Finance

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True Story

Reflection #1

Same slides as 20 years ago. Plus digital.

Microcredit Fans Claim….

- High marginal returns in business
  - → higher income
  - → higher consumption
- Less vulnerable to shocks
- Women empowerment within the household
- Group process builds solidarity and community development
- HIV/AIDS
  - Mitigation because now able to care for the ill
  - Mitigation because now able to adopt orphans
  - Prevention because women empowered

Microcredit Critics Claim…

- Business returns not that high…
  - Debt traps?
- Joint liability can destroy social networks
- **Consumer protection laws not strong enough**
  - **2024 Addition: Digital = 3 clicks-to-credit = awesome & scary**
- Discourages savings mobilization
  - safer way for individuals to build up to investments
- Problem isn’t merely credit
  - Info problem too: need business training alongside?

Contracting Questions

- Why group liability? Group lending (groups w/o liability)?
  - Improves selection?
  - Reduces moral hazard? Or could contagion → higher default?
  - Just cheaper to implement?
- Relational lending? Cash flow modelling?
- Interest rates
  - CGAP pushed lenders to increase rates, achieve market viability
  - Does demand slope down? (yes, some claimed not)
  - Importance of adverse selection & moral hazard w/r/t i-rates?

Behavioral Questions

- "Over"-borrow? (what does that mean?)
- With i-rate so high, why not save up?
  - If someone is borrowing @ 80% APR, they can save risk-free @ 80% by paying down their debt. Is that the best option for them?
- Behavioral challenges?
  - Temptation
  - Attention
  - Compounding underestimate?
- Trust?
- Social/household pressures?

Why Randomize
(abbreviated version from 2004 deck)

- Those who CHOOSE.....
- Weather.....
- Road got built.....

Reflection #2

Heterogeneity across people,
heterogeneity within person across time,
& intermingling with other market failures
= Complicated!

Reflection #3

Catch-22 of External Validity

Catch-22 of External Validity*

- Understand “the why” to then make predictions
  Implicitly includes nuanced and detailed theory
  Inevitably requires a lot of data, across contexts & people & situations

- Go NARROW
  e.g., one industry, one firm size, one key decision, one moment, etc.
  Precise understanding of “why”, but low validity to countless other circumstances

- Go BROAD
  - e.g., all SME in a country or region
  - Limited understanding of “why”
  - but (handwave-y) results apply to broader cross-section of people/world/time/situations

from Fischer & Karlan (AERP&P, 2015)

Starting with the first question: Impact of "Standard" Microcredit

- Entrepreneurial credit, 7 countries, published in Science & AEJ-AE
- Meager (2019, 2022): Bayesian Hierarchical Analysis of the 7
  - Meh on average confirmed (precise zero from 5^{th} to 75^{th} percentile)
  - Noisy outside, but top end had promise, particularly prior biz owners
- How did "industry" respond?

How did Microcredit Industry Respond?

- Called their PR team, told before-after anecdote
- "But you didn't measure long enough"
  - 1-2.5 years
  - My reaction: we didn't measure short enough…
- "But look at our 100% repayment rates!"
  - Uhhh………100%?!?
- "But this is all on the margin"
  - No study compared zero formal lenders to a thick market
  - Fair. (Although for policy, expansion is the policy, not 0→1)
  - Breza & Kinnan (2021): Shifted my thinking considerably
    - Big (negative) impact from shutdown of industry in India

How have we researchers (mostly?) responded?

- Savings!!
  - (some of this preempted the credit)
  - Some progress from tagged, commitment, attention, lower costs
  - Ultimately, when ultra-poor, saving up takes a long time at best
- Improve selection
- Improve products: Match cash-flows
  - Rigid repayment = effectively higher i-rate (hold back $ to make payments)
  - Lean season, conditional loans, flexible repayment timing for risk, bullet for farmers, delayed repayment for startup period
  - Many too scared of debt, don’t even borrow (dream client!)

