

DOES MICROCREDIT REALLY HELP THE POOR?

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Financial system contributes to the economic growth by ensuring efficient resource allocation to the most needed sector. It provides channels by which funds are transferred from those with surplus fund to those with deficit. The system prevents funds to be left abundant yet it ensures that funds are well used in productive activity. In this case, both the surplus unit and the deficit unit are better off. The surplus unit earns return from the fund lent whilst the deficit unit receives the capital needed to consume. This is how financial system supports the economy to develop and grow further.

The above argument has ignited the idea of providing loan to the poor as part of development programs. Such loan provision might help the poor to lift themselves out of poverty by providing necessary capital to set up a productive-income-generating activity. It is strongly believed that Microcredit will make self-employment and small enterprise possible for the poor, a requisite condition to jump out the poverty line.

A strong empirical support of the above was coming from the Nobel-Prize-Winner Yunus with his Grameen Bank. Yunus was considered successful in providing small loan to the people of a poor village in Bangladesh so that it has gained international recognition as one of the pioneer of a microfinance program as part of poverty alleviation strategy (Lard and Barres, 2007 cited by Santen 2010). The concept of Grameen has gained wide popularity and been replicated throughout the world. Since Grameen, a different concept of microfinance has also emerged backed with the strong conjecture of the ability of microloan to change the lives of the poor - a belief that needs further evidence, though.

The impact of microloan have on poverty has been an immense debates, yet a conclusive one. Most influential study by Pitt and Khandker (1998) showed a positive impact that

microcredit has on consumption of the poor especially those provided to women. Aside of having criticized on Pitt and Khandker's work by suggesting no difference in consumption level between those who have access to microcredit and who do not, Morduch (1998) favourably found that access to credit allows the poor to smooth their income as well as their consumption, factors that are also very important for the poor. Following the work, Khandker (2005) strengthens the evidence by asserting that microcredit does reduce the poverty among the poor through increasing consumption and growing local income. However, revisiting the same data and replicating the three previous studies, Roodman & Morduch (2009), weakens the result of the studies.

Despite of the contradicting results, one should question whether that the increasing consumption actually relates to the income or profit from the business financed by the microcredit or the increasing consumption is directly financed by the credit obtained and not through increasing productivity as it originally expected. The previous suggest a successful microcredit program and the later shows otherwise. Microcredit should be an income aid not a consumption aid (Magner (2007)).

A review on the history of microcredit done by Dichter (2007) suggests that such credit was often used by the poor for consumption and rarely for business investment. Here microcredit is unlikely to fulfill the demand of capital to start a business yet it is more likely satisfying the consumptive desire of an individual. As such, the provision of credit may jeopardize the livelihood of the poor by putting them further down in the valley of debt thus keeping them below poverty line instead of taking them out. As cited by Dichter (2010), Milford Bateman argues much of microfinance work prevents growth and is "anti-developmental"

More recent study by Bernajee et. al. (2009) provides additional insight in regards to the impact of microcredit on household consumption. Whilst did find a positive correlation between microcredit and profit of micro-enterprise and household expenditure, their study also reveals different nature of expenditures across different household. Their randomized evaluation suggest that those who already have a business or have the

potential to start a business is likely to use the credit to expand its existing business and as initial investment. In this case, increasing consumption is likely related to betterment in productivity of the poor. On contrary, among households who do not own a business and have no potential to start one use microcredit to increase their spending for nondurable and unproductive goods (e.g. food) or to pay more expensive debts. In such case, microcredit is very unlikely to have a productivity impact, hence, doubtly can reduce poverty.

Most of pioneer studies on microfinance impact take the household consumption as an indicator to observe the microcredit impact on the lives of the poor. Nevertheless, whether that higher consumption is really suggesting that the live of the poor has been improved is another issue that should be examined further. In addition, poverty is a very complex social phenomenon which goes far beyond consumption and expenditure rate. Its dimensions include access to education, health, gender equality, empowerment and other social issues. How microfinance is affecting those social issues surrounding poverty is not really a clear cut.

Bernajee et. al 's (2009) randomized study on microfinance impact conclude that though it is successful in affecting household expenditures and promoting business activity, the success story does not reappear when examining microfinance's effect on the core issues of poverty: education, health and empowerment. Nevertheless, on longer term, the higher expenditures and profit may translate into a better education, health and women empowerments among the poor.

