



What is the evidence of the impact of microfinance on the well-being of poor people?

The concept of microcredit was formally introduced in the early 1970s to reduce poverty by providing small loans to poor households. Microcredit has evolved over the years and does not only provide credit to the poor but now spans a range of other services including savings, insurance, remittances and non-financial services such as financial literacy training and skills development programmes; it is consequently now referred to as microfinance. A key feature of microfinance has been the targeting of women on the grounds that, compared to men, they perform better as clients of microfinance institutions and that their participation has more desirable development outcomes.

Despite the apparent success and popularity of microfinance, there is no clear evidence yet that microfinance programmes have broadly positive impacts for most participants. While anecdotes and other inspiring stories purport to show that microfinance can make a real difference in the lives of those served, rigorous quantitative evidence on the nature, magnitude and balance of microfinance impact is still scarce and inconclusive.

Because of the growth of the microfinance industry and the attention the sector has received from policy makers, donors, private investors, the media and the public in recent years, existing microfinance impact evaluations need to be re-investigated and the robustness of claims that microfinance successfully alleviates poverty and empowers women need to be scrutinised more carefully.

Methodology

We conducted a systematic review following the general systematic review guidelines as set out by the Cochrane and Campbell Collaborations. We searched 11 academic databases, and 4 microfinance aggregator and 8 NGO or aid organisation websites; we also consulted bibliographies of reviewed books, journal articles, PhDs, and grey literature. The papers obtained through the search were screened in several stages. In the final stage

we classified them by research designs in descending order of internal validity, i.e. randomised control trials (RCTs), pipeline designs, with and without comparisons (in panel or cross-section form), natural experiments and general purpose surveys. These five categories were cross-classified with three categories of statistical methods of analysis, which in descending order of internal validity are 2-stage instrumental variables methods (IV) and propensity score matching (PSM), multivariate (control function), and tabulation methods. We found nearly 3000 studies. To restrict the detailed review to a reasonable number of studies which were likely to have good validity, we adopted a heuristic scoring of research designs and methods of analysis; combining these scores into a single value, provided a cut-off to exclude papers which could be expected to be of low quality. As a result we reduced 2643 papers to 58 which we examined in detail. What are the implications for policy and research?

Results

Our overall judgement draws mainly on RCT and pipeline studies, although we also devoted considerable attention to the most prominent with/without studies which have been highly influential in validating orthodox favourable views of microfinance impacts.

There are only 2 RCTs of relevance to our objectives and our judgement is that one has low-moderate and the other high risk of bias. Both are of limited external validity. Neither finds convincing impacts on well-being. We found 9 pipeline studies, which have been reported in ten papers. All the pipeline studies are based on non-random selection of location and clients, and most have only ex-post cross-section data, some with retrospective panel data, allowing only low validity impact estimates of change in outcome variables.

We find no robust evidence of positive impacts on women's status, or girl's enrolments, but this may partly due to these topics not being addressed in the more valid studies (RCTs and pipelines). Well known studies



which claim to have found positive impacts on females are based on weak research designs and problematic IV analyses which may not have survived replication or reanalysis using other methods, i.e. PSM.

Given their importance in validating perceptions of the beneficence of microfinance interventions we invested a considerable amount of time in assessing with/without studies which have low inherent internal validity notwithstanding analysis with sophisticated methods. In particular we discuss the two historically most significant studies (Pitt and Khandker, 1998 and USAID funded studies in India, Zimbabwe and Peru), which, partly as a result of their prominence, have been replicated. The replications fail to confirm the original beneficent findings, and conclude that there is no statistically convincing evidence in these studies to either support or contradict the main claims of beneficence of microfinance. This is likely to be due to their weak research designs and poor data quality.

Conclusions

The majority of the microfinance impact evaluations included here investigate group lending and credit only interventions which do not reflect the diversity of the sector, and hence this does not allow us to reach a conclusion as to the impact of the microfinance sector as a whole; individual lending is a more recent phenomenon that has not yet been evaluated widely. Paired with doubts about the research designs and analytical methods used by the various microfinance impact evaluations, we can neither support nor deny the notion that microfinance is pro-poor and pro-women.

Our report shows that almost all impact evaluations of microfinance suffer from weak methodologies and inadequate data, thus adversely affecting the reliability of impact estimates. Nevertheless authors often draw strong policy conclusions generally supportive of microfinance. This may have led to misconceptions about the actual effects of programmes, thereby diverting attention from the search for perhaps more pro-poor interventions and more robust evaluations.

Recommendations

It is still unclear under what circumstances, and for whom, microfinance has been and could be of real rather than imagined benefit to the poor; not surprisingly we focus our policy recommendations on the need for more

and better research. While there is currently enthusiasm for RCTs as the gold standard for assessing interventions, there are many who doubt the universal appropriateness of these designs. Indeed there may be something to be said for the idea that this current enthusiasm is built on similar foundations of sand to those on which we suggest the microfinance phenomenon has been based. Therefore, the development community may be well advised to engage constructively with evaluation techniques and to understand their limitations so that more reliable evidence of impact can be provided hopefully leading to better outcomes for the poor.

Such research could use a range of research designs (not just RCTs), and analytical methods, to assess both the short and longer-term impacts of microfinance. Well designed and conducted studies should be complemented with qualitative tools prior to, as well as during and after, embarking on quantitative studies. Also, and fashionably, orthodox social survey methods can be enhanced with coordinated behavioural and experimental economics research with microfinance participants (lenders and actual and potential borrowers) to gain a better understanding of the mechanisms underlying microfinance participation and conduct, and the role of unobservable factors likely to confound relationships between microfinance and well-being outcomes for the poor, in this context. Exploring why what appears to have been inappropriate optimism towards microfinance came to be so widespread would also be a suitable subject for further research which would involve political scientists.

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