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Microfinance: What Do We Know? Where Do We Go?

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ABSTRACT

There is little doubt that the revolution in microfinance lending has revolutionized how we think about lending and, in particular, lending to the poorest of the poor with no collateral to pledge. There is also no doubt that the micro lending movement has been an overall success globally. However, there are increasingly emerging signs that all might not be well with the micro lending industry. The problems are not unlike that facing any rapidly growing industry and there is little doubt that the micro lending industry globally has grown in leaps and bounds, perhaps too quickly, over the past four decades fueled by its very own successes. This article summarizes the recent literature related to some of the questions that we consider important and are under researched as fodder for researchers, academics, students and policy makers to spur further thinking and research.

1

Introduction

Micro lending is a global phenomenon where small unsecured loans are made to the poorest people usually in groups so that the borrowers can invest the money in some business or related entrepreneurial venture and improve their social and economic conditions (Churchill and Frankiewicz, 2006).¹ The practice was first conceived of and operationalized by a Vanderbilt trained Economist, named Mohammed Yunus, in the villages of Bangladesh in the late seventies. Since those humble beginnings, microfinance has come a long way. Almost every country around the world has some form of a microlending program usually targeted toward the very poor and there are thousands of microfinance institutions (MFIs) that are engaged in such loan making. According to the most recent data from *miX Market* there are 2,726 MFIs in 117 countries.² We observe the greatest number of MFIs in India (218), followed by Russia (127), and the Philippines (119). We display regional MFI intensity in Table 1.1. As displayed in the table below, the largest number of MFIs

¹Loans are also used by borrowers to fund their consumption needs like buying a major consumer item like a television set or to pay for a wedding, for income smoothing and related purposes.

²Data is from <https://reports.mixmarket.org/crossmarket> covering 1999 through 2016.

Table 1.1: Regional distribution of MFIs using panel MixMarket data from 2000-2016

Region	N of MFI	Percent	Cumulative
Africa	823	30.19	30.19
East Asia and the Pacific	368	13.5	43.69
Eastern Europe and Central Asia	500	18.34	62.03
Latin America and The Caribbean	571	20.95	82.98
Middle East and North Africa	67	2.46	85.44
North America	1	0.04	85.47
South Asia	396	14.53	100
Total	2,726	100	

are located in Africa, Latin America and the Caribbean followed by Eastern Europe and Central Asia.³ According to Consultative Group to Assist the Poor CGAP (2015), Eastern Europe remains the highest subsidy funding recipient (31 percent of the overall funding), followed by sub-Saharan Africa. Interestingly, Middle East and North Africa are the only regions that didn't observe a decline in subsidized funding growth in 2014, relatively to other regions.⁴

Since inception, hundreds of articles have been written examining almost every aspect underlying these loans and how it may, or may not, impact loan repayment rates which is an important, but not the ultimate, measure of success of the Program itself. Through such research, theoretical as well as empirical and experimental, we have improved our understanding of how and why certain aspects of group (and, more

³It is important to note that the MIX data is self-reported and, therefore, does not represent the entire universe of MFIs. By the same token, however, the data is considered sufficiently representative to have a significant volume of research generated with it for well over the past decade.

⁴We also observed a substantial growth in funding to Eastern Europe and Central Asia from 2011(3.9 billion USD) to 2013 (6.39 billion USD). The Middle East and North Africa grew very rapidly from 2009(0.66 billion USD) to 2011(1.90 billion USD), followed by the growth in sub-Saharan Africa from 2009 (1.64 billion USD) to 2014 (2.87 billion USD). However, South Asia & Latin America and the Caribbean have seen a decline in funding over those years. For example, Latin America and the Caribbean in 2009 received 2.15 billion USD whereas in 2014 the region only received 1.74 billion USD. Similarly, South Asia received 3.09 billion USD in 2009 and 2.98 billion in 2014.

recently, individual) lending frameworks work. However, more research awaits!

There is little doubt that the revolution in lending started by Muhamad Yunus and his Grameen Bank in Bangladesh has revolutionized how we think about lending and, in particular, lending to the poorest of the poor with no collateral to pledge. There is also no doubt that the micro lending movement has been an overall success globally. However, there are increasingly emerging signs that all might not be well with the micro lending industry. The problems are not unlike that facing any rapidly growing industry⁵ and there is little doubt that the micro lending industry globally has grown in leaps and bounds, perhaps too quickly, over the past four decades fueled by its very own successes.⁶

In the following sections, we summarize the recent literature related to some of the questions that we consider important and are under researched as fodder for researchers, academics, students and policy makers to spur further thinking and research. As with any review article, ours will, no doubt, reflect our own biases as to what we consider are the important/interesting questions which may, or may not, resonate with some of our readers. For this, we offer our apologies in advance. Also, the ordering of the topics in no way reflects their relative importance. Rather, we want to tell a story and the arrangement of the material is an attempt on our part to do just that. We also wish to apologize to all whose research/writings we may have either inadvertently or, in some cases, deliberately omitted from the article for a variety of reasons not related to the quality, or the veracity, of the work itself. In that sense, writing an article of this nature certainly does not win one friends and we are sensitive to it. However, we hope that our article will be an exception to that rule.

⁵See Gonzalez (2010) discussion about MFI rapid growth

⁶See a nice discussion in Morduch (1999a) involving Grameen Bank and the challenges faced by this venerable institution in recent years regarding declining loan repayments and other associated challenges related to managing costs and financial self-sufficiency. Morduch (2000) also goes on to criticize the notion of a “win-win” advocated by many who espouse that it is possible to follow good banking principles and alleviate poverty at the same time.

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