

The promise and the perils of microfinance



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14.73



The case for microfinance



- What are the elements of the case being built up in the microfinance movie?
 - That the poor have poor access to credit
 - That they are reliable borrowers
 - That group lending may help repayment
 - That microfinance can play an important part in lifting people out of poverty
 - That microfinance increases earnings, mainly through new business creation
 - That the increased earning, especially of women, leads to greater investment in human capital
 - That there is no conflict between the commercialization of microcredit and its social role.

Questions

- We have some understanding of why credit access is bad
- How is that consistent with the poor being reliable borrowers?
- What role can group-lending play?



Questions



- Does microcredit have to lift out of poverty to be useful?
- Can microcredit help people even if they don't set up businesses?
- How would they repay their loan if they don't invest?

Questions



- Why does the gender of the business owner matter?
- What could be a source of conflict between the social role of microcredit and its commercial side?



How should we interpret the evidence provided in the film?



- What is the nature of the evidence?
 - ?
 - ?
- What is problematic about it?
 - ?
 - ?
- Why do we need an RCT?
 - What else could we do?
 - What are potential problems with it?

Spandana's Program



- Traditional microcredit program
 - Group liability
 - Weekly or monthly repayment
 - Starting loan is Rs. 10,000 (~\$250)
 - Interest rate changed over the period but was around 12% per year (nondeclining balance; ~24% APR)
 - A few individual-liability loans were also given
- Spandana was already a large MFI in South India
- Not previously operating in Hyderabad.
- Agreed to randomly phase in operations in Hyderabad.



Endline sample



- 104 slums: 52 treatment, 52 control
- ~7,200 households total
- Households with the following characteristics were surveyed (more likely to become microfinance clients):
 - At least one woman aged 18-55
 - Household has lived in the slum at least 3 years
 - Not rated as someone Spandana wouldn't lend to
- Measures impact for households with these characteristics
 - results for other types of households could be different

Households at baseline



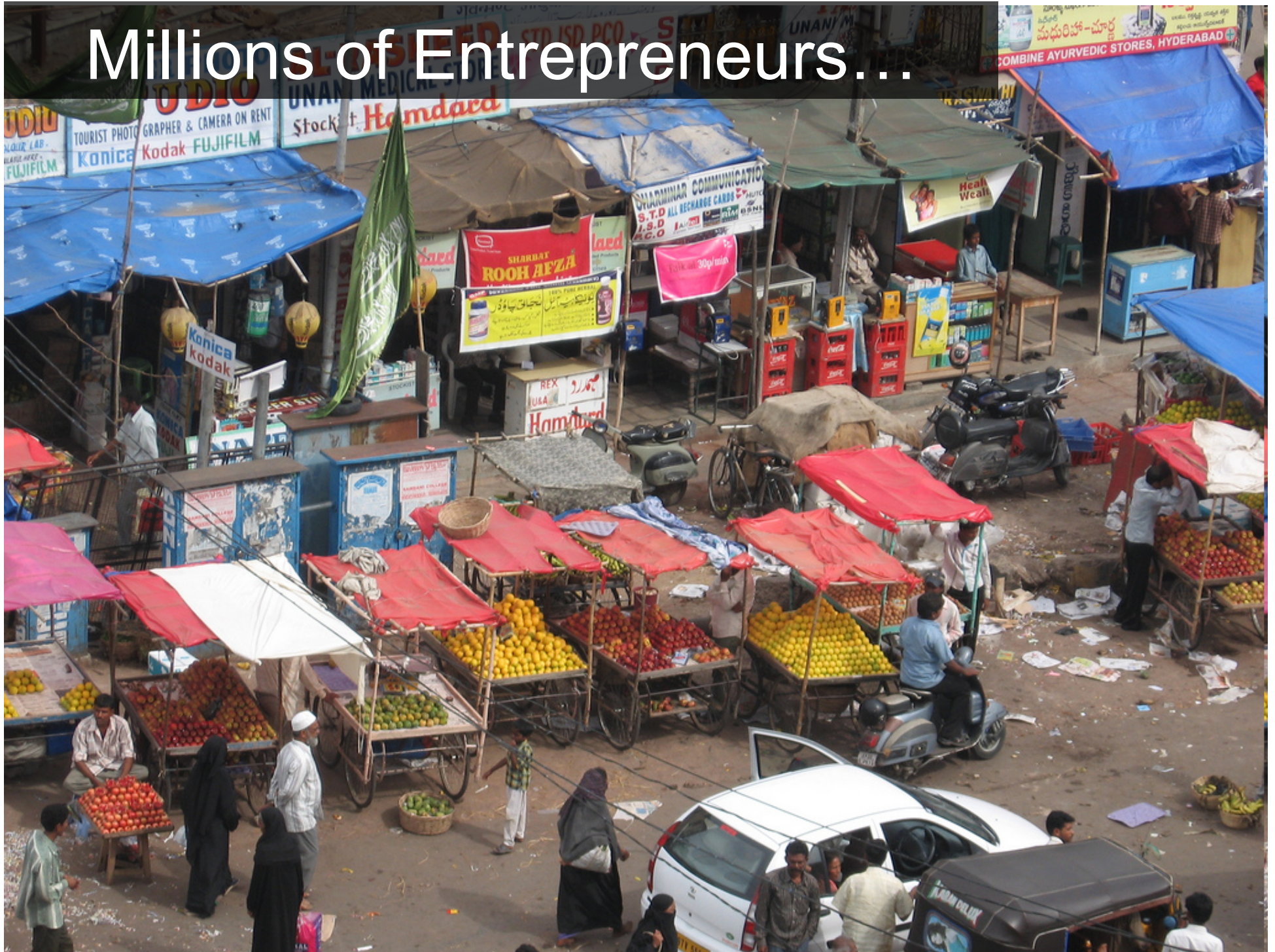
- Family of 5
- Monthly expenditure of ~Rs 5,000 (~\$125)
- 98% of 7-11 year olds, 84% of 12-15 year olds in school
- Borrowing (from friends, moneylenders, etc.) is common (69% of households); average interest rate 3.85% per month
- Almost no MFI borrowing.