We put too much on any one paper

Implicit sub-point of the Catch-22 of External Validity problem

Here are some of my personal favorites,
and their contradictions

Contradiction #1
Time inconsistent demand commitment savings?

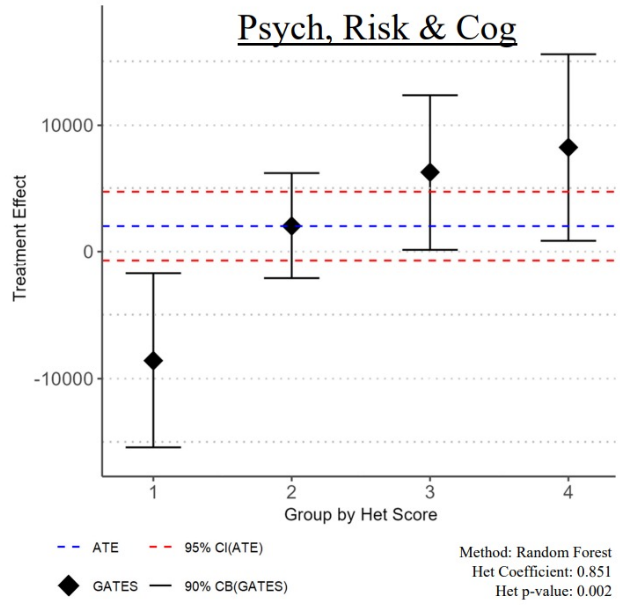
- Tying Odysseus to the Mast (Ashraf et al. 2006)
  - Those time inconsistent more likely to open commitment savings account
  - A few years later: did not replicate.
    - Karlan & Zinman, JDE, very very long footnote
      - Survey design changes
      - Surveyors different (marketers vs surveyors)
      - Prior clients vs new clients
      - Bad luck, sampling variation
      - Commitment rules changed

Contradiction #2
Standard vs consumer credit

- Remember the 7 “standard” microcredit:
  - Entrepreneurial not loans-to-workers
  - Lower i-rates
  - But meh average impacts
- Prior, Karlan & Zinman (2009), South Africa consumer microlender
  - 200% APR
  - 11 percentage points more likely to be employed!
  - Average household income accordingly up
    - Lesson is about credit-->risk management a la Udry (1996).

Contradiction #3
Is selection positively predictive of impact?

- Egypt, attempt to shift micro → SME (Osman et al. 2023):
  - Average impact of 4x vs 2x loans: small positive impact
  - HUGE heterogeneity
    - **Over-optimistic: BAD**
    - Realistic (or under?): GOOD
  - Will it replicate????
- BUT:
  - Mali, farmers, Beaman et al (2023)
  - Farming-tailored loan
  - **Borrowers: high returns to capital**
  - **Non-borrowers: zero return to capital**



Contradiction(s) #4, 5,6,7,8…: Flexible Lending Produce Consistent Results?

