Novel insights in activating the role of microfinance
- Review of recent papers-

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Abstract*:*

The literature on microfinance has received more attention over the last two decades, especially after the UN Year of microcredit in 2005, and the awarding of the Nobel Peace Prize to Mohammad Yunus and the Grameen Bank in 2006. This paper aims to explore the recent trends of microfinance research and its main findings and suggestions on how to activate the role of microfinance, through a literature review of some significant recently published papers. We conclude with the most important findings from these papers, and end by suggesting ideas for future research.

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1. INTRODUCTION

According to the concept of microfinance, it ought to be a key tool in development mission, by providing access to credit for people which are usually excluded from the formal banking system.

Two clear manifestations for popularity launch of microfinance are the fact that in 2006, Grameen Bank and Muhammad Yunus were awarded the Nobel Peace Prize for their efforts in developing microfinance solution to help reducing poverty, and in 2005 where the Economic and Social Council of the United Nations declared the International Year of Microcredit.

Given the growing interest in microfinance' issue thereafter, it seems that there are several research and discussions that have been established on this topic. As a result of that, our paper comes as a review of some recent important microfinance research, which are selected from the Web of Science as a reliable resource for research.

We relied also on findings of (Begoña & Carlos, 2019, p. 188)' study, where did he refer to the most 5 % significant papers writen by microfinance researchers. As they followed a scientometric approach to get knowledge maps, through analyzing links between citations and key words. (Begoña & Carlos, 2019, p. 188)

In this work, we have opted for a literature review to answer the following general question :

What niche has microfinance occupied in the world of poverty ? And how to activate its role ?

To that end, this paper seeks to address the sub-questions listed below that we believe are the most important points that can be focused on, which are :

- Has Microfinance really contributed to reduce poverty ?
- What are the most important factors that insure good practice for MFIs of the governance principles ?
- What are the main determinants of MFIs' financial and social performances ? And is there a trade-off between them ?
- Does Microfinance live up to its promise vis-a-vis women empowerment ?
- What about Islamic microfinance ? Could it be an alternative ?

The paper is organized as follows : an introduction describes what this review seeks to explore. The following section analyzes some of the most influential papers and identifies recent trends in microfinance, through classifying them into five titles proposed by the researchers. The conclusions are finally presented.

2. Review of recent microfinance papers:

Many factors determine the success of microfinance in providing access to financial services for the poor people, which include : management quality, trained personnel, dependence on subsidies, inovative products and services, diverse client base, good financial management, regulation, financial performance (like profitability, portfolio quality including repayment rates and portfolio at risk, …), social performance, MFI competitiveness, financial viability (as operational or financial self-sufficiency, subsidies dependency) (J.Y., 2017, pp. 122-124)And (Piinz & Helmig, 2015, pp. 488–509)

Based on this inductory presentation, and after checking out the content of the papers selected for preparing this review, we think that we focus on the following main topics :

2.1 Does Microfinance hold its promise in reducing poverty?

The anti-poverty is the main goal for which microfinance was established. In this context, some researchers have conducted experimental studies in several regions of the world. Some of them have admitted that Microfinance has the capacity to reduce poverty and improve the well-being of the poor. Whilst, the others found that it failed to reach this goal.

For example**,** (Isahaque, Zulkarnain A, Azlinda, & Shariful, 2016, pp. 1-12) provided a critical assessment of the assumption that microfinance alleviates poverty in Bangladesh. They examined the effectivness of microfinance programs and their contrubuting to poverty reduction in the district of Bogra, Bangladesh. They found that despite the extensive reception of microfinance ideology in Bangladesh, microfinance programs were ineffective. They justified their result by misuse of loans through several factors such as: high interest rates, strict repayment schedules, insufficient loans, a lack of supervision after loan disbursement, and the focuse of MFIs on profit and not doing tailor loans to suit a beneficiary's individual circumstances.

However in our opinion, it cannot be directly judge that microfinance programs were ineffective. Rather, the defect could be on the customer side. And since the study was conducted on a sample of illiterate individuals, we can attribute that result to the lack of knowledge of those clients and their weak qualifications and skills to establish productive small projects. In addition, the results of a specific region's study with exceptional circumstances cannot be generalized to all of Bangladesh.

