

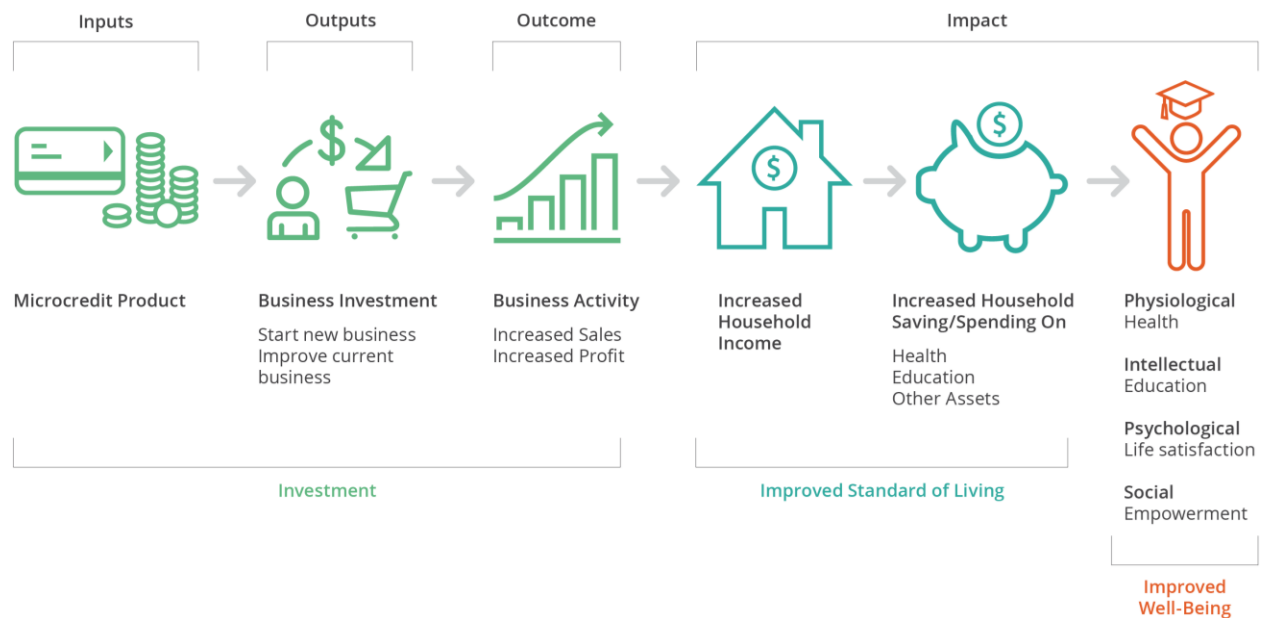


Photo credit: Sawiris Foundation for Social Development

# MICROCREDIT: IMPACTS AND INNOVATIONS

*This document was prepared by the J-PAL MENA Firms and Finance Team for the purpose of evidence dissemination. It is not an exhaustive review of all the rigorous evidence on this topic.*

## THEORY OF CHANGE



## TRADITIONAL MICROCREDIT MODEL

### Product Details

- Small loans with high interest rates
- Attempting to target women
- Immediate repayment schedules

### Typical Impacts

- Modest demand by general population
- No increase in average household incomes
- No increase in women's empowerment
- No investment in children's schooling



