Steering Future Research in Microfinance : Standing Atop Existing Literature

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Abstract

Microfinance has attracted a wide array of researchers worldwide, and as a result, there has been a humungous amount of literature on the subject. Research on microfinance has far-reaching practical implications as it impacts global poverty, thereby providing valuable insights to governments, economists, and non-governmental organizations. However, research on microfinance is constrained by several aspects, as observed by many researchers on the subject. This paper reviewed the existing literature on microfinance and elaborated on the factors that obfuscate the path to a clear understanding of the subject. One such example is the equivocal stance taken by researchers on whether microfinance is restricted to microcredit only or whether it includes other social interventions like training and forming groups. Another factor that undermines research on the subject is the unavailability of granular data, which hinders research on microfinance's social and financial intermediation aspects. These deterrents to more hygienic research on microfinance have been highlighted in this paper. This review helped steer future research into less charted areas like the cost of social intermediation, separating the effects of social and financial intermediation, and avoiding confusion in the constituents of microfinance. Future researchers must avoid these pitfalls so that their work leads to more meaningful conclusions and is free from anomalies hitherto flagged.

Keywords : **Financial intermediation, social intermediation, microfinance, microcredit, microfinance plus**

JEL Classification Codes : B25, D14, D71, D91, E26, G21

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The novelty of the concept of microfinance has worn off since its introduction in the early 1980s. However, the various hues of microfinance have seeped deeply into many countries' economic and social spheres and have become an acceptable part of people's lives, especially those living below the poverty line. Olsen (2011) referred to the acceptance of microfinance by many international organizations as an instrument to eradicate poverty and to the fact that the United Nations had considered microfinance crucial to achieving the Millennium Development Goal of poverty eradication and declared 2005 the Year of Microcredit. Since then, the subject has continued to attract and engage thousands of researchers, perhaps because despite being in existence for around five decades, poverty across continents is yet to be wiped out. Barnett (2011) pointed out that despite considerable investments to eliminate poverty, it continues to plague countries, especially in Africa. The importance of this research can be gauged from the fact that one of the first objectives of the Sustainable Development Goals called "Agenda 2030" continues to be eradicating poverty, and microfinance is still an important tool to achieve this goal. This paper analyzes the more intricate problems faced by researchers in microfinance, namely, the need to segue social and financial intermediation, weaning the effect of microfinance-plus from microcredit, and studying the cost-benefit analysis of social intermediation. By piecing together the findings of existing research and analyzing the same, this paper endeavors to pave the way for future research. There is a need for such an assessment at this juncture as research on the subject is obfuscated by the fact that microfinance is a combination of many factors, and some aspects of the concept are ingrained with abstract

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interventions, which are difficult to measure. Murria and Verma (2013) observed that microfinance is a much-confused buzzword, especially among bankers and policymakers. This paper aims to clear this confusion and address the issues faced by future researchers through its findings. It is crucial to address these issues to clarify thoughts for research users like governments, country planners, economists, and non-governmental organizations (NGOs). This paper, through its findings, suggests ways to overcome these problems by reviewing the literature on the debatable issues in microfinance and the tools which researchers have used to overcome the associated complexities. It offers suggestions to policymakers and researchers in absorbing the cost and amending tools of social intermediation.

Relevance and Need for the Study

Research on microfinance has led to many reforms in this sphere. Setting up Rural Self Employment Institutes (RSETIs) in every district of India is one such example. Sharma et al. (2012), in a report on Indian livelihoods, traced the development of microfinance in India through self-help groups (SHGs) and the evolvement of the National Rural Livelihoods Mission (NRLM). In the overall design of NRLM, RSETI is a part. This can be attributed to research that provided evidence that training as a part of microfinance had a positive effect on the trainees' income, entrepreneurship skills, and financial literacy.

Similarly, research has provided a theoretical grounding and has included issues such as trust, hygiene, health, and other constituents in microfinance. Because of the positive contribution of research in the implementation of microfinance, the constraints and limitations documented by existing researchers must be brought before future researchers so that such obstacles do not hinder their work. Future researchers will also get an insight into how existing research surmounted its problems to achieve sanitized results. These will give the practitioners of microfinance newer leads for lucid investigation.

