research institute, makes it possible to assess such claims. It suggests that fears of an epidemic of over-indebtedness due to excessive lending by MFIs are exaggerated.

The state may be India's most developed microfinance market but it is hardly awash with microcredit. Whereas 82% of households have borrowed from informal sources, mainly village moneylenders and relatives or neighbours, only 11% have an MFI loan. On average, borrowers also owe over four times as much to informal lenders, which charge far higher rates, than they do to MFIs.

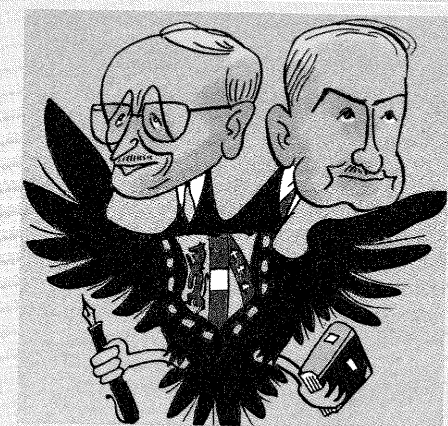
Nor have MFIs in the state faced rising defaults, as they should have if borrowers were really in over their heads. Some reckon that MFI clients are able to stay afloat only by borrowing from one microlender to repay another. But the CMF survey finds that a mere 3% of those who borrow from MFIs have more than one such loan; in contrast, 70% of people have at least two informal loans. People with several MFI loans also tend to take them out simultaneously, rather than staggering them, as they would if they intended to use one to pay instalments on another. Some probably take out several MFI loans for the good reason that they need a larger lump sum than any single small loan can provide.

Credit is not all that poor people need. There is also an enormous unmet demand for savings accounts. Reducing transaction costs enough to make it feasible to cater to very small savers is difficult. MFIs might be able to do this more cheaply than banks, because they have existing relationships with the kinds of people who would use such basic savings accounts. Yet MFIs are prohibited from taking deposits, or even from acting as local collection agents for commercial banks. Fewer restrictions on microlenders, not new ones, would be the best way of helping the poor. ■

Buttonwood | Taking von Mises to pieces

Why is the Austrian explanation for the crisis so little discussed?

JOHN MAYNARD KEYNES is back. The British economist has modern intellectual champions in Paul Krugman and Robert Skidelsky. For all today's talk of austerity, a policy of Keynesian fiscal stimulus was adopted by most governments in the immediate aftermath of the credit crisis.



In contrast policymakers seem to show a lot less interest in the economic ideas of the "Austrian school" led by Ludwig von Mises and Friedrich Hayek, who once battled Keynes for intellectual supremacy. Yet the more you think about recent events, the odder that neglect seems.

A one-paragraph explanation of the Austrian theory of business cycles would run as follows. Interest rates are held at too low a level, creating a credit boom. Low financing costs persuade entrepreneurs to fund too many projects. Capital is misallocated into wasteful areas. When the bust comes the economy is stuck with the burden of excess capacity, which then takes years to clear up.

Take that analysis piece by piece. Were interest rates held too low? The case seems self-evident for Ireland and Spain, where the European Central Bank was setting a one-size-fits-all monetary policy. Many people would also argue that the Federal Reserve kept rates too low. Some lay the housing boom of 2003-06 at the Fed's door, others criticise the central bank's tendency to slash rates whenever the financial markets wobbled.

Was capital misallocated? Again most people would accept that too many houses and apartments were built in Ireland and Spain, as well as individual American states like Florida and Nevada. In some places these dwellings may sit idle for a while, keeping downward pressure on property prices.

Economists who would not describe themselves as Austrian have reached conclusions that chime with Hayek. Carmen Reinhart and Kenneth Rogoff, in their book "This Time is Different", argued that past financial crises have been followed by long periods of sluggish growth. Hyman Minsky, an American economist who died in 1996, said that the financial cycle led to economic volatility. Long booms tended to result in excessive risk-taking and "Ponzi finance", where investors buy assets with borrowed money in the hope of quick capital gains. Minsky's reputation has soared since the start of the credit crunch.

Nassim Nicholas Taleb is a very popular financial author thanks to his books "Fooled by Randomness" and "The Black Swan". One of his principal ideas is the difficulty of forecasting given the role of chance and extreme events. That echoes the views of Hayek, who wrote that "the curious task of economics is to demonstrate to men how little they really know about what they imagine they can design."

The Austrians may have said smart things about the boom, but what about the bust? One criticism is that the Austrians offered a "counsel of despair", suggesting that the authorities do nothing while a crisis blows itself out. At least the monetarists propose cutting rates and expanding the money supply and the Keynesians promote deficit spending.

But Lawrence White, an economist at George Mason University in Washington, DC, argues that this is an unfair characterisation. "Hayek was not a liquidationist," he says, referring to the philosophy of Andrew Mellon, President Herbert Hoover's Depression-era treasury secretary, who wanted to "purge the rottenness out of the system". Hayek believed the central bank should aim to stabilise nominal incomes. On that basis Mr White thinks the Fed was right to pursue the first round of quantitative easing, since nominal GDP was falling, but wrong to pursue a second round with activity recovering.

Mr White is one of the few current economists to promote the Austrian approach. This may be because economists divided into Keynesians and monetarists in the 1970s. You might think that the Austrians would find common cause with the monetarists. But Milton Friedman rejected their analysis, stating in 1998 that: "The Austrian business-cycle theory has done the world a great deal of harm." Efficient-market theorists disliked the Austrians because they appeared to assume that businessmen could act irrationally.

The libertarian streak of the Austrians still has its fans. Glenn Beck, a lachrymose Fox News pundit, turned Hayek's "The Road to Serfdom" into an unlikely bestseller earlier this year. Being associated with Mr Beck will not persuade many academics to take Austrian economic ideas seriously. Given the repeated credit booms and busts of the past 40 years, that may be a pity.

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