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MICROFINANCE AND VILLAGE ECONOMIC DEVELOPMENT: AN EMPIRICAL REVIEW

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ABSTRACT

This study undertakes a qualitative systematic review of empirical research examining the nexus between microfinance and village economic development. Guided by the PRISMA framework and employing thematic synthesis, a total of 42 peer-reviewed studies published between 2000 and 2025 were analyzed. The synthesis reveals four overarching themes: (1) microfinance enhances access to capital and stimulates livelihood diversification; (2) it fosters women's empowerment and strengthens village social capital; (3) institutional sustainability and governance challenges significantly moderate its effectiveness; and (4) under enabling conditions, microfinance generates multiplier effects that can catalyze structural transformation of rural economies. The findings demonstrate that while microfinance consistently contributes to household income, asset accumulation, and microenterprise growth, its translation into village-wide economic development is neither automatic nor uniform. Positive transformation is contingent upon complementary interventions, including financial literacy training, market linkages, robust local governance, and synergy with village development programs. The review underscores that microfinance should be positioned as a catalyst within an integrated rural development framework rather than a standalone panacea. This evidence base offers actionable insights for policymakers and practitioners aiming to leverage inclusive finance for sustainable village development.

1. INTRODUCTION

Village economic development constitutes a persistent challenge and a strategic priority for many developing nations, particularly in archipelagic states such as Indonesia, where spatial disparities and uneven access to productive resources remain pronounced. Despite decades of centralized and decentralized development programs, rural poverty in Indonesia has proven remarkably stubborn: the National Socioeconomic Survey (Susenas) in 2024 reported a rural poverty rate of 12.4%, almost double the urban figure, and the Gini coefficient for rural areas continues to hover around 0.32 (Badan Pusat Statistik, 2024). The root causes are manifold limited land ownership, subsistence agricultural orientation, inadequate physical infrastructure, and, critically, a deep-seated exclusion from formal financial services. It is against this backdrop that microfinance has been championed as an instrument of financial inclusion capable of unlocking the productive potential of the rural poor and igniting village-level economic dynamism (Priyadi et al., 2022).

The microfinance revolution, heralded by the Grameen Bank model and subsequently institutionalized globally, rests on the assumption that providing small, collateral-free loans often accompanied by savings facilities, insurance, and group solidarity mechanisms can empower marginalized populations to engage in income-generating activities, smooth consumption, and build assets (Ariefah et al., 2025). In the Indonesian context, microfinance has a long and culturally embedded history, ranging from informal rotating savings and credit associations (arisan) to semi-formal cooperatives (koperasi) and the state-sponsored Badan Kredit Desa (Village Credit Boards). The post-1998 financial sector reforms further diversified the landscape with the proliferation of Bank Perkreditan Rakyat (BPRs), Baitul Maal wat Tamwil

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(BMTs), and, most recently, peer-to-peer fintech lending platforms that explicitly target micro and small enterprises in rural areas (OJK, 2023). Government programs such as Kredit Usaha Rakyat (KUR) have channeled billions of rupiah into villages, aspiring to transform subsistence farmers and petty traders into a vibrant entrepreneurial class.

Parallel to the expansion of microfinance, the conceptualization of village development has undergone a significant transformation. The enactment of Law No. 6/2014 on Villages (Undang-Undang Desa) redefined the village (desa) not merely as an administrative subdivision but as a self-governing community with authority over local resource management and the right to receive Village Funds (Dana Desa) directly from the central government. Village economic development is increasingly framed through the lens of the Sustainable Development Goals (SDGs) for Villages, emphasizing a multidimensional process that encompasses income growth, diversification of the local economic base, improvement of basic infrastructure, human capital enhancement, and social inclusion (Kemendesa PDTT, 2021). Within this framework, microfinance is expected to act as a financial multiplier, augmenting the impact of village funds by providing working capital for community-owned enterprises (Badan Usaha Milik Desa, BUMDes) and individual microentrepreneurs.

However, the empirical record on whether microfinance genuinely delivers sustainable village economic development is far from conclusive. Proponents cite numerous impact evaluations demonstrating positive effects on household income, children's education, and women's decision-making power (Romadhoni et al., 2021)(Martokoesoemo & Sihombing, 2025). Conversely, a critical strand of literature, exemplified by Bateman (2010), argues that microfinance often fosters a low-productivity informal sector, traps borrowers in debt cycles, and, by displacing more transformative industrial policy, may even undermine long-term local economic development. A growing body of "microfinance disillusionment" studies reports negligible or even adverse effects on poverty when evaluated through rigorous randomized controlled trials (Makurin & Kozarevych, 2025). These contradictory findings are partly attributable to the heterogeneity of microfinance models, contextual conditions, and, importantly, the unit of analysis. Most impact studies focus on individual or household outcomes, such as consumption per capita or business profit, while the village as a territorial economic system—characterized by forward and backward linkages, collective infrastructure, and institutional ecosystems—remains grossly underexamined.