Microfinance and its Constituents

Microfinance is a simple concept that alleviates millions of people from poverty and hunger. It thrives on the precept that the poor also can save money. Though the money saved individually is insignificant, when pooled together by a group, such savings can attain significant proportions over some time if saved regularly. The amount thus saved is lent to individuals in the group to help them start small business ventures. Millions embraced microfinance due to its simplicity. It did not involve complex calculations or ideas and was quickly accepted by the masses. Over time, the amount involved in microfinance, which includes lending and saving arms, ballooned to billions of dollars. Evidence of the depth and extent of microfinance in India can be seen in the annual statistics put out by the National Bank for Agriculture and Rural Development (2020), which showed that the total number of SHGs owing loans to banks as of March 31, 2020, was 56.77 lakh and the amount owed was a staggering INR 1,08,075.07 crore, while the total number of SHGs saving with banks was 102.43 lakh.

The concept of microfinance is not restricted to the financial aspect. Along the way, other interventions like micro-insurance, training, health, and trust were included as a part of microfinance. Nayak (2014) traced how microfinance, which initially started as microcredit, added other components like insurance, micro-leasing, and training as it developed. He also suggested that the synergy of the various components was responsible for the success of microfinance, which has become a debatable issue that researchers grapple with. While some believe that microfinance is the facilitation of service and the delivery of microcredit, also called financial intermediation, others assert that microfinance includes aspects such as training, health, hygiene, and trust, which the researchers term social intervention. Beran Samuelson (2013) wrote that microcredit was the first form of microfinance devised by Muhammad Yunus, which microfinance institutions later exploited. The need to follow a double bottom line approach of profit and social benefits was fit in later by NGOs and the government. Research on the subject is also skewed in favor of only the financial intermediation aspect of microfinance. Kamukama and Natamba (2013) gathered evidence to point out that social intermediation had a positive effect on the financial services provided by microfinance but acknowledged that the literature on the subject was sparse and this, therefore, was a matter of great concern.

Some researchers have called the social intermediation component microfinance-plus. Financial intermediation includes savings, lending, insurance, and other adjuncts directly connected to finance. Social intermediation includes interventions like training, health, trust, leadership, teamwork, and other issues. Though microfinance models may vary in different countries, generally, financial intermediation is preceded by social intervention. The empirical literature on the subject suggests that financial and social intermediations are required to achieve the desired goal of alleviating people from poverty.

The inclusion of social intermediation into microfinance created consternation amongst stakeholders, especially lenders, which led to the debate on the constituents of microfinance. Should microfinance only be restricted to the financial aspect, or should it include social interventions? Literature on the subject is divided. Many proponents of microfinance advocate that microfinance should follow a minimalist approach and be restricted to simple lending without the other services, as microfinance-plus services entail a cost. Another argument put forth by the proponents of the minimalist approach is that the provision of microcredit only results in the sustainability of microfinance institutions. Muhammad Yunus, considered the father of modern microfinance, was not a firm believer in the social intermediation concept of microfinance. In the book *Banker to the Poor*, Yunus and Jolis (2007) observed that the poor get bored by social interventions like training which also gives them a sense of inferiority.

Another school of thought advocates the integrated approach of synergizing microfinance with the plus services. Olu (2009) stated unequivocally that the definition of microfinance included both financial and social intermediations. Mago and Hofisi (2014) stated that there is a tendency to use microcredit and microfinance interchangeably, though there are differences between the two. While microcredit is just providing credit, microfinance includes training, social intermediation, and other social services.

The uninitiated may refer to microcredit as microfinance and vice versa, but it is established by the existing literature and by a majority of researchers that microfinance includes social and financial intermediation.

In India and many other third-world countries, microfinance schemes designed by governments, banks, and financial institutions mandate that subsidized microcredit be made available to borrowers only after they are suitably trained. The debate about the constituents of microfinance can be laid to rest as it is now widely accepted that microfinance includes both social and financial intermediation. Any further debate on the issue is tantamount to hair-splitting.

