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Multidimensional Criticism of Microfinance Institutions in Poverty Alleviation: A Literature Review in the Indonesian Context

Riznar Oliviera[1], Rafi Kumara Sakti[2], Rebecca Yolanda Artha Uli[3], Munasiron Miftah[4], Harry Z. Soeratin[5*]
[1,2,3,4,5] Faculty of Economics and Business, UPN "Veteran" Jakarta, Indonesia
E-mail Correspondence : 2410112072@mahasiswa.upnvj.ac.id[1], 2410112078@mahasiswa.upnvj.ac.id[2], rebeccayolanda@upnvj.ac.id[3], munasiron.miftah@upnvj.ac.id[4], harrysoeratin@upnvj.ac.id[5]

Abstract- This study critically examines microfinance schemes through a comprehensive literature review focusing on economic, social, and gender dimensions. Although positioned as a promising innovation in global poverty alleviation, there is a significant gap between theoretical expectations and field realities. This research utilizes a literature review method to synthesize findings from 15 reputable scientific journals spanning the years 2014–2026, obtained from various databases. The results indicate that economically, microcredit is capable of increasing MSME operating profits through the addition of productive assets; However, it often fails to create new job opportunities due to clients' tendency to utilize family labor for efficiency or even use the credit for refinancing. In the social and gender dimensions, microfinance has proven effective as an instrument for women's empowerment through group models that integrate local cultural and moral values. Furthermore, the challenge of mission drift between institutional profitability and social mission can be bridged through the adoption of digital technologies, such as QRIS and mobile banking, which are capable of drastically cutting operating costs. This study concludes that microfinance in Indonesia remains an appropriate instrument if managed through an integrative strategy that balances technology-based business efficiency with intensive social assistance to achieve a broader and more inclusive impact.
Keywords: Microfinance, Poverty, MSMEs, Digital Transformation, Financial Inclusion.

I. INTRODUCTION

The concept of microfinance, or what is commonly called microfinance, has long been positioned as one of the most promising innovations in global poverty alleviation efforts and driving the growth of micro, small, and medium enterprises [1] . The narrative we often hear usually assumes that providing credit access to underprivileged communities who have not been touched by formal banking institutions (unbanked) will automatically trigger entrepreneurial activity, increase income, and can alleviate them from poverty. This narrative makes microfinance institutions (MFIs) not only business entities, but also social institutions that bear the burden of large social expectations [2] .

As microfinance institutions expand within the community, various literature and empirical evaluations have begun to highlight the gap between theoretical expectations and the reality on the ground. Studies have shown that access to microcredit is not always significantly correlated with entrepreneurial activity or household welfare [3] . In many cases, the credit disbursed is often used to finance short-term consumption needs or simply to cover other debts (refinancing), rather than becoming productive capital that creates added economic value or decent employment.

On the other hand, from an institutional perspective, microfinance institutions are faced with a fundamental dilemma known as mission drift. Microfinance institutions that adopt the Grameen Bank model are often required to balance two conflicting objectives, namely carrying out a social mission to serve high-risk community groups and maintaining profitability to ensure operational sustainability [4] .

In addition to the economic and operational dimensions, the implementation of microfinance also faces social and gender complexities [5] . Although microfinance is often cited as a tool for women's empowerment, access to capital does not necessarily dismantle patriarchal structures. Instead, it has the potential to create a double burden for women and exploit moral and social pressures within the community as a means of loan repayment compliance. [6] .

The complexities surrounding economic effectiveness, institutional dilemmas, and socio-gender implications demand a critical and holistic evaluation of microfinance schemes [7] . Therefore,

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this study was designed to comprehensively review various related literature. In order to unravel the existing paradox and identify relevant research gaps in contemporary microfinance discourse.

II. LITERATURE REVIEW

2.1 Critique of the Impact of Microcredit on Welfare and MSMEs

Microcredit narratives often convey the understanding that microcredit is a tool or form of loan that can be used by lower-income communities to improve their standard of living. However, this understanding often clashes with the reality that access to credit does not necessarily automatically increase the level of consumption or overall household welfare [8] .

Based on research [9] conducted in Hyderabad, India, which at that time was the center of global microcredit growth, it was found that access to microcredit was proven to not produce a significant difference in total expenditure or consumption per capita of households, both in the short term (15-18 months) and the long term (3 years). The article highlighted that the demand for microcredit was not as large as the banking industry had expected, where the lending rate only increased by 8.4% and the loans did not produce an economic “boom” that could drastically change the poverty status of the average borrower.

Microcredit, which was expected to be used by the poor to promote better access to health, education [10] , and women's empowerment, was instead found to be frequently used to refinance living expenses and even to pay off other debts. This phenomenon indicates that microcredit plays more of a role as a financial management instrument than as a driving force for clients' welfare status.

From an industrial perspective, microcredit is always expected to be a bridge for small businesses to transform into larger economies. This increase in business scale does contribute to economic growth, but this contribution can be inefficient if labor productivity is low. The real problem of economic development lies not in the lack of credit for small businesses, but rather in the systemic barriers that prevent business units from becoming more productive and growing larger. Even microcredit has significant risks in economic development [11] .