Entrepreneurship at baseline

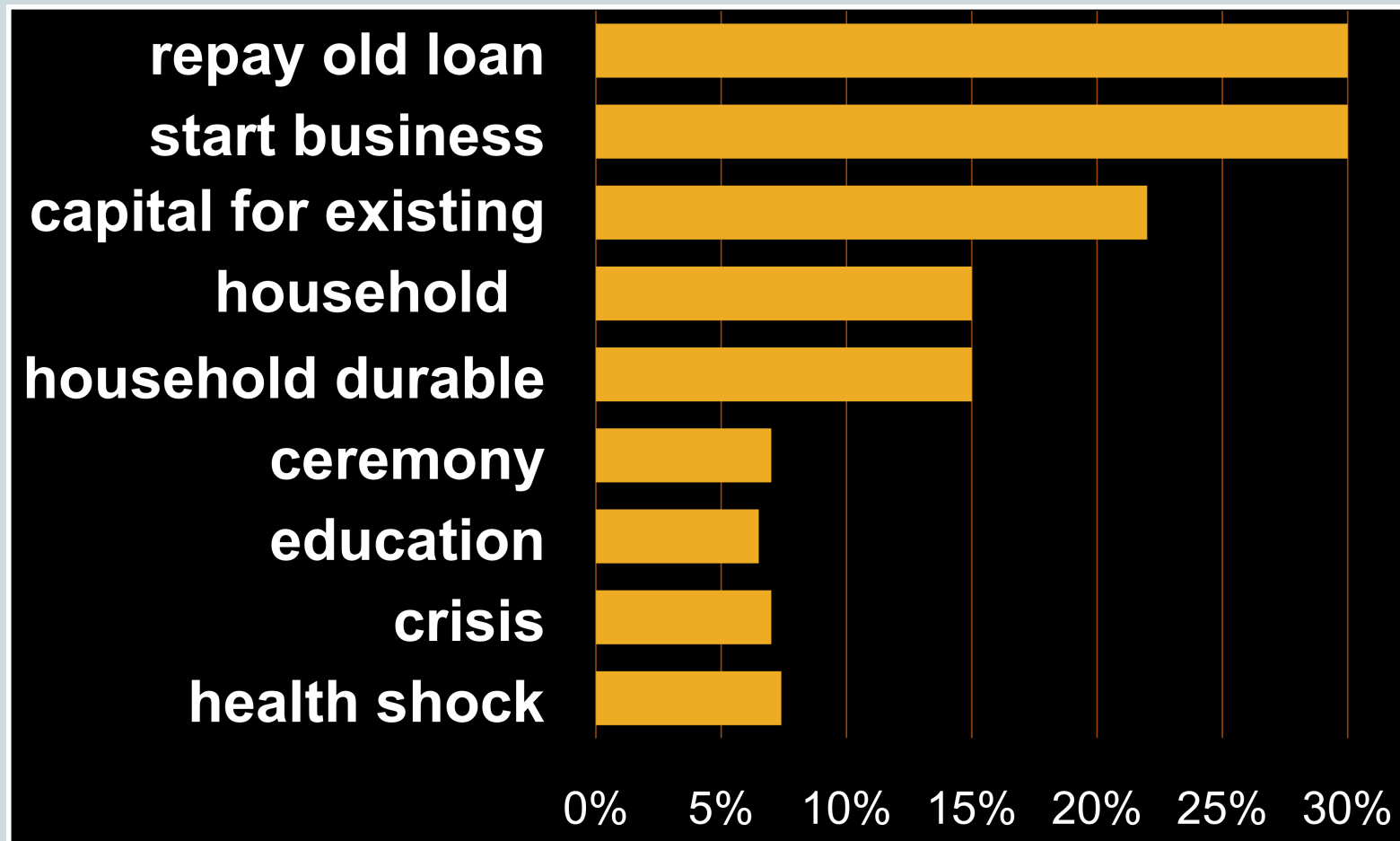


- 31% of the households run at least one small business (vs. OECD average of 12%)
 - Of these, 9% of households run more than one business
- But these businesses had few...
 - Specialized skills (mostly general stores, tailors, fruit/vegetable vendors)
 - Employees:
 - ✦ Only 10% have any employees; none has more than 3
 - Assets
 - ✦ 20% use no productive assets whatsoever.
- Scale of businesses:
 - Sales: Rs 13,000 (~\$325) per month
 - Profits: Rs 3,040 (~\$75) per month

Millions of Entrepreneurs...



Why do you want a loan?