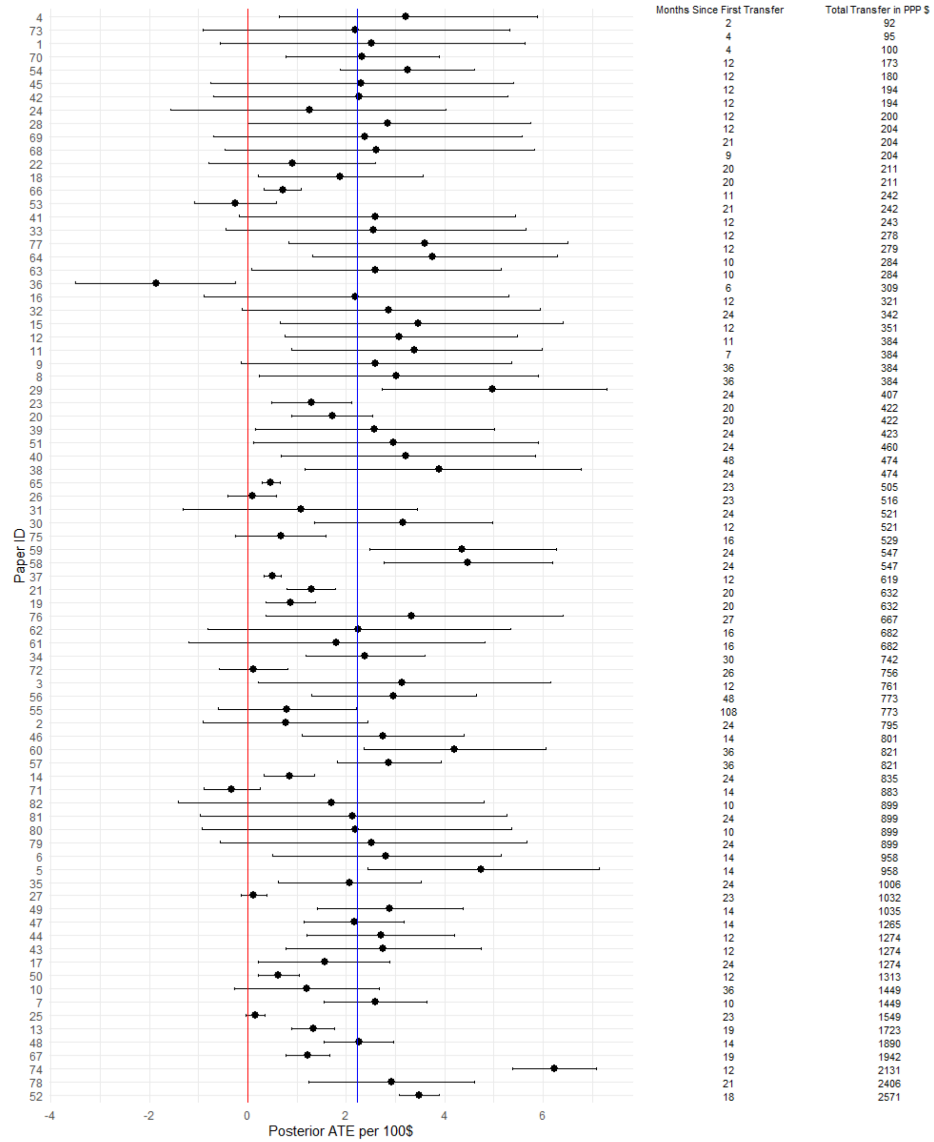
- Six recent(ish) papers
  - Field et al. (2013)
  - Barboni and Agarwal (2022)
  - Battaglia (2021)
  - Brune et al. (2023)
  - Shonchoy and Kurosaki (2014)
  - Aragon et al. (2020)
- Results QUITE mixed
  - Higher firm growth. Or not. (no harm)
  - Higher default. Or not.

Strikingly Consistentish

Meta-Analysis
114 UCT Cash Transfers Papers
Crosta et al. (2024)

