There is now a vast literature investigating the impact of microcredit on poverty in the developing world. Such studies are by and large at the micro-level - investigating the impact of the provision of microcredit loans or a feature of microcredit contracts for a specific microfinance institution (MFI) on measures of well-being such as poverty or female empowerment. This presentation will describe the findings of a paper that evaluates the effectiveness of microfinance programs from a macroeconomic perspective. This paper relates to the conference theme of ‘Equality, Equity and Development’ and the Sustainable Development Goals of ‘reducing poverty’, ‘decent work and economic growth’ and ‘reduced inequalities’.

For many development practitioners, microfinance appears to be a win-win solution – aiming to reduce poverty while achieving financial sustainability. Despite this, microfinance has not brought about large-scale reductions in poverty and female empowerment. This paper investigates more deeply how microfinance varies across countries and asks what features of microcredit loans may improve their effectiveness in reducing poverty, spurring entrepreneurship and decreasing inequality.

We develop a model of financial intermediation which highlights the roles of credit market imperfections, MFI efficiency and occupational choice. We exploit the large cross-country variation in microcredit features and calibrate the model to data for 21 countries in the early 2000s. We then use the calibrated model to investigate the impact of a number of policies such as training for microcredit clients, deposit-taking by MFIs, credit bureaus, individual lending and lower-frequency repayment of microcredit loans. We find the largest reduction in poverty from a non-microcredit loan subsidy, and the largest reduction in inequality from the introduction of credit bureaus. Entrepreneurship is spurred the most by business training.

While existing micro-level studies are crucial for understanding the effectiveness of microcredit in various contexts, unlike this paper, very little analysis has been at the macroeconomic level with a view to understanding the general equilibrium effects of microfinance. This presentation will therefore identify features of microfinance contracts and institutions that may ensure microfinance provides the poverty alleviation and equity-inducing potential it was once thought to offer.