(Control) households at endline



- The average household is a family of 6 (4.7 adu)
- Monthly expenditure of Rs 6,375 (~\$160)
- 96% of the 7-11 year olds, and 85% of the 12-15 year olds in school
- Borrowing is very common (89% of households)
 - average interest rate ~2% per month
- 18.7% have an MFI loan

What should we expect

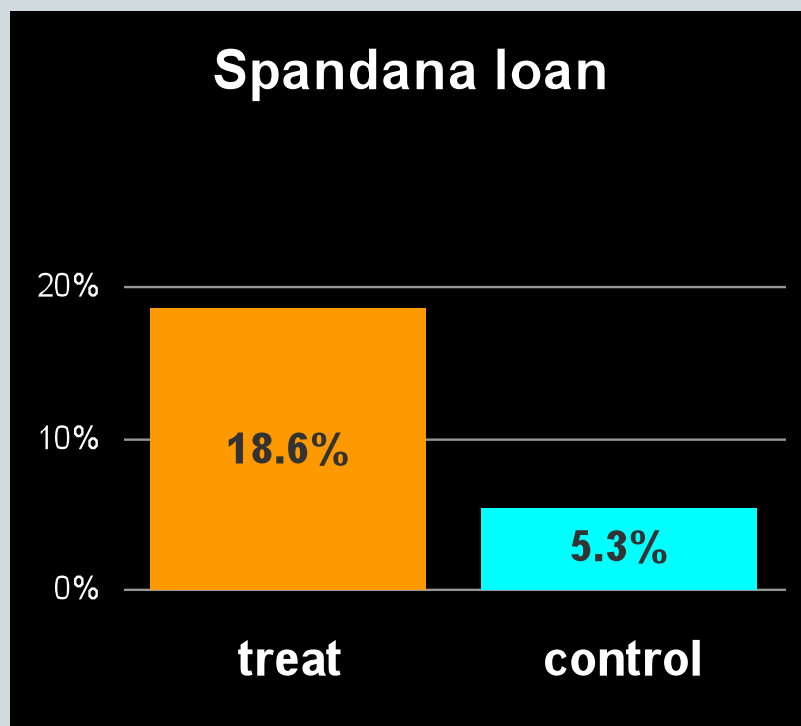


- Assume:
 - fixed cost of starting a business
 - variable cost of running it
- When credit access increases:
 - Those without an existing business decide
 - ✦ Some will start a business (richer, lower opportunity cost, those with better ideas)
 - Starting a business might involve cutting consumption
 - ✦ The rest will just finance consumption
 - Existing business owners don't face a fixed cost: borrow to increase consumption and variable capital
 - ✦ Their profits should go up
- Overall consumption may go up or down

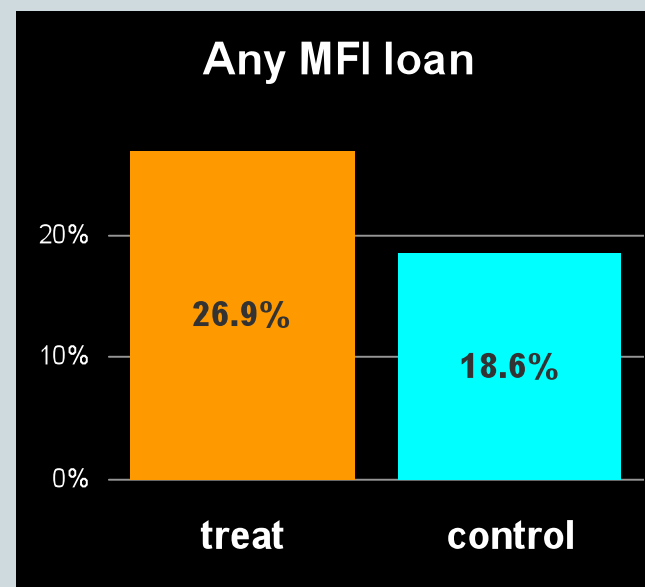
2. TAKE UP?



Spandana loan



Any MFI loan

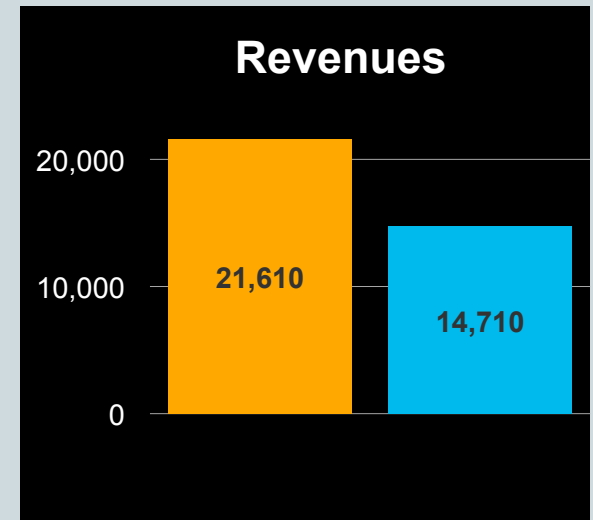
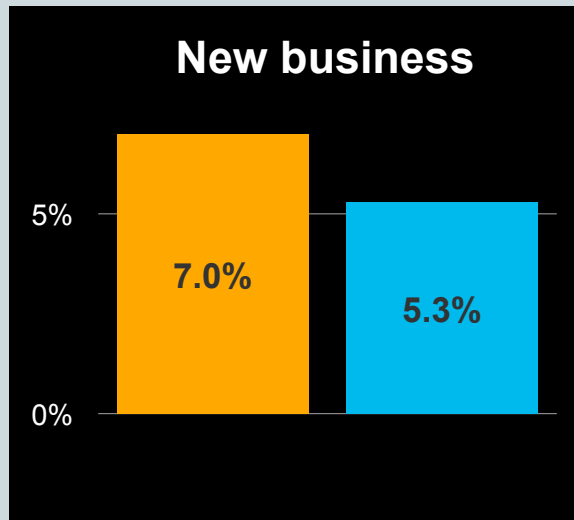