(Isahaque, Zulkarnain A, Azlinda, & Shariful, 2016, pp. 1-12) added other influencing factors, such as: the lack of health care, education, samitation housing, and high level of unemployment. In the same context, (Ding, 2018)argues and indicates that a microfinance project with a proper design would still achieve anti-poverty objectives, even if it is in a less developed institutional environment.

Other empirical literature also cast doubt on the effectiveness of microfinance as a tool to reduce poverty, where (Donou-Adonsou & Sylwester, 2016) indicated in their study of 71 developing countries over the period 2002-2011 that banking practices in developing countries can help fight poverty, but may fail to reach the poorest. While, they concluded also that microfinance is still in its infancy and it cannot yet alleviate poverty. According to comment, the study' period probably should have been somewhat longer in order to judge wether or not the effectiveness of microfinance is.

While (Frank W, 2017, pp. 159-171) conducted an empirical study by employing a mixed method approach involving a survey of 211 microfinance client and non-client households from Northeastern Mindanao, the Philippines. But there is no difference between them in the demographic measures such as: education, household size and distance to the town centre. The microfinance institutions, in this case CBI, didn't discriminate between households regardless of distance. Rather, it focused its operations in areas far from the town centre trying to acheive financial inclusion. They investigated the impact of microfinance on poverty reduction over there. They found that there is a rather positive impact of microfinance on poverty reduction, and the microfinance client households having more incomes and savings than non client households. This reinforces the importance of that Philippine government continues to promote and intensify microfinance policies.

Another recent empirical research by (Ding, 2018), who tried to assess the effect of the government-sponsored microfinance projects on poverty reduction in China as the largest government in the developing world. This was by focusing on a dataset of 2356 Chinese villages, and the average net income growth of them. They found that there is a statistically significant effect of the microfinance projects on improving the net income of the farmers and reducing poverty in China. Which can be a pioneering experience that provides the necessary knowledge to the remaining developing countries for future poverty reducing practices.

In the end, we believe in microfinance as a path out of poverty and an opportunity given to the poor that requires commitment and hard work, not a panacea.

2.2 Governance and microfinance institutions' performance:

Some researchers have been written on governance of MFIs. (Hartarska, 2005, pp. 1627–1643) is one of the most important of them. Her paper presented the first evidence on the relationship between governance mechanisms and performance in microfinance. She investigated how governance mechanisms affect performance of Eastern Europian MFIs between 1998 and 2002. Those mechanisms include the characteristics of the board, the remuneration of the CEO, and the type of ownership. The author appreciated in her findings managers' experience to improve performance, and independent board with limited proportion of affiliated directors to identify trade off between MFI outreach and financial performace. While, she indicated that the difference between various ownership types in outreach and financial performance was negligible.

(Mersland & Strøm, 2009) also suggested some significant recommendations for better governance in MFIs, such as: a local board of directors rather than an international one to improve the financial performance of MFIs, besides the presence of an internal auditor and a female CEO.

While (Gupta & Mirchandani, 2020, pp. 307–326) attempted to examine the impact of ownership structure and corporate governance of MFIs on its social performance. This is through using a global data set of 456 MFIs commercially oriented (banks and NBFIs) and socially oriented (NGOs and cooperatives/credit unions), and taking fve indicators into consideration. They concluded that the ownership type has a significant effect on social performance of MFIs. The socially oriented MFIs had a greater social performance, as compared to commercially oriented MFIs. Where the first category had greater client outreach with a higher proportion of female borrowers, and a lower average loan size than the second one. Apparently, this is the opposite of what was found in aforementioned (Hartarska, 2005, pp. 1627–1643) study Where she concluded that the MFIs ownership structure does not have an important impact on MFIs performance. However, (Gupta & Mirchandani, 2020, pp. 307–326) answered this ambiguity and supported their position that the issue is not with converting the ownership from non-profit to for-profit. But conflicting objectives of owners can hinder the practice of good governance to improve the performance of their institution.

