impact of social capital on the rural credit in the case of a Javanese village. Empirically, social capital in this study refers to dimensions of local associations. Considering on the specific context of study, investigating the impact of social capital on credit is not only on the overall credit but also on types of credit, formal and informal one. Moreover, this study also analyse the influence of village leader factors on the rural credit.

RESEARCH FRAMEWORK

Poor households in rural areas do not familiar with formal credit, which deliver funds through formal financial institutions, such as commercial banks. Therefore, formal credit institution needs a mediation or substitution. Narayan and Prittchet (1997) argue that social capital could to a better flow of information between creditors and borrowers and hence less adverse selection and moral hazard in the market for credit. The guarantee of groups and pressure by social network credit are important techniques to improve credit performance (see Rhyne and Otero 1994).

In the case of Tanzania, Narayan and Prittchett (1997) found that a larger fraction of households in villages with higher social capital report using credit for agricultural improvements. In the case of Indonesia, Grootaert (1999) concludes that households with higher social capital are better able to obtain credit. He found that members of financial associations more likely to obtain credit than non-members and the obtained credit amounts were much larger. There are one-fifth of all memberships that its prime objective is financial. However, he also indicates that other local

associations, whose prime objective is not financial, also contribute to access to credit. In other-words, all associations whatever its prime objectives are important to increase the access to credit. Van Bastelaer (2000) also argues that the social networks are important elements of most type of formal or informal programs that provide credit access to the poor.

It is interesting to take a further investigation since recent studies do not yet analyse the impact of social capital on specific type of credit. In Indonesia, the major reason of households join local associations is to improve their access to credit and savings (Grootaert 1999). We have to mention that Grootaert found that a large part of local financial associations in his study is located in Central Java. However, contrast to East Nusa Tenggara, the dummy variable of Central Java is insignificant both in the model of access to credit and amount of credit received. Central Java has a tradition of ROSCAs (Gootaert 1999). Other study found that more than one-third of rural households in Bantul (a sub-district in Yogyakarta) are members of ROSCAs (Brata 1999).

ROSCA is one of informal financial institutions. Other sources of informal credits are local moneylenders, informal pawnshops, and trade credit. Generally, the fund of ROSCA is rather small than other financial associations. ROSCAs is also already popularised as female activities. The problem is the rural society tends to discriminate the females. In the Grootaert's study, the coefficients of female head of household are insignificant.

Previous studies shows that low access to formal credit persist in Indonesia. For example, Van Diermen (1998) found that fewer respondents that have tried to access commercial (bank) credit and less that received credit although more than one-half of respondents have the bank accounts. In the case of small industrialists in Bantul Yogyakarta, Brata (1999) found only less than 10 percents of rural small industrialists has access to credit from banking institutions although their bank accounts are sufficient for credit rating. Therefore, as Bastelaer (2000) have mentioned, the poorest members of society often do not access to micro-finance services. Limited access to formal credit is an important reason for poor people to borrow from informal markets. In this situation, formal financial institution is a complement of informal ones (Ghate 1988).

Recent credit schemes that designed to combat poverty in Indonesia also have critical aspects such as in the controlling mechanism and conditions to access the credit (Cameron 1999). Both aspects may lead rent-seeking or money politics practices. These issues are critical since communities, groups,

or networks that are isolated, parochial, or counterproductive to society's collective interests (see: World Bank 2000). Therefore, social capital does not guarantee poor people to access formal credit.

Tonkiss (2000) warns that the forms of social capital are not simply or necessarily conducive to economic development, in two respects. The first has to do with inequality, the second with questions of capacity. According to Tonkiss, where resources of social capital are unevenly distributed, social networks can be a basis for corruption, cronyism, or other forms of rent-seeking behaviour.

Therefore, local associations could be the rent-seeker's vehicles to exploit the recent credit schemes. The association that sponsored by a corrupt government is vulnerable to rent-seeking behaviour by its members that have a closed link to the government. At the village level, the corrupt members of associations probably are the village leaders or the local elites. As Grootaert and van Bastelaer (2001) have mentioned, the role of specific village leader or other influential individual in the internal dynamic of community is acknowledged. In this situation, one may expect that social capital does not automatically increase the access to economic opportunities and resources such as formal credit.