This matter due to policies that provide incentives for business actors to remain small-scale to avoid tax burdens and regulations. Research from [7] , [5] agrees that MSMEs, which are expected to be drivers of community income and even absorb labor, are inversely proportional to the existing reality. The number of MSME units has indeed grown significantly since the 1998 crisis, but the absorption of labor absorbed by MSMEs tends to provide negative output to the economic value produced. This sector absorbs a massive amount of labor not because the workers know that their jobs are decent and stable jobs but because they are forced to or work simply to survive.

This phenomenon is exacerbated by the fact that microcredit loan customers tend to only empower family members for reasons of efficiency, so that the job creation hoped for by the government remains a pipe dream. This microcredit can be successful in funding the business activities of these MSMEs. The study "The Missing Middle" revealed an ironic phenomenon where policies that favor small businesses actually create disincentives for them to grow [12] . Instead of being a bridge to a larger economic scale, microcredit is often used by small entrepreneurs simply to enjoy easy loan incentives without any ambition to increase the scale of their businesses.

This happens because business actors tend to choose to remain on a micro scale to avoid the burden of taxes, regulatory costs, and strict supervision that usually come into effect when companies grow larger. become beneficiaries of incentives for those who do not need them [1].

Overall, this phenomenon confirms that the benefits of microcredit have shifted from being a vision of a welfare driving machine to merely a financial management instrument that is only used for day-to-day survival. This mismatch shows that the availability of credit alone is not capable of triggering a complete transformation.

2.2 The Dilemma of Social Mission & Business Profitability

The debate between social mission and financial profitability in the discourse of Microfinance Institutions (MFIs), especially those of the Grameen Bank model, is a fundamental dilemma. In terms of financial structure, MFIs have significantly higher marginal operating costs (MOCL) than conventional banks. This is due to the labor-intensive nature of their business model, where intensive mentoring and monitoring procedures are essential to mitigate the high credit risk inherent in poor, unsecured customers [13] . In this context, the setting of higher interest rates by MFIs is not merely a profit-seeking effort,

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but rather a cost-recovery mechanism to ensure the MFIs can continue to operate their businesses.

To address this dilemma, MFIs can start by improving internal efficiency. Research from [14] in the microcredit sector shows that four main factors, namely operational technology, external environment, financial condition, and institutional size, have a significant positive influence on the economic sustainability performance of MFIs. The influence of these factors was found to be much more significant on economic sustainability than operational sustainability.

Optimizing aspects such as loan approval speed, employee professionalism, and technological excellence are key for MFIs to improve their financial performance amidst the demands of their social mission. However, we need to consider external factors such as country regulations, credit indexes, and economic freedom to determine whether an MFI is capable of achieving financial self-sufficiency. Ignoring these variables risks leading to an overestimation of an institution's financial sustainability [15]

There are interesting results regarding research from [11] which shows that MFIs are able to achieve high levels of financial and social efficiency simultaneously, both at very small and large loan scales. This phenomenon undermines the mission drift assumption, because loan size has been shown not to always create a trade-off between profit achievement and social impact. Through innovations such as relational lending, progressive lending, and solidarity groups, MFIs can manage microloans efficiently.

2.3 Strategic Management Practices

He [2]believes that profit and the social mission of an MFI need not be mutually exclusive. In his research, he believes this dilemma can be resolved through the appropriate use of technology and by creating an inclusive and adaptive microfinance ecosystem through collaboration between the government, MFIs, and clients. For example, from a profitability perspective, the use of mobile payment systems such as QRIS has been proven to drastically reduce MFIs' operational costs and increase field officer productivity by up to 68%.

This cost advantage enables MFIs to offer more affordable and faster services to micro-clients, which in turn increases customer retention by 25% and strengthens MFIs' competitiveness. With digitalization, MFIs can reach low-income communities and MSMEs in remote areas that were previously not served by formal banking. Thus, the social mission to reduce poverty and encourage national economic growth can go hand in hand with the sustainability of the institution's business.

If we connect with research from [16] the success of MFIs in maintaining profitability amidst their social mission can be explained through the implementation of disciplined strategic management practices. Gure and Karugu found that Focus Strategy has the strongest influence on the performance of small-scale organizations because it allows managers to fully concentrate on certain market segments that have unique characteristics. In the context of PNM, this focus strategy is implemented by targeting pre-prosperous women through a group model.

2.4 Social, Gender, and Cultural Paradigms in the Scope of Microfinancing

Microfinance from a strategic management perspective is not only seen as a financial instrument, but as a complex instrument of social change and gender empowerment. This strategy not only targets financial growth, but also seeks to dismantle gender and social barriers at the grassroots level.

Based on the findings [17] , it shows that although access to capital increases women's economic mobility and decision-making freedom, this does not necessarily eliminate the double burden of managing business and domestic affairs simultaneously. This study highlights the use of moral and religious instruments as a moral control mechanism so that customers are responsible for their obligations.