Impact on borrowing



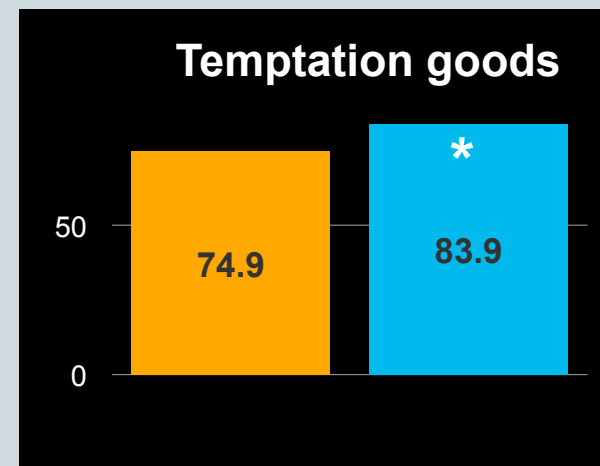
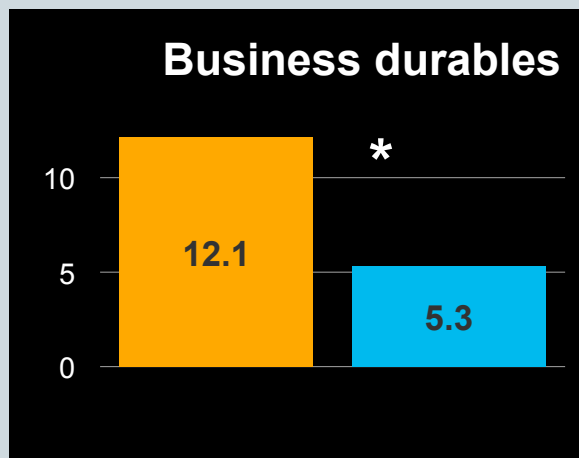
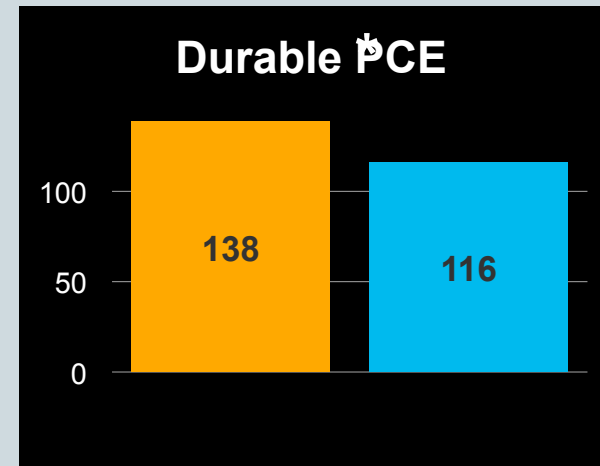
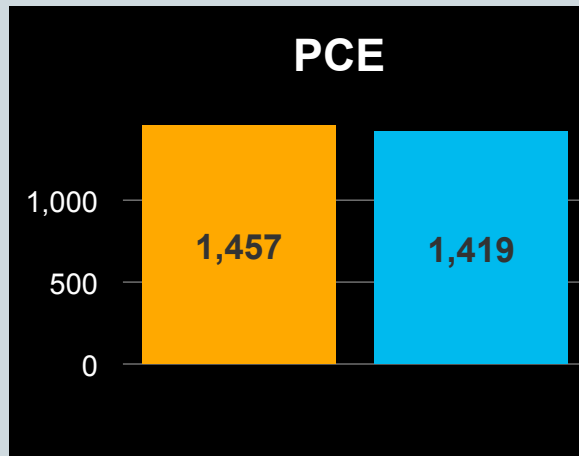
- **8.3** percentage points more MFI borrowers (Spandana or other) in treatment slums
 - **13.3** percentage points more Spandana borrowers
- Average of Rs. **1,260** of additional MFI borrowing per household in treatment slums (ITT estimate)
- These relatively low rates of MFI loan take-up are similar to those found in other J-PAL projects.

