
Recent enthusiasm about microfinance, culminating in the “Year of Microcredit” in 2005, may well have been the proximate motivation for new two volumes on access to finance. Fortunately, the volumes take a much broader view, aggregating current research on how the breadth and depth of the entire financial sector affects individuals, firms and growth.

The first book (Finance for All, or FFA) is written by three staff members of the Finance and Private Sector Development section of the World Bank’s research department, all of whom are widely published in this area. Almost a textbook, the book provides a near-comprehensive overview of what is known about access to finance, with careful attention to policy prescriptions, and needs for future research. Though written at a level accessible to undergraduates or policy-makers, it will also serve as a useful reference to academics unfamiliar with the literature. A key strength is that it often offers sufficient detail when recounting a study that specialists can critically evaluate evidence, without referring to the original paper.

The second book, (Building Inclusive Financial Systems, or BIFS), is an edited conference volume. Each chapter aggregates between three and six shorter presentations, thematically related (in theory), from a 2007 Brookings-World Bank Conference. While not as well published in finance and economics journals, the editors have a broad range of experience in law, development assistance, and government. More uneven in coverage, this volume distinguishes itself by providing more thorough coverage of commercial banking, and the potentially revolutionary role of mobile banking.

Why should one be interested in reading this review, much less either of the books? Because, both books argue, financial inclusiveness matters, for individual welfare, inequality, and economic growth.
FFA makes the case well, citing a range of often high-quality studies throughout the book. BIFS answer to this question most strongly demonstrates the weaknesses of an edited conference volume. Chapter 2 of BIFS, titled “Why does access matter? Impact on Growth and Poverty?” synthesizes four papers. The first addresses the title question, reporting cross-country regressions that relate financial access to growth and inequality. The remainder focus on three rather unrelated questions: which institutions are best suited to deliver microfinance services; whether group liability is necessary for maintaining high repayment in microfinance; and how microfinance has affected the menu of financial services available to Grameen bank clients.

To understand the impact of financial access, it is necessary to measure it. Each book begins with this question: what is access to finance? The answer is not obvious, particularly if one seeks to distinguish between the choice not to use a product (because it is not needed, or too costly) and the unavailability of a product (for lack of physical infrastructure, or credit rationing). Of course, the data rarely admit such fine distinctions. To even measure the share of households with a bank account, FFA relies on three academic papers, which can draw on household surveys from only 34 countries, and must predict bank account usage using administrative data for the rest of the world.

There is wide variation in access to finance: fewer than 20% of households in Sub-Saharan Africa have financial institution accounts, while in Western Europe and North America rates exceed 80 percent. This measure is weakly correlated with GDP per capita, but strongly related to standard measure of financial development, private credit/GDP. A strength of FFA is that much of the data analyzed are available in the appendix or on-line.

Even more interesting is the variation in barriers to access: in Cameroon, the minimum amount necessary to open a bank account is $700, which is higher than the per capita GDP. In Uganda it is 30%
of per capita GDP; Bangladesh has no fees. Not surprisingly, the latter country has more than four times as many bank accounts per capita.

FFA provides much more comprehensive coverage of firms, describing the literature on credit constraints, corruption, new firm entry, bank vs. market finance, the role of credit bureaus, foreign banks, equity market development, and FDI. While no new ground is broken, it is immensely valuable for those new to the literature to have a high-level overview in a compact package. In contrast, BIFS offers only a few pages on firms, reporting for example the degree to which collateral requirements inhibit borrowing.

Much attention is given to household access to finance (Chapter Three of FFA, and the bulk of BIFS). Microfinance has garnered the lion’s share of attention from both the mainstream media and the academy. FFA provides a broad treatment, noting that “the current systematic statistical research evidence on the benefits of microcredit is not overwhelming.” (p. 104). The authors should have gone further, noting that there is to date no good evidence that micro-entrepreneurship enabled by microcredit lifts households out of poverty, though several good studies are underway. The authors rightly call for more research in this area.

Microfinance is transforming household access to finance, and both books devote considerable attention to the profitability of MFIs, with BIFS including an entire chapter to measuring ‘double bottom line’ performance of MFIs. Unfortunately, neither treatment pays much attention to the declared objective functions of MFIs. Compartamos’ recent USD 1.5 billion IPO leaves little doubt that some forms of microfinance can be quite profitable. Other MFIs, particularly those that target the very poor, continually lose money. But neither fact informs us of whether (and by how much) microfinance benefits borrowers.
It is in the coverage of formal financial institutions, and the role of information technology, where BIFS best distinguishes itself from FFA. BIFS takes seriously the idea that formal financial institutions have a role to play in expanding access. In Chapter 5, BIFS discusses the role of commercial banks, contrasting the ‘old paradigm’ in which governments created specialized financial institutions designed to provide agricultural and small business finance with the ‘new paradigm’ which argues commercial banks should profitably serve the poor. Of particular interest to those already familiar with the academic literature are several pages devoted to describing the success of commercial institutions: ICICI of India using MFIs as their agents to make micro-loans; ANZ’s mobile banks in Fiji; and Wells Fargo’s efforts to make unsecured business loans in the United States.