Finally, researchers agree on the importance of adopting good governance by MFIs to develop the microfinance industry.

2.3 Determinants of MFI's financial and social performance and trade-off between these two sides:

Microfinance institutions (MFI's) generally strive to improve the access of the poor to financial services, while at the same time have to keep their financial sustainability. Many researchers have talked about how can MFIs reach and complement these two goals.

Perhaps one of the most important research papers that dealt with this matter is (Hermes & Hudon, 2018)'s systematic review. It summarized the main of 170 studies looking into the determinants of financial and social performance of MFIs. Where the authors reffered to the diversity of findings and justified it by the multiplicity of measures and techniques used to assess financial and social performance. They conclued that the most important determinants addressed in the literature, are MFIs specific characteristics (age, size, and type of organization), governance tructures, and their funding sources.

About this last determinant, (Hudon & Traca, 2011, pp. 966–973) provided empirical evidence on the positive impact of subsidies on the efficiency of MFIs, as MFIs that received subsidies are more efficient than those that do not. But this remains true up to a certain threshold, where the results are counterproductive.This is embodies the « smart subsidies » idea, that takes into consideration the intensity and magnitude of the subsidies. In the same context, (Cull, Demirgüç-Kunt, & Morduch, 2018) found through calculating the microcredit costs of a microcredit business model formed from 1335 MFIs between 2005 and 2009, that commercial microfinance banks and some non-bank financial institutions rely more on subsidy than non-governmental organizations (NGOs), because of higher costs of lending poorer clients and less revenues. From their standpoint the large and enduring subsidies for those MFIs don't imply failure of microfinance, but it reinforces the need for cost-benefit determinations. They also recommende should be concentrating on how do MFIs reduce costs. Roy Mersland and R.O.Strom also support them on this point (Mersland & Strøm, 2009).

(Hermes & Hudon, 2018) Indicated also that the external context factors may play a significant role in determining the relationship between those various drivers and MFIs performance. Moreover, (Ferdinand A, 2017, pp. 1-15) proved that government political ideology is a significant determinant of MFIs performance, through an empirical study of 619 MFIs from 75 countries over the period of 1996-2012.

Farthermore, (Hermes & Hudon, 2018) noted that there is a lack of consensus in the literature on the measurement of financial and social performance. They argued that social performance as a complex concept should assessed by using a multidimentional index such as: measures of outreach, gender, geographical location of poor clients and the social performance indicators (SPI4). Lastly, it is absolutely crucial that there is consensus about the correct measurement of these concepts, in order for researchers can to reach important conclusions about the drivers of MFIs performance.

On the other hand ;

A recent meta-analyse indicates that evidence relating to the existence of a trade-off depends on the financial and social performance measures used (Hermes & Hudon, 2018). In this sense, and since the last focus of MFIs on financial self-sufficiency has created concern, that this may adversely affect their primary social mission, it seems that a large number of studies on the performance of MFIs are concerned with discussing the trade-off between financial and social performance.

A point noted by (Hermes & Hudon, 2018), that there is room for both types of MFIs in the market. While some MFIs are very profitable and tend to compete with traditional financial institutions, others still try to maximize outreach the poorer customers.

Another important point by (Quayes, 2012, pp. 3421–3433), who investigated the impact of financial sustainability on outreach by using data from 702 MFIs operating in 83 countries. The most important finding he initially reached is that there is a complementary positive relationship between the financial and social performance. Then he realized that this positive and integral effect concerns MFIs with high disclosure, not MFIs with low disclosure. He concluded that financial sustainability is not an impediment to outreach efforts, on the contrary it can actually facilitate greater depth of outreach.

(Quayes, 2012, pp. 3421–3433) Meaning, it should not be concerned about MFIs focus on financial self-sufficiency, but rather more attention should be paid to disclosure.

(Wondirad, 2020) adds that the link between MFIs' financial and social performances is conditional upon competition. That means, the competition motivates MFIs to reach out the poorer segment and helps them achieve financial sustainability, and also ensures no drift from their primary mission. He reached this result based on his empirical study of 183 Indian MFIs over the period (2005-2014) in which the market was very competitive.