Impact on business

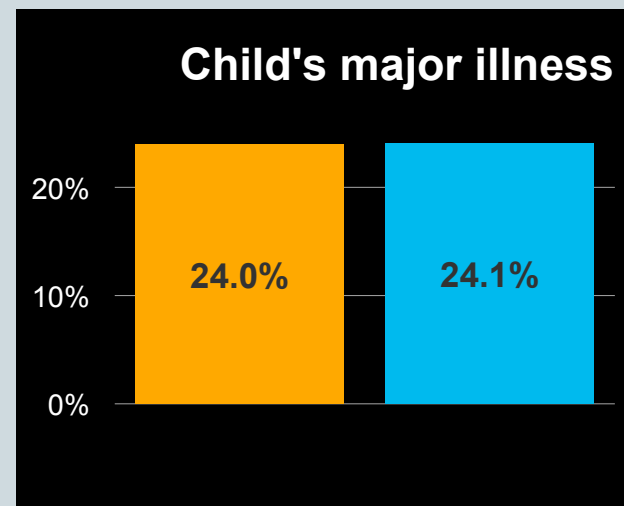
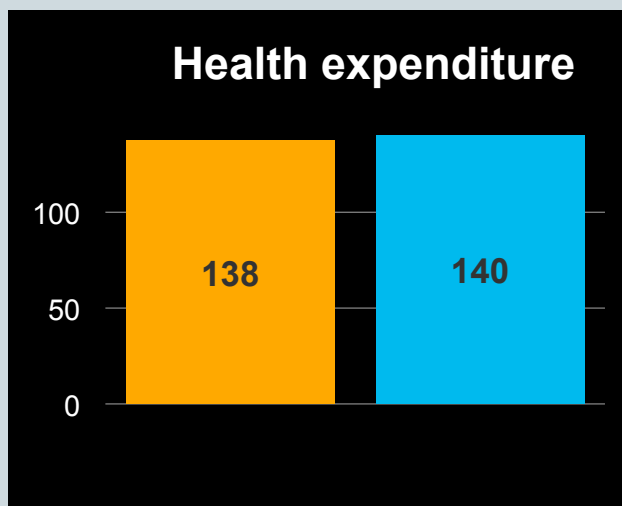
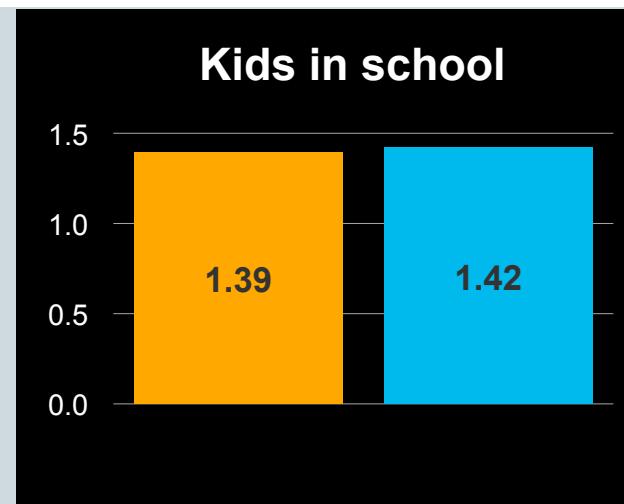
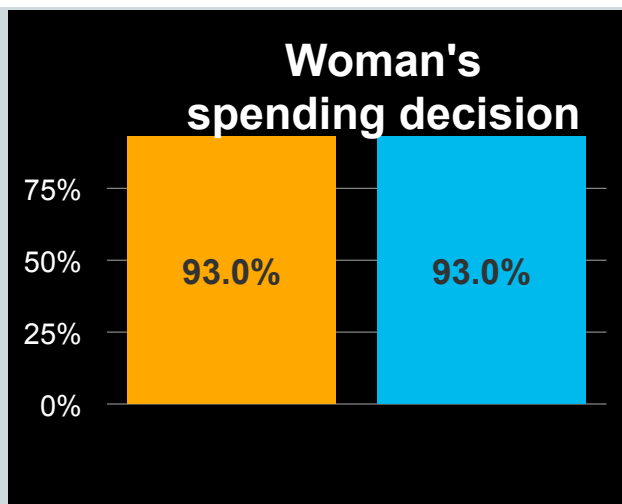