Hindrances to Hygienic Research in Microfinance

There are a few grey areas that confound researchers in the study of microfinance. Bhatt and Tang (2001) discussed three areas plaguing the microfinance sector: vehicles, technologies, and performance assessments for financial service delivery. The first grey area relates to NGOs and commercial banks being used as delivery vehicles for microfinance and the insistence on providing training as a part of microfinance. He weighed the costs of providing training with the benefits resulting from training and concluded that this type of model was followed by the NGOs that depended on donations. For-profit organizations followed the minimalist approach, and such a model could potentially exclude indigent target populations and geographies less profitable, like the rural landscape. The second hindrance relates to the approaches to research that pit the minimalist service delivery approach against the integrated service delivery approach. The third controversy relates to measuring the impact or change in performance of the borrowing individuals/enterprises. In other words, the controversy is whether performance assessment should happen at the individual or institutional levels. We list and discuss some of these grey areas.

Delineating the Effect of Microcredit and Microfinance-Plus

Researchers are vexed with the problem of individually measuring the effect of microcredit and microfinance-plus. In a qualitative study, Siti-Nabiha et al. (2018) conceded that measuring microfinance's social impact was challenging. At the grass-roots level, microfinance delivery combines microcredit and some semblance of services like forming groups and training. The problem is aggravated because, in practice, the plus service and microcredit follow in quick succession. Mbugua (2010) was motivated by the debates between the proponents of minimalist and integrated approaches and the fact that very few studies examined the impact of microfinance services. He, therefore, studied the impact of microfinance services on the performance of micro-enterprises in Kenya.

Solarin (2021) suggested a model where the effect of the variable's microcredit, training, savings, and insurance on alleviating poverty could be tested separately. Ocasio (2012) studied whether microfinance services like skill training and providing literacy services enhanced the effect of microcredit. He examined data from three programs in Bangladesh, namely, the Grameen Bank, the Bangladesh Rural Advancement Committee (BRAC), and Rural Development-12 (RD-12) program. The author argued that in the existing microfinance literature, scholars study the impact of microfinance programs as a unified structure because social intermediation services are a part of microfinance. He made a case to study the impact of social intermediation programs on microfinance separately. Though studies that deal with the impact of social intermediation in isolation are ideal, in practice, such studies are complex as such services are immediately followed by financial intermediation. The lines between social and financial intermediation become blurred. However, Wondirad (2020) suggested using the ratio of the loan portfolio to several clients as a variable to measure social depth and the number of active clients served by the institution to measure social breadth or social outreach.

The amount of research on the integrated effect of social and financial intermediation is high. Some researchers have acknowledged that the results produced by such studies are ambiguous. Various researchers have adopted different techniques to overcome the morphing of social and financial intermediation. For example, Alam (2013) studied the effect of credit and non-credit aspects of microfinance on the income level of borrowers. The study was based on an extensive survey that interviewed 1,798 households in 87 villages. Credit was provided to the borrowers by Grameen Bank, BRAC, and BRDB. Non-credit aspects, which included vocational training, education about health, family planning, civic responsibilities, and rights, were also provided by these agencies. To measure the borrowers' income levels on credit, the researcher used loan size as a proxy for credit. Any other effect of profit that is not through the loan size was attributed to the non-credit aspects of the loans. The results showed that both credit and non-credit had a positive effect on the income of the borrowers. However, the non-credit aspects of the programs increased profits above and beyond the credit aspects, and these effects were substantial.

Nagaraj et al. (2009) studied the factors that affect the economic performance of SHGs. The indicator for measuring the economic performance of the SHGs was the total income earned by the members of the SHG for every Rupee borrowed by the group. Their study revealed that the training of SHG members emerged as a crucial explanatory variable in shaping economic performance. The researchers proved that those who received training realized a better return from their borrowings than those who did not receive training. ManyMany researchers feel that providing micro-credit has solved one dimension of the problem, namely, economic empowerment. Apart from microcredit, the borrowers must have the capacity to understand business, ability to take risks, and access information. Social intermediation in the form of providing soft services like health education, literacy training, and business training would create synergies for the borrowers. Sonam et al. (2019) expressed similar views in their study.

