Impact of Credit on the Welfare of Rural Households: Evidence from a Long-Run Panel in Bangladesh

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Access to credit has long been considered a potential solution to ease liquidity constraints and improve household welfare in rural Bangladesh. Households in rural areas often borrow from different formal, quasi-formal, and informal sources and use credit to improve their livelihoods. Being a pioneer of microcredit, Bangladesh has become the global hub of microfinance sector and since its inception many studies evaluated the impact of credit on poor's lives. Most of the studies focused on the impact of microcredit only and hardly evaluated the comparative benefits of different sources of credit. However, available results could not provide conclusive findings, and failed to suggest how different sources of credit affect household welfare in the long-run. In order to fill up this evidence gap and contribute to the on-going academic debate, this study aimed at evaluating the long run impact of different credit sources on household welfare indicators in rural Bangladesh. To generate evidence a five-round (1988, 2000, 2004, 2008 and 2014) true-panel dataset is used which was collected from a nationally representative sample following the multi-stage random sampling technique. 791 households from 62 villages are found to be repeated in all five rounds of the survey. A household level fixed effect regression technique is used to estimate the impact of credit on different household welfare indicators. Results suggest that, access to credit from any source has no significant impact on the increase in household welfare in long-run. However, in the short-run access to bank credit increases access to rented-in land, improve rice yield and enhance girls' school enrolment among rural households. In addition, microfinance can increase income from agriculture and business compared to non-borrowers in the short run. Results also suggest that, credit participation decision of a household depends on past borrowing experience borrowing from any credit source doesn't substitute borrowings from other sources. The impact estimates are found to be consistent over different estimation techniques that imply robust internal validity of the study results. To conclude, as credit is found to be an effective intervention to improve household welfare in the short run but in the long run it is crucial to investigate more why credit fails to generate long run benefit before advocating credit as a sustainable poverty antidote. However, this study recommends strengthening the formal and quasi-formal sources of credit to improve a number of welfare indicators of rural households in Bangladesh.