



Impact of Microfinance Programme on Poverty in Bangladesh

What We Already Know and What We Still Need to Know

This brief examines the analytical basis of expecting positive impact of microfinance on poverty. Based on empirical evidence it summarizes what can be concluded as known and outlines what we would still need to know about contributing of microfinance programmes to poverty alleviation in Bangladesh.

What Can be Expected?

Theoretically one could look at different types of characteristics that determine poverty. For example, national or regional characteristics, such as isolation, frequency of natural calamities, would cause poverty. Similarly community characteristics (e.g., quality of infrastructure, access to public goods), household characteristics (size of households, its assets, employment status of its members) and individual characteristics (e.g., age, education, and health) also are determinants of poverty. Microcredit programme would have strong impact on household characteristics that create self-employment and income. As for community characteristics (infrastructure, land distribution, access to public goods) and individual characteristics (age, education, employment, health), microcredit could have limited impact. Among key national or regional characteristics (environmental condition, governance, inequality) microfinance would have some impact on inequality. Also, credit is only a factor (short-term capital) in the production and therefore it is difficult to expect a major shift in the income level within a short time.

What Does the Evidence Indicate?

First, the coverage of microfinance programme has expanded at an astonishing rate and it is difficult to believe that such a growth rate can be achieved without the programme benefiting some. The aggregate time series data between 2003 and 2009 show that microcredit sector grew on average at 12% per annum.

Second, there are a few studies to show that rates of return on enterprises funded of microcredit are generally higher than the interest rate paid on microcredit. In Bangladesh, studies show microcredit BRAC experienced 24%, BRDB 35% and Grameen 53% rate of return on activities funded by microcredit.

Third and most importantly, overwhelmingly majority of empirical studies show positive impacts of microfinance on the poor.

Conceptual Framework

To understand the likely impact of microfinance on poverty, one has to consider different categories of poor and how they could be affected by access to microfinance. The poor can be divided into 4 groups:

- 'Chronic poor': their status over time would always stay below the poverty line. Microfinance can improve their condition but they still remain below the line.
- 'New poor': their poverty status over time starts from above the poverty line and then falls below it at some stage never to rise above it again. This group could again rise above the line with the help of microfinance.
- 'Transitory poor': their poverty status keeps fluctuating around the poverty line. This is also the group who can be helped to remain above the line.
- 'Graduating poor': This group starts from below the poverty line, and then graduates out of it at some stage and never slide back into poverty. Microfinance may help them to avoid sliding back into poverty.

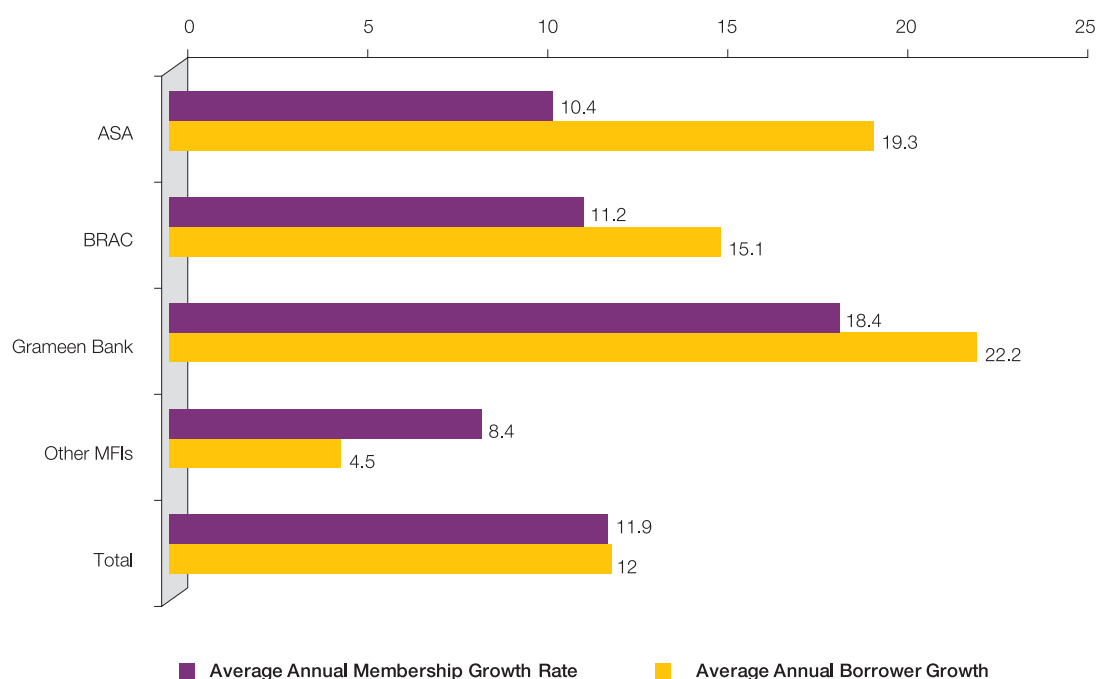
The impact of microfinance on poverty can take three varied forms:

- Participation in microfinance may lead to a permanent exit from poverty.
- Access to microcredit may provide temporary relief and avert further sliding down in poverty scale.
- The participants of microfinance programmes may lead to going down permanently further down the poverty scale.

The majority of the early impact studies like Hossain (1988), Pitt and Khandker (1998), Zahir et. al (2001) as well as comparatively recent studies like Hossain and Bayes (2009), Imai and Azam (2010), B. Khalily (2011), S. R. Osmani (2011) do show that microcredit programme has helped the poor households through raising income and consumption, empowering women borrowers. Some studies particularly show that microcredit has helped in consumption smoothing particularly to withstand shocks.

Two recent studies carried out by InM on special microcredit programmes for ultra poor—Impact Study of PRIME (2011) and Impact Study of FSVGD (2011)—indicate strongly positive impact of the programmes on the income, consumption and asset formation of ultra poor. Table presents the positive results of selected important studies, using the income or expenditure variable, which is the most common outcome variable available in the studies.

Figure: Membership and Borrower Growth of MFIs from 2003 to 2009



Source: Bangladesh Microfinance Statistics 2009

In contrast, the positive effect of credit on poverty has been questioned by a few studies like Zaman (1999), Q. K. Ahmad (2007). Those studies have found that benefits enjoyed by most of the microcredit borrowers are uncertain and many face setbacks and that the short term impact on income and consumption level could not bring any substantial change in the level of poverty. The validity of the results of some of the studies is controversial because of sample size used, for not fully separating out the effects of other variables and selection biases. A recent UKaid review paper on ‘the evidence of the impact of microfinance on the well-

being of poor people’, conducted in a worldwide context concludes that there was no robust evidence that microfinance has had a positive impact. The review has questioned the existing results relating to Bangladesh on the ground that all the studies reviewed “had weak research designs and used poor quality data.” This paper does not do any study and makes a judgment on other papers. The review questioned the results of a nationally represented household data. The criticism made by the review seems to be based on doubts about the quality of the data but the basis of the doubts has not been elaborated.