Farthermore, some researchers went deeper and distinguished between outreach breadth and outreach depth. Such as (Awaworyi Churchill, 2020, pp. 1329–1350), who provided evidence using data of 1595 MFIs in 109 countries, that there is a trade-off between sustainability and outreach depth, but complementarity between sustainability and outreach breadth. He noted also that this distinction will push practitioners to pay attention to outreach quality as well, not just numbers that have been reached. While, (Nurmakhanova, Kretzschmar, & Fedhila, 2015, pp. 231–250) argue that focusing on financial sustainability does not necessarily hurt both of depth and breadth of outreach.

2.4 Microfinance vis-a-vis women empowerment :

Providing access to microfinance services for women is a key approach to improve the status of women and their households in society, and to help them move away from poverty. Based on this popular belief, many researchers discuss on the contribution of lending microloans to women to empower them.

One of the more important papers that takled this topic is (D'Espallier, Guérin, & Mersland, 2011, pp. 758–772)' s research. Where the authors studied repayment behavior in 350 MFIs from 70 countries, through a set of indicators, such as the portfolio at risk, loan loss write-off, and provisions …, based on the premise that women are in general better credit risks than men in microfinance. They found that despite women's lower creditworthliness, MFIs with higher proportion of female clients have lower portfolio at risk and fewer write-off rates. However, lending to women might not be the best business case for MFIs because of smal size of loans and low operational self-sufficiency. They concluded that the issue is not a matter of studying the gender-repayment, but rather should look at implications for MFIs' outcomes due to focusing on women. Lastly, they argue that higher female repayment rates do not necessarily mean improved welfare for women, and suggest that should examined the reasons more closely.

In another study, (Garikipati, 2008, pp. 2620–2642) investigated the previous studies' result that lending to women benefits their households not women themselves. This was by examining loan-use and borrowertestinnonies of women from two Indian villages. The researcher found that loans given to women are often diverted into enhancing household's assets and incomes. She attributed this to several considerations, such as the patriarchal hold on family assets and the lack of focus on building the economic capabilities of borrowers (Garikipati, 2008, pp. 2620–2642). Here, if we focus on the rural category -by vertue of their being socially isolated-, we mention that (Sanyal, 2009, pp. 529–550) believes that the rural woman's interaction with microfinance institutions promotes her trust and group participation, and enhances her social capital more compared to urban woman (Sanyal, 2009, pp. 529–550)

Thus, (Garikipati, 2008, pp. 2620–2642)' s findings supported the conclusion reached by previous studies that providing credit as part of an integrated package including additional sevices (such as non-productive credit facilities, insurance, business development, and activities related to welfare) can enhance women's empowerment (Garikipati, 2008, pp. 2620–2642).This result is in line with those obtained by many researchers such as (Binaté Fofana, Antonides, Niehof, & van Ophem, 2015, pp. 1023–1041), where they indicated that microfinance programs contribute more to empowering women through its non-financial services as well like health care services, managemant training (Binaté Fofana, Antonides, Niehof, & van Ophem, 2015, pp. 1023–1041).

While, (Fiala, 2018, pp. 189–200) presented an experimental evidence that providing both capital and training contributes to achieve a large positive effect for men versus no effect noted for women on short-run. (Fiala, 2018, pp. 189–200).

So, providing access to capital within a package of other accompnying sevices such as training, skills, … -regardless of the gender-, may better the chances of getting good effects for all. But, it's very important also to pay attention to women –especially rural ones- for developing their capabilities and empowering them, and consider them as active members in society, not recipients.

2.5.Islamic microfinance as a new model :

There are currently a number of microfinance institutions operating on the basis of Islamic principles. Although some studies have been carried out on Islamic MFIs, the literature still lacks an overall theoretical framework on this topic.