Sorted by
Total Grant Amount

Key result:
Impact per $ linear w/r/t grant size



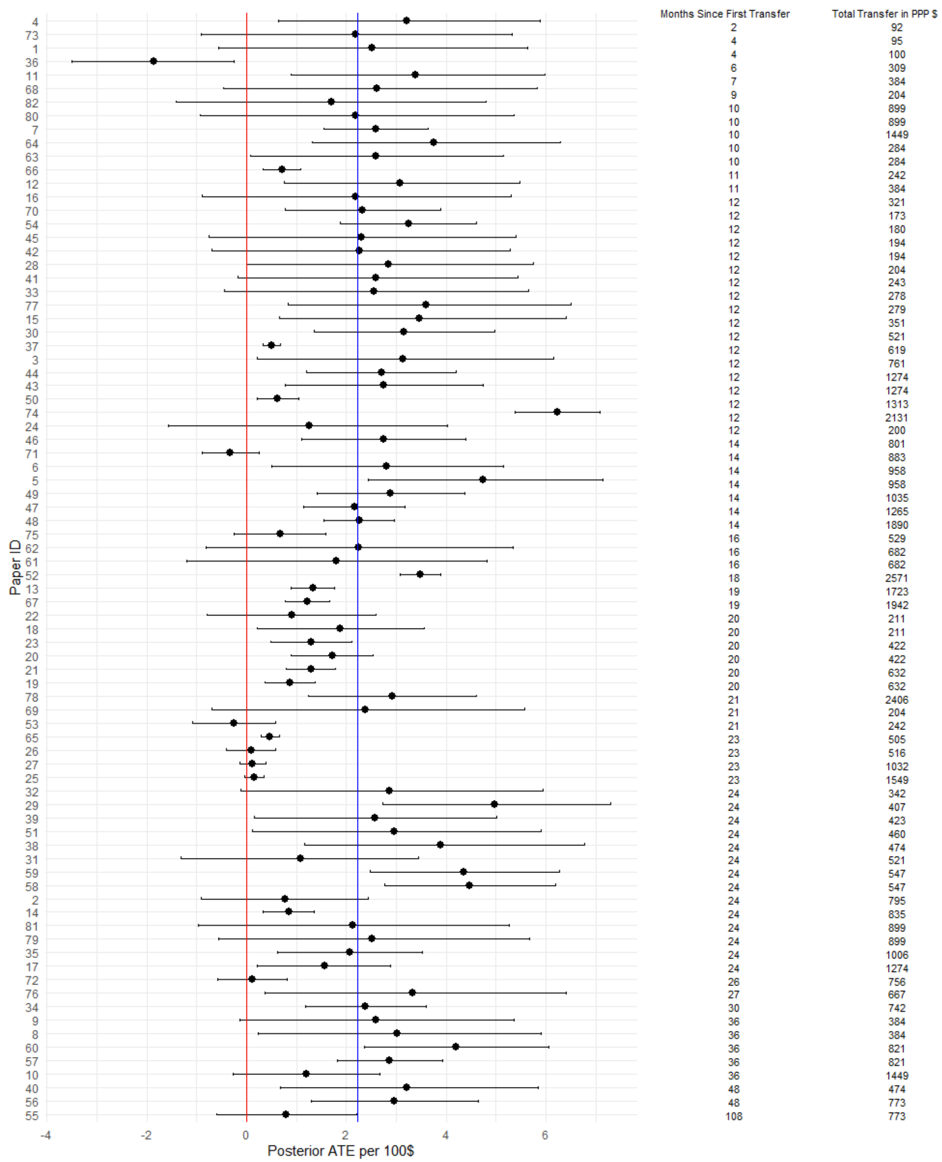
Strikingly Consistentish

Meta-Analysis
114 UCT Cash Transfers Papers
Crosta et al. (2024)

Sorted by
Time since transfer

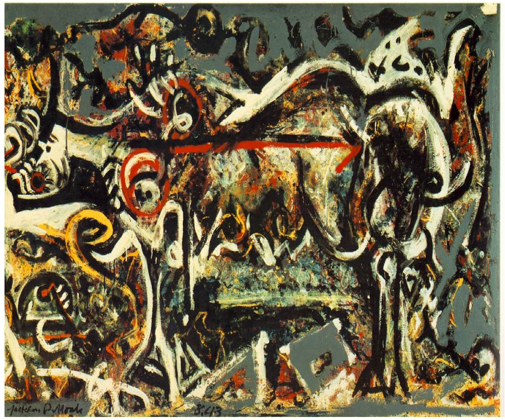
Key result:

Lump-sum: persists, but diminishes
Stream-ongoing: amplifies
Stream-ended: converges to lump-sum



Where does this leave us?

Where we are



Where we can get

Where we will never be

Need more replication, syncing & coordination & measurement research

Theory + Empirics → External Validity → Better Policy

Thank you!

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