The second point of Tonkiss' critic on the effect of social capital is the questions of capacity. She suggests that social networks cannot simply create physical or financial capital where this does not already exist. Strong social ties become useless under domination of 'mainstream' economic and social networks. 'Network poverty' in this sense refers not to the absence or weakness of social network, but to the difficulty of accessing opportunities or resources through these networks. Therefore, talk about 'social capital', here, can become a way of not talking about poverty. Grootaert (1999) also indicates these notions. Although he argues that investing in social capital is a sensible strategy for poor households in Indonesia, however he also suggests that the poor have to work their way into social capital while the rich 'buy' their way.

EMPIRICAL FINDINGS

Data Description

Dukuh Senden in Prambanan, a sub-district in Sleman, Yogyakarta Indonesia was the location of field survey. Questioner is partially adopted from World Bank (1998) and our previous study (Brata 1999). Survey was

conducted in August 2004. Total respondents in this survey are 70 head of households or about 37 percents of total households in Sanden. Social capital indicators were inspired by Grootaert's work that analyses dimensions of local association (Grootaert 1999). The dimensions of local associations that applied in this research are the number of membership, meeting attendance, and participation in decision-making. In order to capture the "benefit" of local elites status, survey also collect the information do the respondent is a village official or village informal leader. Note that these indicators indicate social capital of head of households due to the role of head of households in their household.

The number of memberships is the number of memberships of head of household in local associations. Field survey found that more than 80 percents of head of households are member of local financial associations and *pengajian* (Moslem praying group). On average, each head of household join in five associations. TABLE 1 shows that average membership of the group with access to formal credit is larger than the other group. However, in the case of informal credit, average membership of the group with credit access is smaller than the no-access group.

Since meeting of association is also a media for information sharing, therefore, members that often attend in meeting perhaps will have better information and networking than other members will. The average of meeting attendance of respondents is 3.04 in the last three months. Table 1 shows mean of meeting attendance of group with access to credit are larger than the other group. For example, in the case of formal credit the average of meeting attendance is 3.27 and 2.88 for each group, respectively.

The survey also asked respondents they were 'active' or 'not active' in the decision making process in the association. This question was only addressed to an association that most important for the head of household. The survey found 51 respondents (72.9%) respond that they active in the decision making process in association. Table 1 indicates that proportion of "active" respondents in the decision making process in the group whose credit access is larger than the other group.

This study also asks to respondents about their social positions in the village community. The first issue is does the head of household was a village official during or before the survey conducted. The second one is does the respondent was an informal leader in the village. In order to capture both issues, the surveyor ask to each respondent to determine what is the social background they used in their involvement in facing social issues or problems in the village daily life. Note that each respondent may not only a

formal leader but also informal one. Both indicators perhaps represent the village elites position that makes them superior in the credit access than other members of society in their village. As shown in TABLE 1, there are 23.0 percents of respondents in the group that have access to formal credit were categorised as formal leaders. Similar figure also found in the second indicator of the village elite aspect. For example, in the case of informal credit 7 percents are informal leaders.

TABLE 1 *Descriptive Statistics of Social Capital and Credit (Mean)*

Social capital indicators	Have access to credit					
	Formal+informal		Formal		Informal	
	No (n=10)	Yes (n=60)	No (n=40)	Yes (n=30)	No (n=16)	Yes (n=54)
Number of memberships	4.00	3.08	3.05	3.43	3.81	3.04
Meeting attendance	2.80	3.08	2.88	3.27	2.75	3.13
Decision making	0.60	0.75	0.60	0.90	0.63	0.76
Formal leader	0.20	0.12	0.05	0.23	0.25	0.09
Informal leader	0.00	0.08	0.03	0.13	0.06	0.07
Monthly income (000 rupiahs)	1,130.00	759.17	676.25	993.33	1,100.00	726.86
Amount of credit (000 rupiahs)	-	1,413.50	-	2,607.33	-	122.04

TABLE 1 also shows two different relations between income and the credit type. In average, monthly income of respondents that have access to formal credit are larger than the average income of group without access to formal credit. In the contrary, monthly income of respondents with access to informal credit is smaller than the group that has no access to this credit type. As already known, informal credit in rural area only cover small credit. Therefore it is not surprising that average amount of informal credit is very smaller comparing to formal credit. In average, amount of formal credit of 30 respondents are Rp 2,607 millions while in informal credit are only Rp 122.040.

The distribution of respondents based on the source of credit is presented in TABLE 2. This table shows that 85.7 percents of respondents have access to credit. There are 72.9 percents of respondents whose credit from ROSCA. It is not surprisingly since ROSCA is an informal credit institution that still important for rural people. Other important credit sources are banking institutions and cooperation.