**** For those starting a business:**

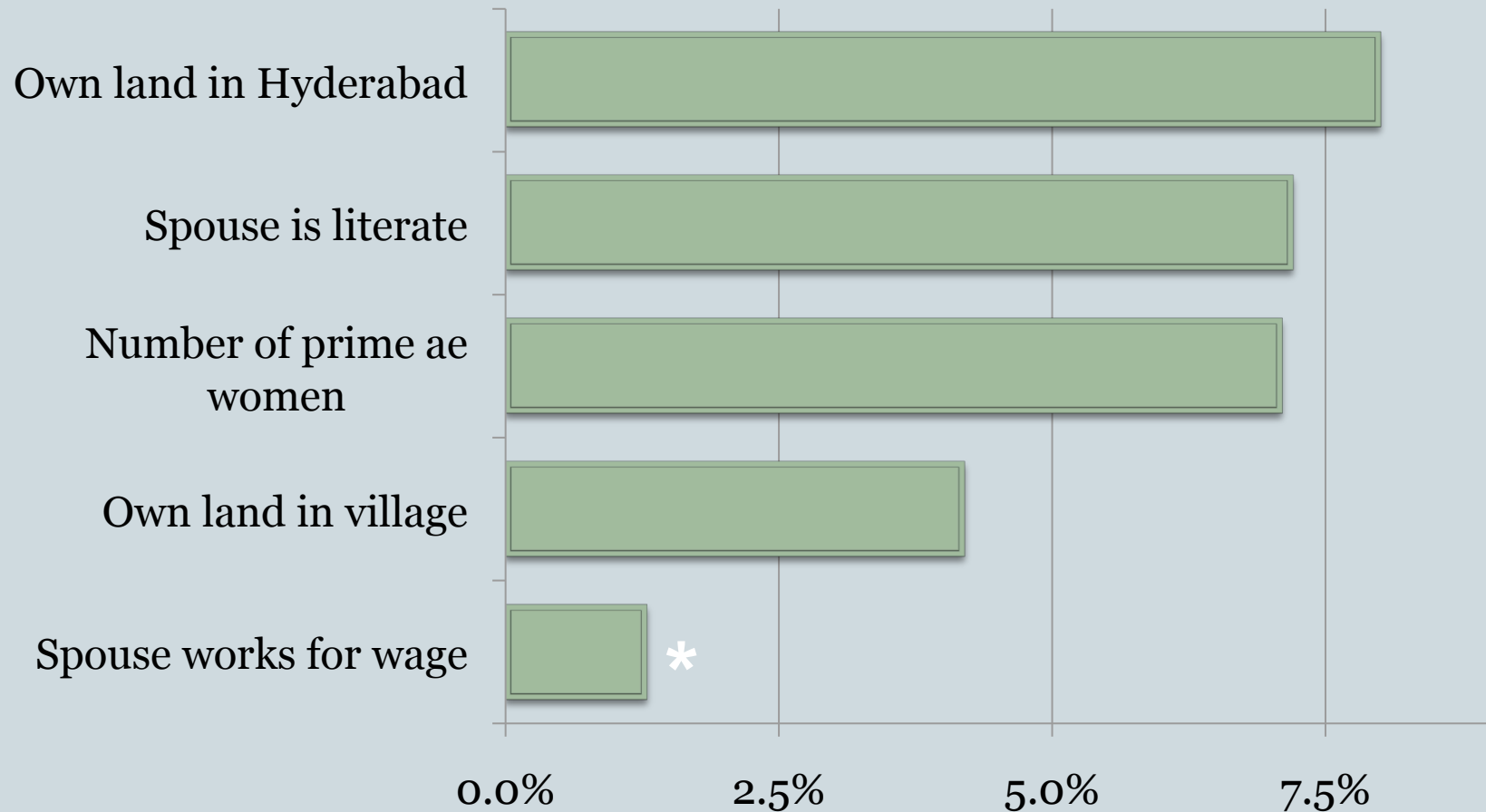
Impact on expenditure



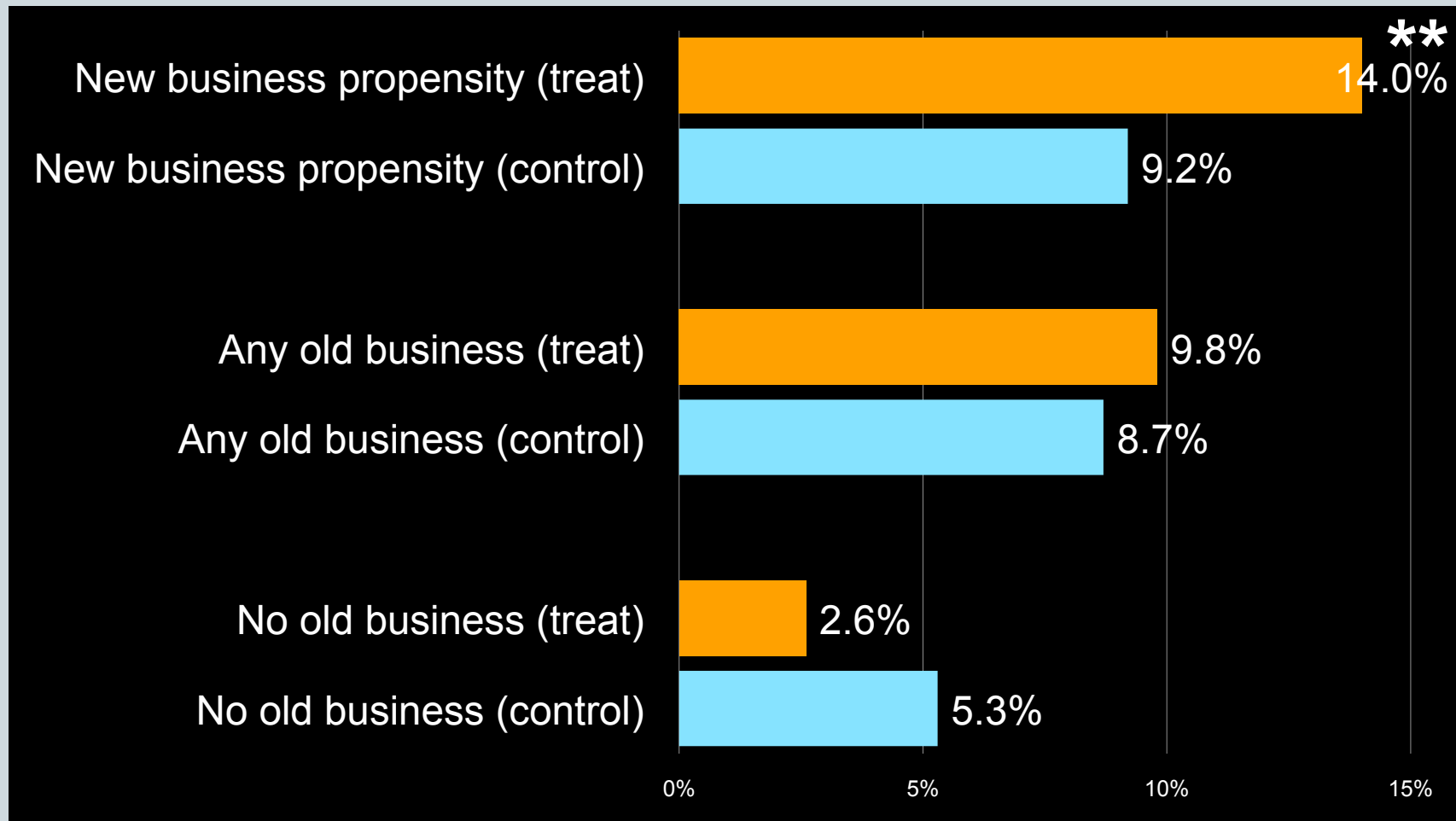
Child welfare and women “empowerment”



