1 INTRODUCTION

Poverty[1] in the midst of plenty is one of the central challenges in today's global economy and society. It is widespread and chronic in many parts of the developing world, triggering a myriad of responses at individual, national and international levels, all of which could be subsumed into a World Bank slogan that says: *"Our dream is a world free of poverty"*.

In order to attain a poverty-free world, many poverty alleviation strategies often advocate increased production/economic growth as well as a more equitable distribution of wealth. In other words, policy makers are faced with the challenge of not only sustaining economic growth but also adopting policy tools that can reduce (income) inequality, protect the poor from shocks and other vulnerabilities and give them a voice in decision-making. One such policy tool has been the provision of loans to the agricultural sector to boost output, create employment and stimulate overall economic growth (Woller and Woodworth, 2001).

However, the provision of many such loans within the framework of subsidised agricultural credit programmes has been criticized for failing to produce the expected outcomes (see for example Adams and Von Pischke, 1992; Buckley, 1997; Woller and Woodworth, 2001). As it became clear that the solutions to poverty did not simply lie in supplying 'productive' farm loans, but in integrating other non-farm economic activities in the rural sector, policy attention gradually shifted to rural credit, which adopted a more integrated approach to the problems of the rural household (EU, 2000:5). With the rapid increase in urban poverty, and the stark realisation that the poor also demand savings services, the concept of microfinance gained roots. Today microfinance is the generic name for a range of financial

[1] See Chapter 2 for various definitions of poverty.

services/products provided to economically handicapped individuals, households and/or their economic ventures.

Microfinance for the poor, whoever they are, is currently one of the leading issues in the development debate, and continues to generate high expectations from a wide range of interest groups and stakeholders including governments, non-governmental organisations (NGOs), investors, development practitioners, policy makers and researchers (Maxwell, 1999; UNCDF, 1999; Hulme and Mosley, 1996; Wright, 1999; Woller and Woodworth, 2001; Snow and Buss, 2001). As Rutherford (2000a) puts it, micro-finance is "a new reality in a new era", and there is a widespread acknowledgement of a microfinance revolution[2] especially since the early 1990s. Statistics from Daley-Harris' (2005) recent report on the state of a microcredit summit campaign clearly confirm this. Launched in 1997, this microcredit campaign aimed to reach 100 million of the world's poorest families with microfinancial services by 2005[3]. As of 2004, the report says, over 92 million clients, 67 million[4] of whom are said to be among the poorest, have been served by a worldwide register of over 3,000 microfinance institutions. This represents an explosive growth of 700 percent in the number of poorest clients in seven years (1997-2004).

Over the years, there has been not just a mere shift in nomenclature from farm/agricultural credit, to rural credit, microcredit, and now to microfinance, but also a fundamental change in paradigms[5]. In her

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[2] Seibel (2000) describes the "revolution" as a "new consensus" in the microfinance industry.

[3] There have been calls for that target to be extend to 200million poor families by 2015, with 100 million of them moving above the 1$ per day poverty line (Daley-Harris, 2004:28).

[4] In fact, when a family size of 5 is assumed, this works out to over 300 million poor family members affected, a number equal to the combined populations of the United Kingdom, France, Germany, Italy, Spain, The Netherlands, Switzerland and Norway (Daley-Harris, 2005:2).

[5] See chapter 3 for a brief description of the evolution of microfinance, drawing heavily from Kargbo (2000) and Robinson (2001).

book, *The Microfinance Revolution – Sustainable Finance for the Poor*, Robinson (2001) argues that this fundamental shift is inexorably pushing the microfinance industry from its 'charitable' origins to full commercialisation. The fact is that, according to Rutherford (2000b), a number of traditional assumptions about the poor and the best ways to alleviate their misery have been shown to be grossly simplistic or even inaccurate. One such assumption was that the poor are too poor to save and cannot repay loans at market interest rates. This provided justification for the sole emphasis on subsidised microcredit (agrocredit) targeted mainly at (male) crop farmers in rural areas. Emerging research has shown that the poor do in fact save and repay loans at competitive interest rates (Barry, 1995; Woller and Woodworth, 2001:271). Consequently, the hitherto standard approach of providing credit for (agricultural) production purposes only, is gradually giving way to a more integrated approach which recognises the demand for financial services related to non-farm income generating activities, education and even consumption.[6] Development interventions are increasingly being geared towards enabling poor households achieve a sustainable livelihood security, of which the goals of food security and/or income security can be seen as sub components.