A more pessimistic view is sounded by Dichter (2007). Intriguing by saying microfinance as a longstanding idea of poverty reduction resting on little empirical evidence of success, he also citing several studies showing evidences which go against what microfinance proponents expect. Karlan and Zinman (2009), as cited by Dichter (2007), found that microfinance disappointingly does not reduce poverty.

Despite of the inconclusive debates on the empirical result, it is also appealing to questioning the role of microcredit as poverty alleviation strategy in the view of poverty theory. A fundamental, thus philosophical, question which should be raised is then whether microcredit addresses the root cause of poverty. Simply put, is loan provision fundamentally needed by the poor or is it not? -- The question barely touched.

Though lowness of income is always considered as main reason of poverty and by which it is measured, it is actually only the consequences of its real cause which goes beyond financial and material matters. The real cause of poverty lays on the inability of the poor to involve in income-productive activity whether an opportunity to do so is exist or not. It is the lack of knowledge, skills and capabilities that creates poverty. Khan (2007) as cited by Santen (2010) argues that higher employment rates might not reach the poor or improve their condition. It is investment in human capital and capabilities that will increase productivity that leads to pro-poor economic growth which will have impact on poverty reduction.

This argument is quite the opposite of what microcredit proponents have long believed that the poor has the necessary entrepreneurial skills to start a small business but only lack in the capital needed. Hence providing loan will enable them to do so. This assumption, however, is a bit too heroic, not to say unrealistic, as not everyone will have such skills. Most of the poor, especially the very poor, is very unlikely to have the knowledge and the capabilities to run a business and able to encounter the complexities of running a business, even a small one. Financial illiteracy and the ability to comprehend the nature of the microfinancial product might exacerbate the problem.

Money is surely something needed by the poor and lack of income is surely a huge problem for them yet providing loan may not be a proper solution. Development wise, the borrowed fund must be translated into a productive activity so that the holy mission of providing it in the first place will possibly be realized. In order to do so, the poor, the beneficiary of the microcredit, must have the capability to well use the fund obtained. In

other word, microcredit can help the poor yet it alone is not fulfilling what the poor is really needed.

One might say it is like a problem of egg and hen: which one did come first? Education, health and empowerment? Or the income which will enable the poor to have better education, health services and other necessities? Yet, how can they generate income if they do not have the knowledge to do so and unable to fulfill their basic needs? To be wiser, it seems that the two are no difference in term of the importance. Hence, having an anti-poverty program which addresses the two issues, economical as well as non-economical, may translate into a more optimum result.

Providing only financial services to the poor will not likely to do any better for them as it is not addressing the core issue of poverty. The provision of microcredit should be accompanied by other program that helps to improve the capabilities of the poor. Microcredit program should not be the sole instrument of poverty reduction (Khandker (1998) as cited by Santen (2010)). The provision of credit must be followed by development program that will upgrade the skills and the knowledge of the poor. The program may vary from a more sophisticated entrepreneurial training, health education and to a simple reading and writing class. Consultation services that monitor and control the use of the fund should also be provided along the loan period.

Microcredit may help five percents of its participants cross the poverty line each year as some studies had shown. Nevertheless, there are another 95% of them did not make it over the finish line, meaning stay in poverty. Most of them who fail going out of poverty are often the poorest of the poor. Among the identified reason of the failures are helath, natural disaster and, of course, education. Having a microcredit programs that link to services addressing the aforementioned issues can improve the impact of microcredit on poverty (Magner (2007)).

Some of pioneering microfinance institutions has integrated additional services with their microfinance product and shown a delightful result in terms of greater outreach and better

development impact on their participants. As cited by Magner (2007), BRAC of Bangladesh links its microfinance program with training and food program in cooperation with the government and World Food Program. The others are Pro Mujer adding healthcare services and Fonkoze of Haiti offering literacy and educational program. These microfinance institutions have put more meaning to microfinance as a development tool.

Summing up, it is not to say that the idea of microcredit as poverty alleviation tool is way too far above the sky. Apart from the academic as well as empirical debacles, microcredit may have positively affected the livelihood of the poor. Nevertheless, poverty is a multi-dimensional social phenomenon that is too complex to be addressed by simply providing the poor with access to capital. Though the development of microfinance has added microsavings and microinsurance on the map to enhance the efficacy of microcredit to fight poverty, it needs more than just financial services to help the poor. As a development tool, microfinance must integrate their product with other services that are more developmental in nature. Microcredit program, even more complete microfinance, which gives only financial services to the poor, is just like its macro-financial-institution counterpart differs only in the poor as the customers. In such case, no developmental motives exist, thus less impact on the livelihood of the poor.

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