In Chapter 6, BIFS discusses financial infrastructure. The chapter begins by noting that financial services have historically involved very high transactions costs, but that information and communications technology have begun to change this. One particularly astonishing case study involves the roll out of electronic point-of-sale systems throughout Brazil, which reduced the share of Brazilian municipalities without formal financial access from 26 percent to 0 in just three years.

Cell phone banking clearly has the potential to be a disruptive technology. Apart from some successes in the Philippines and Africa, mobile banking has been surprisingly slow to take off. BIFS provides a better discussion of why: technology is not a barrier, nor, evidence suggests, is the willingness of the poor to adopt electronic technology. Rather, it is not yet clear whether such services can be profitable, as providers are wary of the high start-up costs and uncertain revenue stream. The success of payment services depends on the success of the network, particularly if competing networks are not interoperable. Perhaps most important are regulatory restrictions: while in practice mobile deposits could be sold in the same way as prepaid airtime is, in fact anti-money laundering restrictions make it difficult for banks to acquire customers so easily. The declining cost of biometric technology may soon
allow the integration of fingerprint readers into low-cost cell phones, allaying both security and regulatory concerns.

The books, perhaps inevitably, conclude with a discussion of the correct policy response to the problems they have identified. Both books recognize the long and poor performance of government intervention in financial markets, and do not recommend dirigiste policies.

It is easy to come up with generic recommendations that most anyone would support: efficient judicial systems, credible commitments not to expropriate, and insulating financial institutions from political pressure. Fortunately, neither book does this, instead making specific, and often interesting recommendations: implementing regulations that enable mobile banking; assisting in the development of credit registries; and allowing MFIs to take deposits, perhaps working as correspondents with regulated banks. Both oppose usury laws, but FFA does point out the need for some protections, particularly given that consumers new to financial systems may lack sophistication.

An intriguing idea proposed in BIFS is to use insights from the behavioral finance literature in the U.S., and require firms to automatically enroll employees in a retirement plan, or deliver paychecks electronically, unless the employee opts out. Individual inertia could be used to significantly increase access to financial services.

While most readers will focus on the content, they will be well-served by the careful attention to methodology. In FFA, a full-page box is devoted to the question “Are Cross-Country Regressions Credible?” The authors point out that studies are often plagued by “intractable” endogeneity problems, that many instruments proposed are likely not valid, and conclude in the end that cross-country regressions are but one arrow in the quiver of economists. This is particularly laudable given that the World Bank Research group produces a large number of cross-country studies.
Both books advance randomized field experiments as a compelling methodology. Indeed, some of the most clever field experiments in economics have focused on microfinance, and both books describe several field experiments. Of particular interest is work by Dean Karlan and Jon Zinman, which managed to measure moral hazard and adverse selection, the elasticity of demand for credit, and the impact of consumer credit all in a single field experiment. Other work covers the role of credit information bureaus, and group vs. individual liability lending. FFA and BIFS describe much of this work in detail, but also in a way that would be accessible to undergraduates or even an interested layperson.

Both books are in general rather dry, though there is occasional unintended irony in FFA. For example, it laments that “unfortunately, most control groups are not selected until after the program has been started, complicating the subsequent evaluation,” (p. 168). In fact, the World Bank’s Independent Evaluation Group itself rarely engages in prospective evaluations. FFA also criticizes government attempts to increase SME lending, describing its efficacy as “doubtful,” and subject to political subversion. Clearly the authors do not set World Bank Group operational policy, as the Bank’s sister institution, the IFC, funds and oversees large programs designed to do exactly this.

Any comprehensive survey is bound to have errors and omissions. The errors were rare and small and not worthy of mention. I instead note some omissions.

First, there is a striking lack of attention to the business of providing financial services to the poor. The word “profit” does not appear in the entire text of FFA. Both books examine the “sustainability” of microfinance, but neither discusses how the profitability of offering various services affects their provision. While one might be tempted to dismiss this criticism by observing that if services are not provided, they must not be profitable, understanding the size of the wedge between cost and revenues for various products (remittances, savings, credit, and insurance) is essential to understand how to broaden their use.
Second, there is little attention to theory. FFA provides a lucid explanation of Stiglitz and Weiss’ credit rationing model, and occasionally links empirical results to standard theory. But the first chapter, subtitled “Theory and Measurement,” spends only three pages discussing theory, with scant attention to, for example, behavioral models.

A third limitation of the books is their backward-looking nature. Financial services in emerging markets are evolving rapidly and Bank staff and the BIFS conference attendees include many who are close to innovation. It would have been useful to have some (even speculative) discussion of what the landscape might look like in five or ten years.

Other quibbles are minor. Both books tend to present results that are intuitive, suggesting a brief discussion of publication bias might be beneficial. Neither book does a very good job of indicating how important access to finance is, relative to many other constraints thought to impede economic growth. I would have preferred more attention to micro-insurance, as well as the potential importance of financial literacy.

In the final analysis, though, both books provide a good overview of access to finance in emerging markets. Finance for All is a more cohesive document, with a broad discussion of firm and household access to finance, and more logical development. BIFS is inevitably more piecemeal, though provides stronger coverage of some key topics.