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## Perhaps microfinance isn't such a big deal after all

By Tim Harford

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Last December, I showed some unwitting prescience by worrying about a [backlash against microfinance](#), the practice of providing small loans – or perhaps savings products or insurance – to poor people. I fretted that there was little compelling evidence that it worked.

A year later, the evidence is arriving and the backlash has begun. The Boston Globe published an [article](#) in September, subtitled, "Billions of dollars and a Nobel Prize later, it looks like 'microlending' doesn't actually do much to fight poverty." Other media have weighed in on all sides, with [The Wall Street Journal](#) concerned about a microcredit bubble. What is going on?

Three important randomised controlled trials were unveiled this year. **In one**, economists Dean Karlan and Jonathan Zinman persuaded a lender in Manila to tweak a credit-scoring computer program so that it randomly awarded or denied loans to marginal borrowers. The results were disappointing, considering that an earlier Karlan-Zinman study of a consumer-finance lender in South Africa had shown more substantial benefits from microcredit, despite annual interest rates of 200 per cent. In Manila, male-owned businesses tended to become more profitable after a loan, and female-owned businesses did not. This runs counter to a strong focus on women in the microfinance culture. The loans produced no improvement in diet or income about 18 months down the line.

**A second trial**, by Abhijit Banerjee and three other MIT economists, studied a more traditional scheme in India, which lent to groups of women. Spandana, a leading microfinance operator, agreed to randomise the way it entered the Hyderabad market. The company chose 104 suitable areas of the city but at first only marketed loans in 52 of them. Again, the results were modest. Households seemed to use the loans to buy more expensive goods and then cut back on everyday spending to repay the loan, but income did not rise, nor were there improvements in health or women's empowerment. Business owners did manage to improve profits. The time horizon, again, was less than two years.

**A third trial**, of a micro-savings scheme in rural Kenya, was more encouraging. Economists Pascaline Dupas and Jonathan Robinson found that the savings accounts were popular among women and helped them save, invest in businesses, spend more and cope with bad luck. All this was despite the fact that the accounts paid no interest and charged hefty withdrawal fees.

Microfinance fans should not feel too defensive about these mildly positive results, especially when microfinance itself has passed a market test by growing very rapidly, often without subsidies. All such trials are context-specific and have other limits: the Manila study targeted marginal borrowers, while in the Hyderabad study, Spandana was not the only microfinance lender in town.

The reason for the backlash is obvious: microfinance was supposed not just to be a useful financial product, but to emancipate women, create millions of entrepreneurs and get rid of stubborn stains on your collar. Such claims were always going to be difficult to justify – even if donors tend to lap them up in the search for the next development panacea.

David Roodman, a [microfinance expert](#) at the Center for Global Development, sums it up well: "Suppose microfinance is not having much average impact on poverty, but is giving millions of people a modicum of greater control over their lives ... is that so bad?" Other serious studies are in the pipeline. If microfinance is to thrive under the microscope, perhaps its practitioners should establish more realistic expectations.

*Tim Harford's latest book is 'Dear Undercover Economist' (Little, Brown)*

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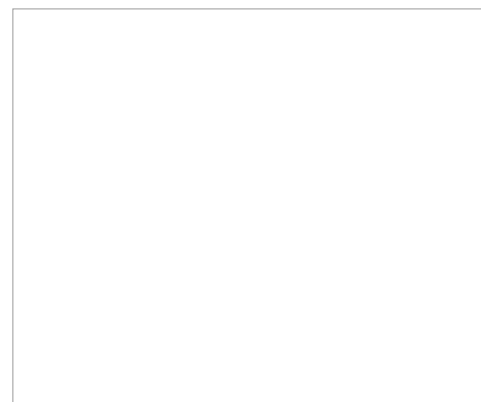
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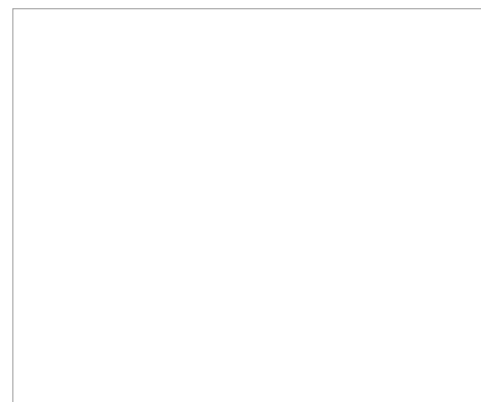
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