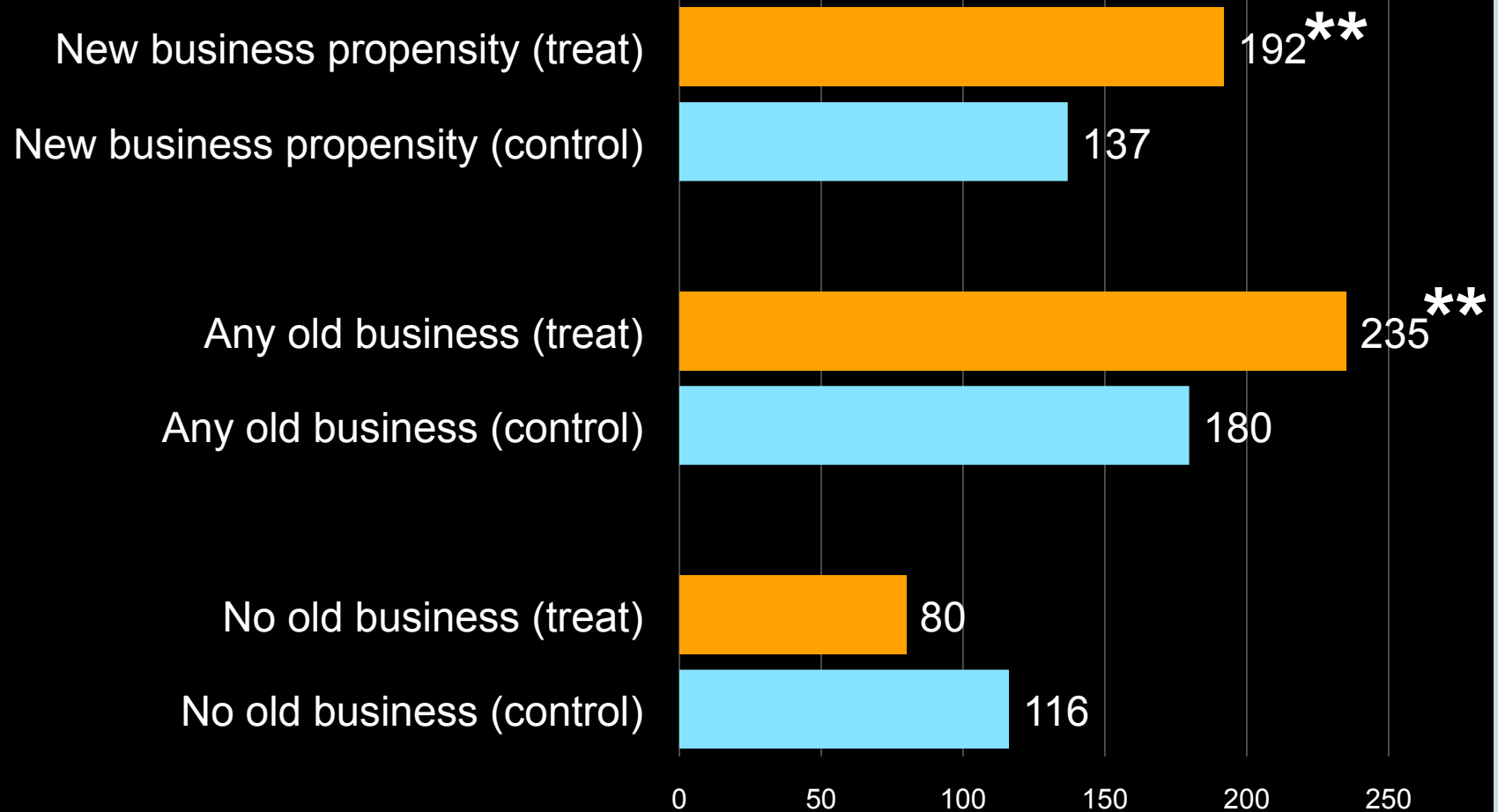
Predicting who is a likely entrepreneur



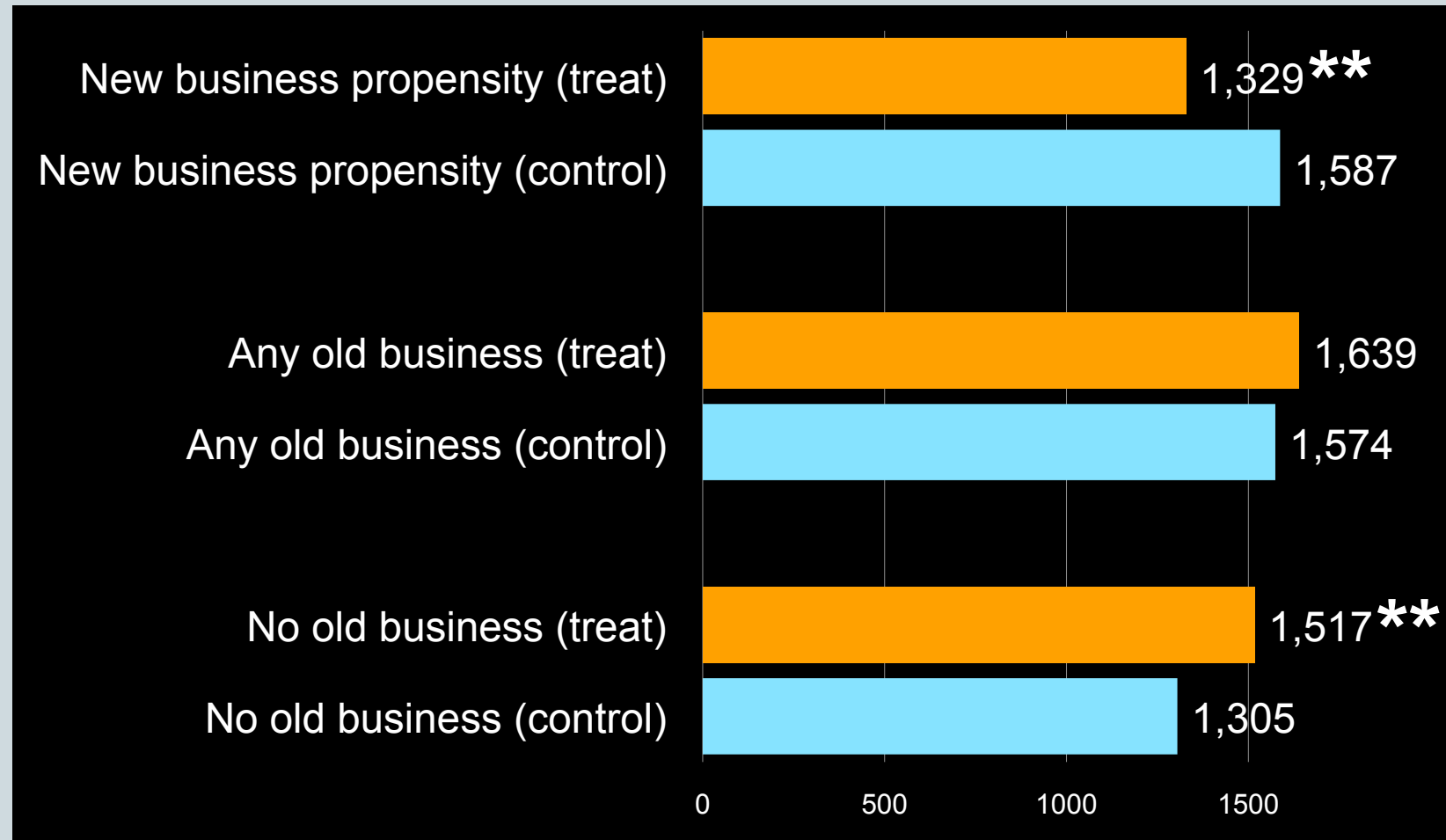
Start a new business



Durable expenditure



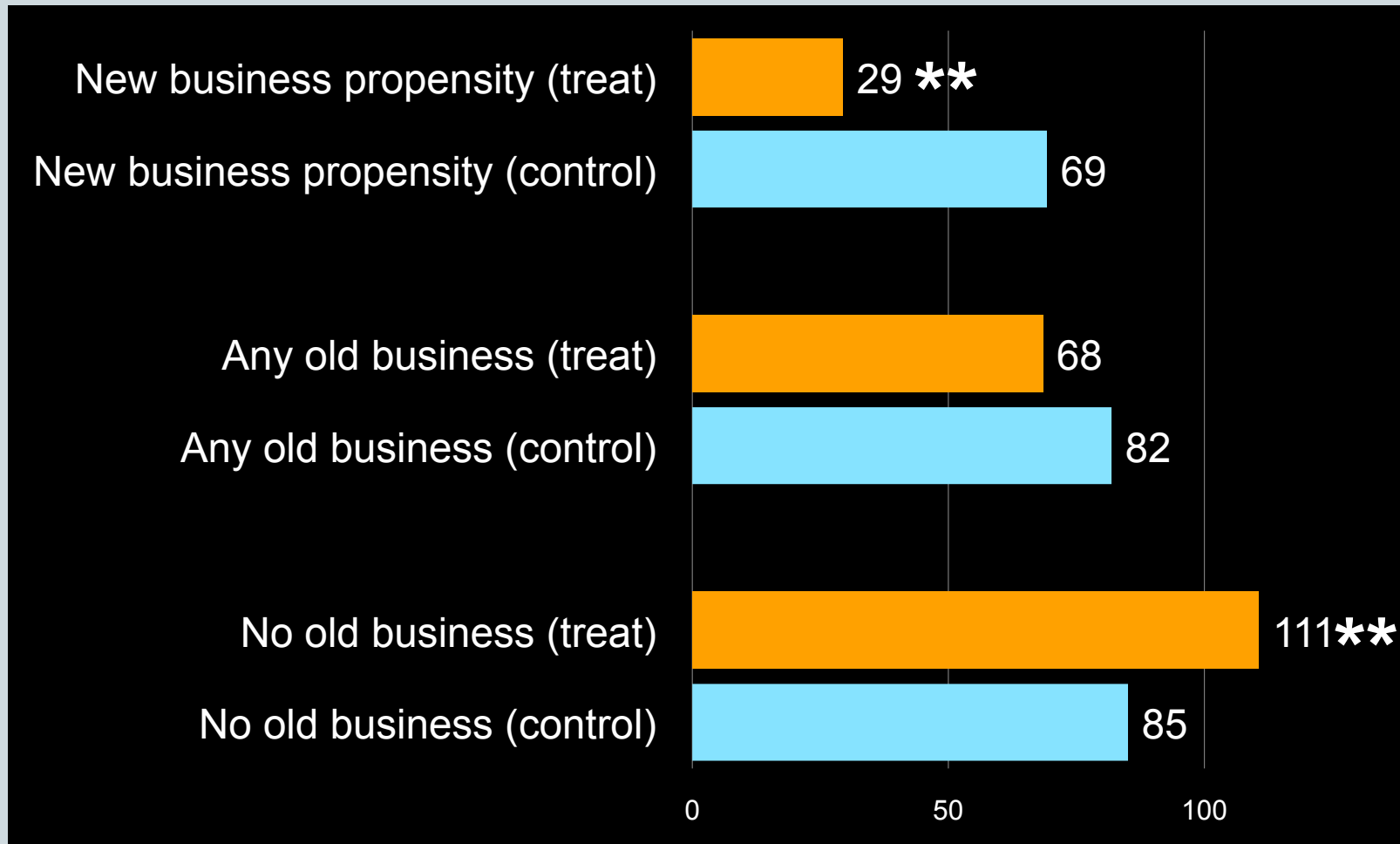
Non durable expenditure



Temptation



Temptation goods



The recent crisis



- Last few years have seen massive entry of for- profits into the microfinance sectors
- IPO of Compartamos (interest rate 100% or more) yielded huge valuation
- Inspired by this SKS, India's largest microfinance had an IPO as well (interest rate 24% or less)
 - Again raised lots of money

The new usury

- Mohd. Yunus criticized this trend: called them the new usurers
- Why did they go for an IPO?
- Is it reasonable to criticize them for doing so?



The crisis



- The SKS IPO could not have been worse timed.
- This showed that they were rich and profitable
- But this was also when a number of debt suicides happened
- Set off a political process leading to the promulgation of a new law which is close to shutting the sector down.
- Suddenly everyone is against microcredit: does the evidence warrant that?