Mutai and Osborn (2014) also studied the combined impact of financial and social intermediation services of microfinance. They essentially stated that microfinance services economically empowered the women as measured by the improvement in income and assets of the borrowers. Working on a sample size of 117, the researchers did not differentiate the effect of microcredit and training in their impact studies. They clubbed financial and non-financial services like training, advisory, money transfer, and deposit services into one combined independent variable and studied its impact on the income and assets of the beneficiaries. However, the study quoted that the respondents felt that training was an important input that helped them achieve economic empowerment after the loan component and savings.

The above reviews show how researchers have grappled with the problem of alienating the combined effect of financial and social intermediation. Another tool that can be used to solve the above problem, but is not covered under the review above, is conducting Random Control Trials. By conducting trials and tracking the performance of groups that have received both social and financial intermediation and groups that have received only financial intermediation, this problem can be resolved to some extent. There is scope for researchers to study newer tools and use different methods to unravel this knotty problem.

Cost of Microfinance-Plus

Providing social intermediation or microfinance-plus entails a cost. In an era where the single bottom line – as compared to the double bottom line – is still a ferociously pursued goal, minimizing cost is a high priority for commercial organizations. Three different types of costs incurred by microfinance institutions were explained by Sharma et al. (2017): costs involved in providing loans, costs of default, and transaction costs. They further explained that transaction cost in finance referred to the transfer of one unit of currency from the saver to the borrower and included the cost of recovery of such borrowing at a later date with interest. The researchers made out a case where the costs incurred by microfinance institutions for social intermediation can be recovered by identifying less risky and high-risk borrowers during the training. While the less risky borrowers were given low-interest group loans, the high-risk borrowers were given high-interest individual loans. Siti-Nabiha et al. (2018) alluded to the opposing notions of commercial and social logic, as they called it. When the government or the regulator thrusts microfinance-plus, these services, at best, are very minimal and cursory.

Microfinance is embedded with the dichotomy between the Welfarist and Institutionalist approaches or the contradictory objectives of profit and purpose. Zainuddin and Yasin (2019) elaborated on these two approaches, where they inferred that the Welfarist school of thought preferred that the costs be recovered from the government or donations. On the other hand, the Institutionalists preferred that the costs were recovered from the microfinance borrowers themselves, and they cited sustainability as an alibi for this approach. Abdulai and Tewari (2017) also referred to a similar trade-off between outreach and sustainability. Their research supported the view that outreach expansion could achieve sustainability. They recommended that to achieve sustainability, institutions must achieve productivity through cost-effective and efficient strategies. Chowdhury (2013) referred to the cost of operating in remote areas by private banks and other commercial players, which were beyond the reach of microfinance borrowers. He suggested that as an alternative, NGOs were more effective in reducing costs as they had more resources, state-of-the-art technologies, and a larger workforce. He, however, recommended that all social costs of microfinance, like training, transporting, and monitoring of field workers, were borne by government organizations.

Similar views were echoed by Simkhada (2018), who advocated governmental intervention for a noble cause. He supported the view that the high costs due to low financial literacy, low population, and low economic diversity led to small ticket and high-risk loans. Transaction costs in such an environment were high, whereas the business opportunities were low. He, therefore, rooted for external support. An attempt to distinguish between financial and non-financial costs was made by Swamy (2019), as he endeavored to study whether these costs affected financial intermediation in the form of small-ticket loans. His study examined financial costs in the form of interest paid on all rate-sensitive liabilities and expenses incurred on government funds purchased and securities sold. Non-financial expenses studied by him were employee costs, operating expenses, capital expenses, provisions and contingencies, depreciation, and miscellaneous expenses. This study is inadequate as it did not address the cost of social intermediation referred to in this paper, but it is still significant as the researcher suggested that small ticket microcredit enhanced the cost of financial intermediation.