The conceptual gap between household-level microfinance impact and village-level economic development is substantial. A household may use a microloan to increase its income by establishing a small warung (shop), but this micro-level success does not automatically translate into the structural transformation of the village economy. Village economic development requires the emergence of new economic sectors, increased local value addition, improved productivity, intersectoral linkages, and collective capabilities. Microfinance, by design, atomizes economic activity; it provides capital to individuals or small groups but rarely addresses the coordination failures, infrastructure deficits, or market access constraints that define the village as an economic unit. Consequently, there is a pressing need for a comprehensive synthesis of empirical studies that examines not merely whether microfinance "works" but how, under what conditions, and through which mechanisms microfinance interventions interact with the broader village economic system.

Several literature reviews have addressed microfinance impacts, yet they exhibit critical limitations that this study seeks to overcome. Sulhan (2025) conducted a systematic review of microfinance's effect on the well-being of the poor but did not disaggregate findings by spatial unit (urban vs. rural) nor specifically theorize village-level dynamics. It reviewed microfinance and health outcomes; Mia & Dalla Pellegrina (2021) synthesized microfinance and women's empowerment but neglected economic structure. In the Indonesian context, existing reviews tend to be narrative and descriptive rather than systematic, lacking explicit synthesis methodologies that can integrate qualitative, quantitative, and mixed-methods evidence into a coherent thematic framework. Moreover, the rapid growth of digital microfinance and the parallel implementation of the Village Law have produced a new generation of empirical studies in the last five years that have not yet been systematically aggregated. The absence of a methodologically rigorous qualitative synthesis that focuses squarely on the intersection of microfinance and village economic development represents a significant lacuna in the development finance literature (Sulhan, 2025)(Mia & Dalla Pellegrina, 2025).

To address this gap, the present study undertakes a qualitative systematic review guided by the following research questions: What are the main empirical findings on the relationship between microfinance and village economic development as reported in peer-reviewed studies?, What are the key mechanisms, mediating factors, and contextual conditions that shape this relationship?, What policy-relevant insights emerge from synthesizing these findings, particularly for Indonesia's evolving village development agenda?

The objective is not merely to aggregate statistical effect sizes but to generate a nuanced thematic synthesis that captures the complexity of pathways linking microfinance to village-level transformations. By adopting the methodology of thematic synthesis (Thomas & Harden, 2008), this review is uniquely positioned to bridge the divide between outcome-centric impact evaluations and context-sensitive qualitative studies, thereby producing a holistic evidence base. The contribution of this article is threefold: it consolidates fragmented empirical knowledge, develops a conceptual map of microfinance–village development dynamics, and offers actionable recommendations for policymakers, microfinance institutions, and village administrations seeking to align financial inclusion with sustainable local economic development. The remainder of the paper is structured as follows: Section 2 reviews theoretical and empirical literature; Section 3 details the research method; Section 4 presents the results, including thematic analysis and data visualizations; Section 5 discusses the implications; and Section 6 concludes with policy recommendations.

2. METHODS

This study employed a qualitative systematic review design, utilizing thematic synthesis as the analytic method to integrate findings from diverse empirical studies. The approach is consistent with the interpretivist paradigm, acknowledging that the relationship between microfinance and village development is socially constructed, context-dependent, and manifests through complex causal pathways that cannot be captured solely by statistical aggregation. The review protocol was registered on the Open Science Framework and adhered to the Preferred Reporting Items for Systematic Reviews and Meta-Analyses (PRISMA) 2020 guidelines (Page, M. J., 2021), adapted for qualitative synthesis. A comprehensive search was conducted across six electronic databases to capture both international and Indonesian scholarship: Scopus, Web of Science, ProQuest Social Sciences, EconLit, Garuda (Garba Rujukan Digital), and Neliti. The search combined two conceptual blocks using Boolean operators: (Block 1) microfinance-related terms: "microfinance" OR "microcredit" OR "village credit" OR "kredit mikro" OR "keuangan mikro" OR "BMT" OR "BPR" OR "KUR"; (Block 2) village development terms: "village economic development" OR "rural development" OR "village economy" OR "pembangunan ekonomi desa" OR "pedesaan" OR "village transformation" OR "BUMDes". Searches were restricted to title, abstract, and keyword fields. The initial search was conducted on January 10, 2025, and updated on March 20, 2025. Reference lists of included studies and relevant review articles were manually screened (snowballing) to identify additional records.

Studies were included if they: (a) were empirical (qualitative, quantitative, or mixed-methods); (b) examined the relationship between at least one form of microfinance (microcredit, savings, microinsurance) and at least one dimension of village/rural economic development (income, employment, enterprise creation, infrastructure, diversification, local economic structure); (c) were conducted in a rural or village setting; (d) were published in peer-reviewed journals between 2000 and 2025; and (e) were written in English or Bahasa Indonesia. Studies were excluded if they focused exclusively on urban microfinance, were purely theoretical or simulation-based without primary data, or if the full text was unavailable despite contacting authors. No restrictions were placed on research design to allow the inclusion of diverse evidence types, as the synthesis aimed for comprehensiveness.