This new paradigm is an expression of an increased understanding of the complex problems, potentials and dynamic processes affecting the behaviour and welfare of poor individuals, households and communities. But it is still unclear how far the provision of financial services to the poor has really advanced the fight against poverty, an issue that this work aims to further illuminate.

[6] But there is a growing momentum, spearheaded by FAO and GTZ, in favour of refocusing financial services to farmers/farming activities, rather than the (all too) general microfinancial approach now in vogue.

1.1 RESEARCH PROBLEM AND PURPOSE

The dismal performance of agricultural credit programmes of the 1990s has been documented in various assessment reports[7], and the search for innovative ways to ensure positive effects of microfinance interventions on the poor has been quite intense. Policy interventions such as microfinance generally commit substantial resources that are then unavailable for alternative programmes (World Bank, 1996). "Microcredit is at a critical point. ... A programme with such a commitment of resources cries out for both solid goals and evaluations …", and "… the policy problem now is the extraordinary support for a programme that has not been proven to make people better off..." (Snow and Buss, 2001:304). The assessment of effects and costs of an intervention is therefore imperative not just to ensure administrative and public accountability but also to serve as a feedback mechanism, which establishes a scientific basis for promoting/discouraging the choice of certain policy instruments.

The relationship between research and policy innovation is dynamic and complex, shaped by multiple relations and reservoirs of knowledge (RAPID, 2004). Although evidence based decision-making is not always the dominant approach to many policy formulation and implementation processes, research findings can and do make a difference. The influence of research is said to often depend "on external influences; context – politics and institutions; evidence – approach and credibility; links – influence and legitimacy" (ibid). Indeed, the assessment of development activities or interventions is an essential component of successful policy formulation and implementation, and the call for impact assessments and reviews has perhaps been loudest in donor-funded microfinance programmes (Duflos et al., 2004).

[7] See for example Meyer and Nagarajan (1997), Zeller and Sharma (1998), Modurch (1998), Sabharwa (2000).

With the preponderance of political rhetoric about the potency of microfinance to eradicate poverty, the need for credible evidence attributing improved welfare effects to specific financial services is increasingly being recognised even outside academic circles. While research has enhanced current understanding of the role of new technology in agriculture and rural infrastructure, price regimes in poverty alleviation, and has further contributed to the formulation of clearer policy guidelines, it is unclear what the role of (rural) financial markets is in alleviating poverty (Zeller et al., 1997:9). Existing evidence of the impact of microfinance interventions - with respect to household livelihood security, including food and income securities - is inconclusive and, in some cases, even contradictory. Some studies indicate that the provision of microcredit to the poor improves their wellbeing, others show no effect or quite the opposite[8]. A careful arbitration is therefore justified, and is achievable through a systematic analysis of the evidence contained in primary studies/assessments.

Such a systematic analysis or research synthesis clearly has a scientific and an economic value (Cooper and Hedges, 1994), given the reality that research results have been conflicting and can be rather overwhelming. It is considered good reasoning to try and resolve conflicts/inconsistencies using existing studies, before embarking on an additional study which is often very costly (Hunt, 1997). Moreover, it is becoming increasingly difficult for one to keep pace with the overwhelming amount of incoming data in one's field of interest. This has increased the importance of systematic literature reviews, which summarize the large number of findings and hence reduce the information overload. Today, systematic reviews are recognised as one of the most useful and reliable tools to assist evidence-based decision-making (Khan et al. (eds.), 2001). Since most research and policy

[8] Diagne and Zeller (2001), and Zeller et al. (2001) are two examples which highlight negative and positive impacts of access to credit in rural Malawi and Bangladesh respectively.

information needs cannot be fully met by the results of one empirical study, review articles are needed to provide an overview of all the relevant findings on a given topic or in a given field. Traditionally, such articles have been written by subject experts, but research since the 1980's shows that whilst those articles are educational, they are commonly incomplete and rather selective in the data that they reference (ibid).

In the field of Microfinance, Sebstad and Chen's 1996 *"Overview of Studies on the Impact of Micro Enterprise Credit"* is probably illustrative and representative of the review literature to date[9]. While such a study is clearly commendable, its usefulness may be rather limited due to a number of reasons:

1) The total sample is only 32 and contains only "very few studies that used rigorous, quasi-experimental methods."

2) The study identification, selection, review criteria and analytical procedures are not sufficiently explained in the report to allow for a fair judgement on their adequacy, or facilitate replication.