The issue, therefore, is laid bare for researchers. Social and financial intermediation, or welfarist and institutional approaches, or instrumentalist and transformant approaches, as some researchers prefer to call them, are opposing and contradictory notions. Is there a model that translates into a win-win situation that reconciles these opposing notions to benefit all stakeholders? Fanconi and Scheurle (2017) stated that there was no trade-off between social performance and profitability, and their findings were based on empirical analysis. From the literature review, it is clear that microfinance lenders are disadvantaged by including social intermediation as they have to shoulder its cost. However, there is overwhelming evidence to show the benefits of social intermediation.

The issue of the cost of social intermediation can be partly resolved by the government agencies, which can take up the responsibility of providing social intermediation. Setting up centers for social intermediation of microfinance can also be given additional weightage under the Corporate Social Responsibility (CSR) prescribed in the Companies Act 2013. As far as microfinance lenders are concerned, they can load a part of the cost into the lending rates and increase the lending volumes to achieve economies of scale.

Diversity in the Target Group

Researchers are often forced to treat the target group as a monolithic block, ignoring the fact that the target sample is diverse in many aspects. The target sample differs in age, education, and economic and social background. Mizanur Rahman and Ahmad (2010) studied the impact of the microfinance program of Islami Bank Bangladesh Limited (IBBL) on the livelihood of the rural poor. Apart from providing microcredit, the program also provided training and non-formal education to the borrowers, hoping that these would enhance their level of skills in performing income-generating activities. The study's findings suggested that microcredit, along with other factors like clients' age, number of family members engaged in farming, total land size, and clients' ethics and morals, had a positive and significant influence on household income. Feroze et al. (2011) studied the impact of homogeneity of target groups on loan repayment. For homogeneity, they considered factors like age, caste, marital status, education, occupation, and landholdings of the group members.

Murria and Verma (2013) stated that many researchers treated the microfinance groups as homogeneous, whereas in reality, at least in India, the group members belonged to different castes and socio-economic categories. Hence, treating the target groups as homogeneous needs rethinking. After reviewing the literature on the subject, they further exposed that loans were cornered by the leaders and more influential members within the group, whereas Scheduled Caste/Scheduled Tribe members were left out. Moreover, they averred that the occupations of the group members ranged from laborers to small entrepreneurs to agriculturists, and therefore treating them as a homogeneous group was erroneous.

Kundu and Mitra (2010), in a longitudinal study assessing the impact of microfinance on SHGs, found that the target groups, though seemingly homogeneous, were different in respect of the acreage of ownership of landholdings and, accordingly, the purpose for which the loan was utilized was different. Moreover, many group members did not avail of loans from the group and preferred other cheaper sources. Considering the members as a unified variable in research may be misleading in such a scenario.

In summary, researchers must recognize that though microfinance cohorts possess similar traits like caste, creed, religious beliefs, and wealth, treating them as a homogeneous group is fraught with risks leading to erroneous conclusions. As most of these groups are formed at the bottom of the pyramid, harsh realities like extreme poverty, exploitation, and adverse living conditions may override other sublime traits like trust, mutual obligation, and expectations, even though they possess similar economic and social characteristics. Researchers are also advised to check the ratings of microfinance cohorts or SHGs while sampling for their research. The ratings of these groups include marks for homogeneity, and researchers can include only such groups which have cleared the homogeneity test for their sample. Though measuring homogeneity is a complex task involving many abstract traits, the above intervention can help to some extent. Further, agencies involved in forming groups and providing training can devise a tool and screen the beneficiaries more thoroughly to ensure homogeneity. For example, beneficiaries above a certain income level or beneficiaries holding land and other movable or immovable assets beyond a certain level could be excluded from the group.

Assumptions about Uniformity in the Social Intermediation of Microfinance

The social intermediation component of microfinance has myriad hues and facets, which have dynamically changed over time. The individual components of the social intermediation of microfinance also are not uniform. Training, a significant component of social intermediation, is often used by researchers as a broad term that includes management or business education, skill training, on-the-job training, entrepreneurial development training, etc. Steve Kwok-Leung Chan (2018) referred to an NGO that offered 20–30 optional courses for members under microfinance training, which included bookkeeping, communication, gender issues, domestic violence, law, small business management, etc. The point is that training is vast and extensive, even those meant explicitly for microfinance borrowers. Bradley et al. (2012) conducted research that recognized such variances. They distinguished general education and specialized business training. They observed that while general education did not predict innovation, those with more education positively impacted income.