This phenomenon is complicated by findings from [18] regarding the existence of significant psychological barriers, where poor communities still have the perception that formal banking institutions are exclusive and intimidating institutions. The absence of services that can effectively mitigate this fear remains a major gap in current financial inclusion strategies. This makes it even more difficult for women, especially those from the lower classes, to develop through microfinance.

Based on this case, there needs to be strategic intervention from both the government and MFIs to develop human capacity, in this case, customers, in a sustainable manner. Shaira [19] in her research emphasized that the productivity of female customers is often hampered by limited access to technology and relevant skills training. Without adequate training, microcredit will only be a short-term financial management instrument and not a total solution for poverty alleviation. This requires MFIs to be

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empowerment partners that provide not only physical capital, but also knowledge capital for their customers.

III. RESEARCH METHODS

The author compiled this research using a literature review method to identify research gaps. Using this method, the author was able to comprehensively synthesize findings from various studies to develop specific research, create a theoretical framework, and identify gaps in existing research. [20] .

The author sets criteria for literature selection, namely: (1) published scientific articles must be in the range of 2014 to 2026 to ensure the relevance of the data used; (2) articles that are in accordance with the provisions (1) will be reviewed by us whether the journal that published is indexed in SINTA 1-3 or SCOPUS Q1-Q3; (3) the selected articles are related to the topics of "microfinance", "grameen bank", or " PT PNM ". After carrying out these three steps, the author found 15 main journals that will be used as the main synthetic basis in this study.

IV. RESULTS AND DISCUSSION

Results

4.1 Economic Effectiveness: Household Welfare and MSME Productivity

The review results show that microfinance schemes in Indonesia have a crucial role in boosting MSME productivity by providing fast and easily accessible working capital. Analysis of the latest literature confirms that microcredit distribution can increase customers' operational profits by increasing their stock of goods and productive assets. However, this economic effectiveness does not happen automatically.

4.2 Social and Gender Dimensions: Women's Empowerment

In the social dimension, this study found that microfinance functions beyond simply providing credit; it is an effective instrument for women's empowerment through a group model. This success addresses the challenge of empowerment effectiveness by demonstrating that capital support coupled with communal social ties is far more effective than providing individual credit without assistance.

4.3 Operational Dilemma Evaluation: Profitability vs. Social Mission

The dilemma between pursuing institutional profits and pursuing a poverty alleviation mission can be bridged through an integrative strategy model. These findings demonstrate that microfinance institutions do not have to experience mission drift or lose their social focus to achieve financial efficiency. Based on the Resource-Based View (RBV) perspective, internal capabilities in the form of digital technology enable institutions to drastically reduce operational costs. This efficiency provides room for institutions to maintain competitive interest rates for the poor without threatening the profitability of the institution as an independent business unit.

Discussion

The use of digital technology in the post-pandemic era is a determining factor that allows customers to be more connected to the market, so that capital assistance is not only used for emergency consumption, but is truly transformed into a sustainable increase in household welfare. Although global studies such as [12] doubt the long-term social impact, the Indonesian context shows different results due to the integration of local cultural and moral values. Social instruments such as regular meetings and the value of mutual cooperation serve as supporting mechanisms that strengthen women's bargaining position in household decision-making [21] .

The integration of digital technology in the post-pandemic era has revolutionized the microfinance landscape by providing more inclusive channels of accessibility for vulnerable communities. The use of this digital platform acts as a key enabler, directly connecting customers with a wider market, significantly improving the operational efficiency and capabilities of micro-businesses. Consequently, the distribution of capital assistance is no longer limited to meeting emergency consumption needs or mitigating short-term risks alone [22] .

The concept of global microfinance often raises skepticism regarding its long-term social impact, as shown in several international experimental evaluations. The dynamics occurring in the Indonesian domestic context show a different track record. [23] . This difference in results is mainly influenced by the integration of local socio-cultural and moral values that are integrated into the micro-credit distribution scheme. Local institutional structures not only position microfinance as a financial transaction instrument per se, but also as a means of community empowerment that is responsive

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to the characteristics and real needs of local communities.

The success of this scheme is further strengthened by the existence of community social instruments, such as regular group meeting forums and a commitment to the value of mutual cooperation, which function as a solid *support system* . Structured social interactions within this forum have proven effective in building social capital, increasing financial literacy, and strengthening women's *bargaining position* in decision-making processes at the household level [24] . Ultimately, this articulation between digital transformation, financial capital, and strengthening local social networks creates a microfinance ecosystem that is not only economically resilient but also socially empowered.

V. CONCLUSION AND SUGGESTION

This study concludes that microfinance remains an appropriate instrument for poverty alleviation in Indonesia if managed through a strategy that balances business efficiency and social empowerment. Household welfare and MSME productivity significantly improve when access to capital is supported by an efficient digital ecosystem and intensive mentoring. Specifically, the gender dimension demonstrates that women are not merely targets for credit distribution but also key agents of family economic change through unique social control mechanisms. Ultimately, the institutional operational dilemma is addressed through the integration of technological innovation; digitalization not only increases institutional profitability but also becomes a key factor in expanding the reach of the social mission of improving the lives of ultra-micro communities more broadly and inclusively.

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