3) The style of the report is narrative and the authors could have done more to make it more analytical. Not a single statistical estimate is reported (even though some of the studies analysed were 'rigorous') to quantify/substantiate such conclusions as "The studies found positive changes in output, with average increase in sales". Their analysis practically reduces to a simple *vote count:* "Of the ten studies that looked at impacts of credit on micro enterprise assets, seven found a positive change ... (Jamaica, Honduras, Dominican

[9] Two more recent reviews of microfinance impact studies are discussed later in the thesis (chapter 4), where they are used as examples of microfinance literature reviews that relied on a qualitative approach.

> Republic, South Africa, Kenya, Bangladesh, and Indonesia). Two found no change (Guinea and Sri Lanka) and one found mixed effects (Malawi)" (ibid).

A review of the "Impact of Finance on Food Security and Poverty Alleviation" by Sharma and Schrieder [in Zeller and Sharma (eds.), 1998:185-210], though more creative and informative, also exhibits similar analytical weaknesses.

For these and similar shortcomings, traditional reviews generally do not provide a sound basis for decision making (Cooper and Hedges, 1994; Hunt, 1997). On the other hand, systematic reviews, such as meta-analysis, aim to overcome the problems of traditional review articles by following an explicit review process. Meta-analysis is one of the relatively new approaches that have been successfully used in various scientific disciplines – but perhaps more so in the fields of psychology and medicine - to synthesise empirical evidence across studies (see for example Cooper and Hedges, 1994 and Lipsey and Wilson, 2001 for more details on the development of meta-analytical approaches). Its application in the social sciences is now only gaining ground, and is yet to be introduced in the field of microfinance, for example.

Thus, the first key component of this work is the development of a framework for the meta-analysis of microfinance impact studies. This involved a comprehensive identification and criteria-based selection of all relevant primary impact studies, the design of a coding system to extract/record the important features and findings of each study, and the identification of appropriate techniques to facilitate the analysis of the resultant database. The importance of such a framework lies in its methodological aptness and scientific superiority (to traditional overviews/reviews) in synthesising empirical results scattered and buried in the numerous literature.

The second key component is an application of the analytical framework to appraise, compare and combine study results as appropriate. Considering the wide variety of methods employed in the primary assessment of microfinance interventions, a framework that allows for the integration of qualitative and quantitative techniques in a single meta-study could prove innovative. Results derived from a practical application of this meta-analytical framework to statistically describe and/or aggregate evidence from microfinance impact studies could help build a basis for policy and future research. It is hoped that the entire research output will amount to a single scientific compendium - probably the first of its kind and, for that matter, new to the microfinance industry - with a potential for widespread appeal and use by policy makers, donors, researchers/scholars, practitioners and the general public.

The application of the proposed review framework to a sample of studies was intended to answer three central (sets of) questions:

1) What is the impact of microfinance interventions as reported in the empirical literature so far? Does access to credit lead to reduced poverty (higher incomes, increased food security, and/improved general wellbeing)? Is the calculation of an 'average effect' or the portrayal of an 'overall picture' desirable and feasible?

2) Under what conditions can a microfinance intervention be particularly (in)effective?

3) Are there substantive differences in the reported impacts of microfinance across studies? If so, which factors might be responsible for such differences?

1.2 STRUCTURE OF THE THESIS

The thesis comprises eight chapters grouped into three main parts. **Part I** explores the nexus between poverty, finance and development in general, highlighting some definitions of poverty as a basis for understanding pro-poor policy interventions (chapter 2). It examines the centrality of poverty as a development goal and outlines various strategies that are employed to alleviate poverty in different settings. Chapter 3 focuses on the role of microfinance in development through its linkages with the farm and non-form sectors of an economy. After a brief review of the relationship between financial intermediation and economic growth, the chapter discusses the meaning of microfinance and its various components, the evolution of microfinance over the years and the suitability of the *sustainable livelihoods* framework for the design, delivery and analysis of financial services.

In Part II (chapters 4 and 5), an analytical framework is developed against the background of commonly used impact assessment methods and traditional and modern approaches to reviewing and synthesizing research literature. Chapter 4 particularly focuses on the generic *evaluation problem* and the various methods and techniques that are applicable to the primary assessment/evaluation of policy interventions such as microfinance. It also presents a short description of qualitative and quantitative methods for reviewing research literature; that is, the literature reporting the findings of primary impact assessments. Chapter 5 gives special coverage to the method of meta-analysis. It reviews general aspects of meta-analysis, including definitions, stages and procedures and an overview of its strengths and weaknesses.

Part III contains the analysis and results based on an application of the meta-analytical framework developed in part two (chapter 5). Chapter 6 explains how the primary studies were collected and