Another significant component of social intermediation is social sanctions and social relations. Xiong and You (2019) drew a subtle difference between the two. While social sanctions include peer screening, monitoring, and enforcement of penalties, social relations combine harmony, sharing of information, trust, mutual learning, and social interaction. Each of these variables is profoundly complex and measuring them based on a few questions posed to the respondents is tantamount to spreading the concept too thin.

These results show that taking social intermediation as a monolithic variable and ignoring its various inconsistencies will lead to misleading results. A more recent Kenya-based research studied the impact of managerial training on the performance of Small and Medium Enterprises (SMEs). Rotich et al. (2015) explained that the research trigger was that many SMEs did not possess managerial skills or experience. Without this, the SME owners followed their approach, which was generally on a trial-and-error basis. Their management style was more likely to be intuitive than analytical, leading to a more pronounced focus on day-to-day activities rather than long-term issues. Most research on social intermediation is intuitive, and to avoid this pitfall, researchers must take cognizance of the complexity, granularity, and interplay between the social intermediation variables. One of the tools to measure the uniformity of social intermediation is to conduct a simple test that includes generic and fundamental questions on the loan, end-use, rate of interest, repayment of loans, subsidies available, etc. Vijaykumar and Naidu (2018) suggested a few generic subjects that can be included in such tests. Those who clear the test can be used as a sample, giving some semblance of uniformity in social intermediation.

Policy Implications

This research assumes importance for government agencies, NGOs, micro-finance institutions, and other stakeholders as it suggests tweaking existing policies to make microfinance more meaningful. For example, rigorous screening of beneficiaries of social intermediation, giving additional weightage to corporates under CSR activity, and bearing the cost of social intermediation have significant policy implications, which will go a long way in alleviating poverty and spreading financial awareness.

Conclusion

The multi-layered and multi-stack issues surrounding microfinance have primed future researchers about the subject's complexities. One must have a clear picture of the effect of social and financial aspects of microfinance separately, enabling public policy practitioners to concentrate on that aspect of microfinance that they find beneficial. Surprisingly, this researcher found that while it was acknowledged that microfinance-plus comes with a cost, few studies did a cost-benefit analysis of the same. The debate relating to the constituents of microfinance is more or less resolved as it is accepted that microfinance is a combination of microcredit and the plus services. However, the amorphous nature of the variables representing social and financial intermediation and their interplay is still in the uncertain domain. The problem relating to the dispensers of microfinance-plus services was largely untouched in this paper. The onus on these services has been taken up by governmental bodies, at least in India.

Limitations of the Study and Scope for Further Research

The theory and research in microfinance are riddled with myriad problems. The present research is limited and addresses only a few of them. It does not focus on the effect of microfinance on poverty, though researchers like Toindepi (2016) averred that impact assessments of microfinance on poverty provided conflicting evidence. Another limitation of this research is the study of the outreach of microfinance. Armendáriz and Labie (2011) referred to this argument as they claimed that the outreach of microfinance in 30 years of its existence had only been around one-and-a-half million, whereas the unbanked poor numbered around two-and-a-half billion. There is immense scope for further research. An overarching study of the literature on microfinance from the last 30 years assumes that microfinance is the panacea for alleviating poverty without searching for an alternative paradigm. Therefore, there is a dire need to study alternative strategies, wherein lies the scope for future researchers. As Ukanwa et al. (2018) put it, microfinance has not addressed the cause of the very poor and suggests an alternative strategy to replace microfinance.

Author's Contribution

Dr. N.V. Vijaykumar sieved through the existing literature on microfinance and extracted high-quality research papers from reputed journals, which provide scope for further research. The entire paper was conceived and written by him to provide a platform for future research.

Conflict of Interest

The author certifies that he has no affiliations with or involvement in any organization or entity with any financial or non-financial interest in the subject matter or materials discussed in this manuscript.

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