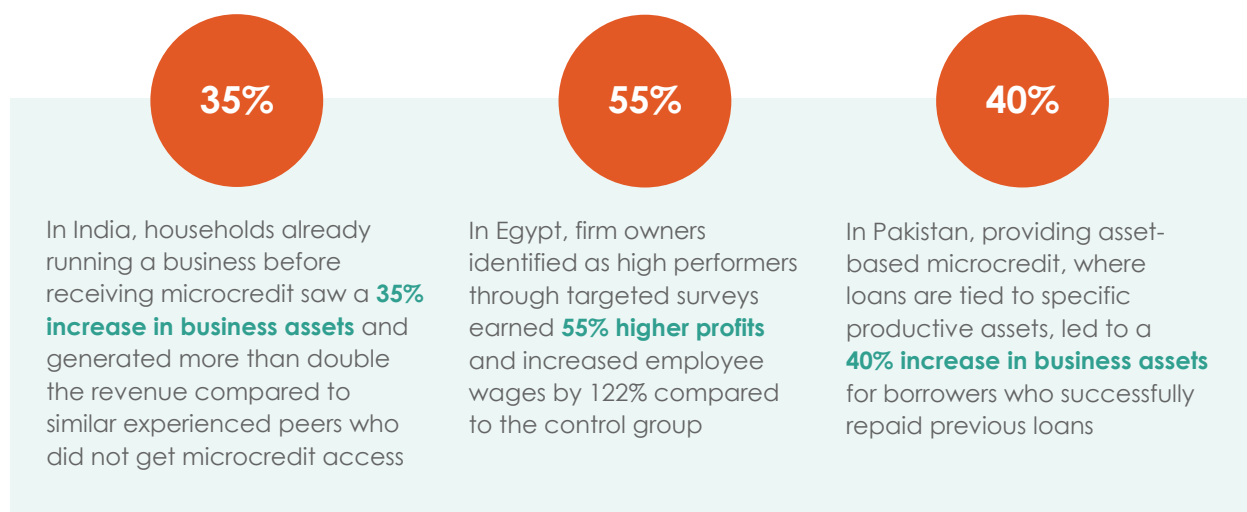
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# INNOVATIONS IN MICROCREDIT

## INNOVATION 1.

### Targeting high-potential entrepreneurs

Programs like microcredit, which aim to alleviate business constraints, can be particularly effective for a subset of entrepreneurs who are better equipped to utilize the funds.



## INNOVATION 2.

### Flexible repayment schemes

Modifications to the traditional microcredit model, such as grace periods and flexible repayment options, can improve business outcomes and consumption.

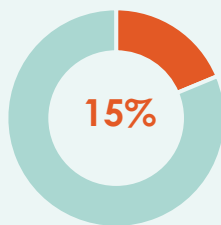
Country	Innovation	Effect on firm profit	Effect on household income	Effect on the likelihood of default
India	Repay whenever	↑ 15% (INR 125), daily	N/A	None
Bangladesh	Repayment deferral option	↑ 27% (USD 97), monthly	↑ 17% (USD 1,309), annually	↓ 1.7 percentage points (35%)
Colombia	Repayment deferral option	Insignificant effects	N/A	↑ 3-4 percentage points (5%)
India	Grace period	↑ 41% (INR 641), weekly	↑ 19.5%, monthly	↑ 6-9 percentage points (213-372%)

### INNOVATION 3.

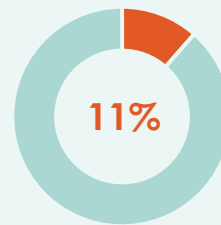
#### Changing the mode of disbursement

Intrahousehold dynamics may be a barrier to growth for women-owned enterprises. Specifically, women-owned businesses that are the sole enterprise of the household see higher returns to credit than those who share households with men-owned businesses and may thus have to compete for household financial resources.

Therefore, directly depositing loans into a private digital account has shown a:



**Increase** in women's monthly enterprise profits (USD\$18), relative to those who received cash



**Increase** in the value of their business capital (USD\$70), relative to those who received cash

This approach alleviates the pressure to share funds with family, enhancing women's control over their capital and enabling higher returns in their enterprises.

## BROADER IMPACTS ON LOCAL ECONOMIES

Microcredit can have significant spillover effects on local economies, influencing wages and employment even for non-borrowers. However, the introduction of microcredit may also reduce the availability of informal credit from social networks.

#### Benefits

- Microcredit access can increase local economic activity as borrowers use loans to consume goods/services, purchase business assets, or hire workers.
- In India, losing access to microcredit led to a 4% decrease in daily wages and a 10% decline in weekly household earnings (INR 86) in districts with greater microcredit exposure.

#### Drawbacks

- The introduction of microfinance institutions (MFIs) in India reduced social network links, including for households unlikely to borrow.
- Borrowing activity fell most sharply for households unlikely to borrow from MFIs, suggesting social networks serve as informal credit/insurance sources.

**Policymakers should consider the broader economic impacts, both positive and negative, when assessing the full effects of microcredit on local communities.**