Institut ekonomických studií

Fakulta sociálních věd, Universita Karlova Praha
Referee report on the Bachelor/Master Thesis submitted to State Exam

Student Name:	**Bc. Martin Tesař**
Thesis Supervisor Name:	**PhDr. Pavel Streblov, MSc**
Thesis Title:	**Microfinance: Fighting poverty vs. sustainable banking**

Overall Evaluation:

The thesis focuses on microfinance, a hotly debated topic among development economists and practitioners. Martin studies well-articulated and relevant question: Is there a fundamental tradeoff between targeting the poor and financial sustainability of the microfinance organizations (i.e., relying on external subsidies)? In more general terms, the question is: can we rely on purely market solution in delivering the social mission embedded in the microfinance movement? The author collects data from the annual reports of 6 MFIs in South Asia to examine this question and conducts empirical analysis. As I explain below, this thesis is exemplary in many respects, but unfortunately the author does not correctly interpret the econometric results leading it to, in my view, biased conclusions with regard to the main question of interest. Given the overwhelming qualities in all other respects I still recommend to evaluate the thesis with "A" (vyborne).

One can easily identify Martin's long term interest for the topic (the thesis is actually an elaboration of his earlier essay for Economics of Least Developed Countries). He focuses on a very interesting question. He introduces the major microfinance innovations in a very understandable manner and he is capable of critical and balanced evaluation of their pros and cons. He references the right and large number of contributions in the microfinance literature and sometimes even touches questions that are on the frontier of the current research agenda on the topic.

Then Martin turns to the original analysis. He collects data from annual reports of 6 MFIs in south Asia including Grameen Bank and uses an established methodology of Yaron (1992) to approximate the level of subsidies and contstructs the Subsidy Dependence Index. He observes, similarly as earlier studies, that for most the years the MFIs would be in loss if not subsidized. Using his small panel he conducts an empirical analysis. After controlling for the MFI fixed effects he finds several very interesting and plausible results: MFIs that charge higher interest rates and focus more on mobilizing savings need to rely less on external subsidies. In compliance with the infant industry argument it is found that the reliance on subsidies diminishes with maturity of MFI. To answer the main question of the thesis the author looks on the effect of average loan size (proxy for wealth of client base). The coefficient is found to have negligible negative size, though significant. It is concluded that financial independence does not have to be sacrificed to ensure targeting the poor. The tradeoff does not exist and both goals are possible to achieve at the same time.

However, I don't think Martin correctly interprets the result about the loan size. In table 9 the small size of the coefficient for loan size results naturally from the fact that units of loan size are in dollars and units of SDI is typically btw. zero and one. As a consequence beta is low, but it does not mean the effect is small. If the loan size would be in hundreds of dollars instead of in units of dollars, the coefficient would be hundred times bigger. Let's take an example and assume there is an increase in average loan size of $50. Then the results imply that there will be a significant decrease amounting 0.10 in predicted value of subsidy dependence index (SDI). I don't know what is the average SDI in the sample, my guess is that it is around 0.60. In my view this is quite big effect and these results suggest the

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existence of the tradeoff between outreach towards the poor (measured by lower loan size) and financial sustainability (measured by SDI), which makes this study more compliant with what has been found in other contexts (experience with Compartamos in Mexico or Bank Rakyat Indonesia). Figure 25 captures only MFI fixed effects (which are controlled for in the regression). In terms of the question asked, it is more informative to look how the SDI changes for the given MFI as the given MFI changes the loan size (which is what the regressions in columns 2-4 do).

I have two more minor suggestions or topics for discussion. First, I would be keen to know how the results relate to the earlier study of Morduch 1999: The role of subsidies in microfinance. Morduch also calculates the SDI index for Grameen Bank, but for the period 1984-1996. This analysis starts for Grameen at the year 1997. Are these results directly comparable? Morduch's study is referenced, although his results are not compared to even though one could then get longer series of data with similar measure.

Second, as long as a size of client base does not deteriorate, less financial subsidies to MFIs are interpreted as automatically desirable even if the interest rates would need to go up. The fact that individuals are able to repay higher interest rate (to ensure sustainability of MFI) does not necessarily imply that the welfare of individuals is not different. They may spend less on education, health, expanding their business. Or they spend less on trivial expenditures. As with any other social program, one would need to make impact evaluation and cost benefit analysis for this assumption.

To sum up, it is a very nice work, most of it is well above the standards for master theses and I have enjoyed reading it. The author finds several plausible and useful results about financial sustainability in microfinance institutions. Unfortunately one of the key conclusions is affected, I think, by incorrect interpretation of the econometric results. I recommend grade A.

SUMMARY OF POINTS AWARDED (for the explanation of categories and scale, please, see below):

CATEGORY	POINTS
Quality of Research	25
Clarity and Readability	10
Content/Quality of Ideas	40
Organization & Development	10
Manuscript Form	5
TOTAL POINTS	**90**
LETTER GRADE	**A**

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PhDr. Michal Bauer

Evaluated on: **June 9, 2008**

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Explanation of categories and scale:
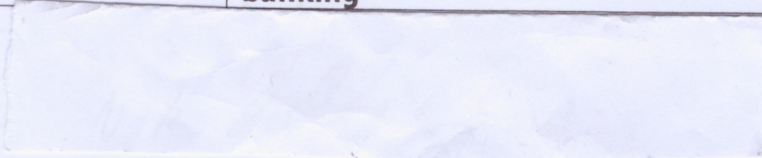
QUALITY OF RESEARCH: *The thesis demonstrates the author's full understanding and command of current literature and he/she uses it competently. The topic of the thesis is well structured and methods used are proper and relevant to the research question being investigated. A full and accurate analysis of thesis statement, from both a theoretical and applied perspective, is provided.*

Strong			Middle			Weak			
30	27	24	21	18	15	12	8	4	0

CONTENT/QUALITY OF IDEAS: *A range and depth of exposition; an appropriate sense of complexity of the topic; appropriate analysis of the thesis statement; and an accurate understanding of theoretical concepts is demonstrated. A full discussion of applicable and relevant theories stylized data is included. Original, creative thought is provided and evident. Demonstrates critical thinking and analysis with application of theory and student's ability to draw conclusions based on their knowledge, skills and research.*

Strong			Middle			Weak			
40	36	32	28	24	20	15	10	5	0

ORGANIZATION AND DEVELOPMENT: *The paper demonstrates a logical and clear arrangement of ideas; an effective use of transitions; a unity and coherence of paragraphs; and a clear development of ideas through supporting detail and evidence. The reader is successfully oriented to the subject, purpose, methodology, and structure of the report; an overview of the whole is included; the reader's attention and interest is engaged. The thesis statement is clearly and definitively stated without ambiguity. The conclusion is strong and reflective of the work as a whole.*

Strong			Middle			Weak			
15	13	12	10	8	6	4	2	0	

CLARITY AND READIBILITY: *Ease of readability; appropriate use of language and style for the rhetorical content; clarity of sentences (reader doesn't get lost; minimum need for slowing down or re-reading) is appropriately demonstrated. Professional level of English expression is evident (limited amount of non-native language to English translation is detectable).*

Strong			Middle			Weak			
10	9	8	7	6	5	3	2	1	0

MANUSCRIPT FORM: *The appropriate manuscript form and style for the rhetorical content; a professional image; an appropriate use of headings and sub-headings; an appropriate format for graphs and tables; an effective referencing of graphs and tables in the text; complete and accurate bibliography documented to support the applied research; and the overall impact of document design is considered.*

Strong		Middle		Weak	
5	4	3	2	1	0