Table: Impact of Microcredit on Household Income/Expenditure

Source	Name of Organisation Studied	Impact Variable (Income/Expenditure)	Income/Expenditure (in Tk.) for Participants	Income/Expenditure (in Tk.) for Control (Non-Participants)	% change in Income or Expenditure
Hossain 1988	GB	Income, per capita	3524	2523	39.7
BIDS 1990	BRDB	Income, per household	6204	4260	45.9
IMEC 1995	Proshika	Income, per household	22244	17482	27.2
Rahman 1996	PKSF	Expenditure, per household	26390	23802	10.9
Khandakar 1998	BRAC	Expenditure, per capita	5180	4202	23.3
Khandakar 1998	GB	Expenditure, per capita	5050	4335	16.5
Halder 1998	BRAC	Expenditure, per capita	8244	6480	27.2
BIDS 1999	PKSF	Expenditure, per capita	36528	33732	8.3
IMEC 1999	Proshika	Income, per household	48635	43584	11.6
Sossain 2002	GB	Income, per household	18134	14204	27.67
Khandker 2003	GB, BRAC, RD-12	Expenditure, per capita	3923	3838	2.22
Rahman, Atiur 2005	PKSF	Annual Income, per household	58109	38968	49.1
Khalily 2010	PRIME 2 of PKSF	Annual Income, per household	53394	48505	10.10
Rabbani 2011	PRIME 3 of PKSF	Annual Income, per household	61530	45680 (benchmark)	34.7
Khalily 2011	FSVGD & UP of PKSF	Monthly Income, per household	5224	4463 (Early dropouts)	17.0

Source: Rahman [2000] and Author

Methodology Matters in Assessing Impact

Alexander-Tedeschi and Karlan (2007) study sought that varying results on empirical evidence are partly due to different methodologies used to estimate the real impact and many of the studies suffer from serious conceptual and methodological problems resulting in their failure to disentangle the effects of microfinance from that of other factors. The best possibility to get to the impact analysis is to do both before and after and with and without comparisons of longitudinal data (except cross-sectional data) along with base level surveys of programme participants and comparable programme nonparticipants.

Cost Effectiveness Analysis is Relevant for Aided Microfinance Programmes

One needs to find cost-effectiveness, and not just effectiveness, of the programme to reach a conclusion that microcredit programme, if using Government or donor support, would be the most efficient use of resources to alleviating poverty. If microcredit is not using public or donor support, then the focus is only to find out whether we are succeeding to help the poor through the microcredit revolution. There has been one attempt (Khandker, 1998) to compare the cost effectiveness of microcredit programme in comparison to other programme interventions to reduce poverty.

Summary of What We Know and What We Still Need to Know

To sum up, based on survey of theoretical reasons and empirical evidence, one can conclude

- Microcredit has had some positive impacts, though somewhat limited and mostly effective in the short run.
- Microcredit has helped borrowers to smooth consumption, particularly to withstand shocks. This has helped borrowing households to avoid sale of assets during shocks.
- Almost all studies consistently indicate positive impact of special microcredit programmes (with elements of subsidies) on ultra poor households.
- Programmes, which include more services than just microcredit, have had more significant impact on poverty than programmes offering microcredit only.
- Methodology matters in estimating the real impact (free of self-selection biases and influences of other variables). However controversy continues and a new group calls for increasing rigor in methodology particularly the need for using social experimental design in which the group receiving services and group not receiving should be exactly similar.

Even with extensive research so far, we still need to know the following

- While most studies generally confirm short run positive effect of microcredit, we still need to assess long run effect of microcredit on the poor and this will have to be done by assessing net worth of microcredit borrowing households over a fairly long period in comparison to a comparable control group observed over the same length period.
- We need to understand when shocks become a factor changing the status of the household and which assets are more important than others in offering a cushion against shocks.
- One needs to examine why the relative magnitudes of short run and long run effects vary differentially for different types of shocks and different types of households and how microfinance and other public programmes could be conducted in an effective manner in shaping the post-shock change of poverty status of different categories of households.
- It would be important to know what would be the threshold size of microcredit that gives optimal result. Since some studies show that credit plus services have a distinct stronger positive effect, it would be desirable to know the combination of what additional programmes or services with microcredit that would produce the maximum impact.
- We need to particularly understand the potential of microfinance in including growth through development of microenterprises, where the dynamics of asset formulation and the trajectory becomes important.
- When a programme involves use of public funds in the form of subsidized loan or free supporting organisation or services, we also need to have an assessment of cost-effectiveness and not just effectiveness of microcredit.