TABLE 2 *Source of Credit*

Source of credit	n	%
Family/relative	10	14.3
Friend/neighbor	4	5.7
Seller/trader	10	14.3
ROSCA	51	72.9
Bank	21	29.0
Cooperation	18	25.7
Other	1	1.4
Total	60	85.7

Regression Results

To investigate the relationship between social capital and credit, this study applies econometric approach. It refers partially to the model that has applied by Narayan and Pritchett (1997) and Grootaert (1999). The dependent variable is amount of credit received. There are two groups of independent variables. The first group is the social capital indicators. The second group is the rural elite factors that consist of village officials or formal leaders and village informal leaders dummy variables. In addition, the third group is the characteristic of household that represent by the household's monthly income. Ordinary least square (OLS) employs to estimate the equation of credit that consists of informal and formal type.

Since there are two type of credits, estimation run on each credit type to explore the impact of social capital and other factors on each credit. Dependent variable in this estimation is the amount of credit. Definition of these variables was already discussed in the description data. Regression results are presented in TABLE 3.

In the column of 'amount of total credit', estimation result shows three variables that significantly influence the amount of credit. These variables are meeting attendance, dummy variables of formal leader, and dummy variable of informal leader. These dummy variables were argued as proxies of the elite position issues.

However, estimation results indicate difference impact of social capital on each type of credit. Meeting attendance was the important determinant on the amount of formal credit. The positive sign of meeting attendance indicate that household which its head have high meeting attendance tend to get high amount of formal credit.

TABLE 3 *Regression Results*^a

Independent Variable	Dependent Variable		
	Amount of Total Credit	Amount of Formal Credit	Amount of Informal Credit
Intercept	-922181,0 (-0,901)	-1065082 (-1,044)	142900,8* (3,518)
Number of memberships	-209659 (-0,860)	-178784 (-0,735)	-30875* (-3,190)
Meeting attendance	539755,5** (2,292)	526287,3** (2,241)	13468,208 (1,441)
Decision-making	176758,5 (0,314)	172868,2 (0,308)	3890,238 (0,174)
Dummy formal leader	1356886*** (1,772)	1360693*** (1,782)	-3806,403 (-0,125)
Dummy informal leader	3146249* (2,973)	3136522* (2,971)	9726,351 (0,231)
Monthly income	0,785 (1,650)	0,777 (1,637)	7,956E-03 (0,421)
R squared	0,445	0,444	0,168
F-statistic	8,421	8,393	2,121
Number of observations	70	70	70

^a * denotes significance at 1% level; ** denotes significance at 5% level; *** denotes significance at 10% level. Figures in parentheses are t-ratios.

Meanwhile, social capital indicator that determine amount of informal credit is number of memberships. However the sign of this coefficient indicate that membership have negative relationship with informal credit. Intuitively this finding indicates that respondents with high memberships in local associations tend to avoid informal credit. The negative relation between number of memberships and amount of credit are also found in formal credit although statistically insignificant.

Estimation results indicate that decision-making participation does not influence the amount of credit in all type of credits. Income variable also does not have significance impact of the credit. Note that applying monthly expenditure, as an alternative variable for monthly income does not make statistical improvement.

The regression results also give other interesting finding on the impact of formal and informal leader position of respondents. The dummy variables give positive and significance influences on the amount of formal credit but insignificance on the informal credit. In the village daily life, the local government officials and informal leaders perhaps have an advantage position than other member of society. As found in this study, they have better access to economic opportunities such as formal credit from banking institutions.

CONCLUSION

The objective of this study is to investigate empirically the impact of social capital on the rural credit. Social capital in this study is focussed on three aspects of local association: number of memberships, meeting attendance, and participation in decision-making of head of households. Based on empirical results on the formal and informal credits, social capital has difference impact on each type of credit. Meeting attendance was found positively influence the amount of formal credit. Meanwhile, number of memberships negatively affects the amount of informal credit.

This study also analyse two social aspects that represent social position of respondents in their village community on the credit. These aspects are 'formal leader' and 'informal leader' that were assumed make those rural elites have superior position to access the formal credit access than other members of society in their village. Estimation results indicate that both variables give positive and significance influences on the amount of formal credit, but insignificance in the case of informal credit. This finding confirms that the rural elites have more accessibility to economic opportunities such as formal credit than non-elites do.

Therefore, this study suggests that the implementation of formal credit program in rural areas should consider not only the existing social capital but also the social structure of the rural society. This approach perhaps bring improvement on the role of formal credit program as an anti poverty program in rural areas.

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