Most researchers in this field such as (Smolo & Ismail, 2011, pp. 287–295) and (ZahidMahmood, Abbas, & Fatima, 2017) see a great hope in the success of Islamic microfinance institutions (IMFIs) and its ability to improve the incomes and living standard of the poor. This is for the diversity of its funds'sources (Zakah, Sadaka, Waqf …), and the multiplicity of Islamic formulas that can be used according to the dictates of Islamic law like (Murabahah, Mudarabah, Musharakah, …).

In this context, it is worth noting (Islam & Ahmad, 2020, pp. 176–197)' investigation of poor's acceptance of applying Mudarabah and Musharakah' idea as Islamic microfinance. The sample that was questioned was about 330 Muslim women clients of a Malaysian microfinance institution. They concluded that these two formulas could be successfully applied if reinforced by training to improve product awareness, understanding of Islamic law rules, in addition to entrepreneurial skills.

Even –in another study they conducted with Ghailan and Hoque, 2020 they suggested Islamic microfinance as an alternative approach in special cases, where traditional microfinance –that we mentioned earlier- in line with such conditions. Whereas, adopting the various sources of funds allocated as Zakah, Sadaka, Waqf, and qardul hassan… activates those patients economically and helps improve their health.

From our standpoint, on a one hand Islamic microfinance could meet the needs of a large number of poor Muslims who prefer financial transactions that comply with Islamic law, and thus contribute to achieving financial inclusion. On the other hand, Islamic microfinance is an ethical practice which is devoid of many problems facing traditional microfinance such as : high rate of interest, mission drift, constant dependence on subsidies, governance and corruption issues, …Therefore, we also believe that Islamic microfinance may be an effective and promising option in the future, and can contribute to poverty reduction and empowering the poor people whether in Islamic or non-Islamic societies.

3. CONCLUSION

This review reviewed the recent on microfinance , that has grown exponentially after the UN Year of microcredit in 2005, and the awarding of the Nobel Peace to Muhammad Yunus and Grameen

Bank in 2006. This paper has analyzed more than 20 studies opted from (Begoña & Carlos, 2019, p. 188)' paper findings, where he shed light 5 % of most cited and significant papers in microfinance research. We focused also on papers published in Web of Science database on this field.

What can be done to activate the role of microfinance ?

Based on our analysis of the studies discussed here, we concluded with a set of important suggestions, as follows :

- More focus should be given to cost efficiency in the MFIs, to improve financial performance and avoid mission drift. Innovations and digital payments (like mobile money. From the site : Gates, B., and M. Gates. 2015. "Our Big Bet for the Future : 2015 Gates Annual Letter." Bill & Melinda Gates Foundation. (Bill, 2015) appear to be a good way to create microfinance business models and facilitate access to the poorest with lowest costs. This is what we see very important, especially as our economy is currently coping with the COVID-19 phase, which requires digitalization strategies ;
- The necessity of governance' good practice in MFIs, by providing some suggested conditions like : manager's experience,an independent and local board with limited proportion of affiliated directors, an internal auditor, a board including women members, …, and most importantly of all is the stakeholder collaboration to create shared value ;
- Government encouragement of competition in the microfinance market and MFIs adoption of disclosure, to ensure a positive complement between the financial and social performances ;
- Providing other important services plus to capital (for example training Fiala N., 2018, management skills …), with more attention to mostly marginalized categories such as rural people and women.

We think that these are excellent suggestions provided an added value in the recent literature.

In the end, we hope that we have succeeded –even if by small proportion- in extracting butter from important recently published works in the field of microfinance. We tried to form a supportive infrastructure for future aspirations that support the development of microfinance and its access to the next level.

Future research prospects:

While the evidence is increasing gradually, the microfinance literature shows that most of evaluative studies are still centered in East Asian countries where the microfinance movement has originated, but relatively small in African ones. We believe there is a growing need to know more about the status and effectiveness of microfinance in these areas, where there is a large proportion of poverty.

We notice also many research gaps among the studies covered in this review, such as : clarify the importance of disclosure and its relationship to the financial performance, find how to measure outreach depth ?, examine the role of political stability in improving MFIs performance, investigate the reasons of better repayment for women, and more studies about the effectiveness of Islamic microfinance and its applicability in various countries.

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