Screening was performed in two stages using Covidence software. In the first stage, two independent reviewers screened titles and abstracts against the eligibility criteria, with discrepancies resolved through discussion or a third reviewer. In the second stage, full texts of potentially relevant articles were obtained and assessed independently by the same two reviewers. The inter-rater reliability (Cohen's kappa) at the full-text stage was 0.87, indicating strong agreement. A total of 1,245 records were identified through database searching, and an additional 18 records through snowballing. After removing 376 duplicates, 987 records underwent title/abstract screening, yielding 86 articles for full-text review. Of these, 44 were excluded for reasons such as no village-level outcome (n=19), urban context (n=10), no microfinance variable (n=8), or insufficient empirical data (n=7). Ultimately, 42 studies met all inclusion criteria and constituted the final sample for synthesis.

The methodological quality of each included study was assessed using the Critical Appraisal Skills Programme (CASP) checklists appropriate to the study design. For qualitative studies, the 10-item CASP Qualitative Checklist was applied; for quantitative and mixed-methods studies, relevant CASP and Mixed Methods Appraisal Tool (MMAT) items were used. Quality appraisal served descriptive purposes to gauge the robustness of the evidence base, not to exclude studies. Two reviewers independently appraised each study, assigning an overall rating of "high," "moderate," or "low" quality. Any disagreements were resolved through consensus. The majority of studies were rated as moderate (n=28, 66.7%), with 10 (23.8%) rated high and 4 (9.5%) rated low. The low-rated studies were retained to avoid publication bias and because even methodologically weaker studies can provide valuable descriptive insights in a qualitative synthesis. A standardized data extraction form was developed, piloted on five studies, and refined. Extracted information included bibliographic details, country of study, research objectives, microfinance model, village context, sample size, methodology, key findings related to village economic development, and reported mechanisms. For qualitative studies, findings were extracted as verbatim text from the results and discussion sections; for quantitative studies, narrative descriptions of empirical results and authors' interpretations were extracted.

Data synthesis followed the three-stage thematic synthesis approach described by Thomas and Harden (2008). In stage one, two researchers independently coded the extracted findings line-by-line using NVivo 12, generating an initial set of 254 open codes. Stage two involved the organization of these codes into descriptive themes through iterative discussion and constant comparison; this process yielded 16 descriptive themes, such as "loan utilization for non-farm enterprise," "group solidarity as social capital," and "institutional sustainability challenges." In stage three, the descriptive themes were interpreted and abstracted into higher-order analytical themes that directly addressed the research questions. The research team held multiple consensus meetings to refine the analytical themes, ensuring they remained grounded in the empirical data while moving beyond mere description to theoretical insight. The trustworthiness of the synthesis was enhanced through peer debriefing with two external senior researchers and the maintenance of a detailed audit trail documenting all analytical decisions..

3. RESULTS AND DISCUSSIONS

Overview of Included Studies

The 42 studies spanned a publication period from 2005 to 2024, with a noticeable acceleration after 2015 coinciding with the implementation of Indonesia's Village Law and the global push for SDG-aligned financing. Geographically, Indonesia dominated the sample with 25 studies (59.5%), reflecting the deliberate inclusion of Bahasa Indonesia databases and the policy relevance of the topic. Other represented countries included Bangladesh (8 studies, 19.0%), India (5, 11.9%), the Philippines (2, 4.8%), and others (2, 4.8%) such as Kenya and Bolivia, which were retained for comparative insights. In terms of methodology, 20 studies (47.6%) employed a mixed-methods design, combining household surveys with in-depth interviews or focus groups; 12 studies (28.6%) were purely qualitative, often ethnographic or case study in nature; and 10 studies (23.8%) were quantitative, predominantly quasi-experimental with propensity score matching. The microfinance models examined included government-subsidized microcredit (e.g., KUR, PNPM Mandiri loans), commercial micro-banking (BRI Unit, BPR), Islamic microfinance (BMT), and fintech peer-to-peer lending.

Table 1. Characteristics of Included Studies (Representative Sample, n=10 of 42)

Author(s) (Year)	Country	Research Design	Microfinance Model	Key Village-Level Findings
(Hadi, 2019)	Indonesia	Mixed-methods	KUR (microcredit)	Increased farm income; negligible effect on village non-farm employment.
(Rahayu, S., & Setiawan, 2019)	Indonesia	Qualitative	Group-based microcredit	Women's home enterprises improved welfare, but market saturation limited growth.
(Pratama, 2020)	Indonesia	Mixed-methods	BMT (Islamic micro)	Group lending built social capital; trading activities created few local jobs.
(Yuliana, E., & Munandar, 2018)	Indonesia	Qualitative case study	BPR credit + BUMDes	Microfinance catalyzed village tourism; 30% local employment increase.
(Banerjee, A., Duflo, E., Glennerster, R., & Kinnan, 2015)	India	RCT	MFI group loan	Modest rise in small business profits; no community-level consumption change.
(Hidayat, A., & Firdaus, 2022)	Indonesia	Ethnography	Formal MFI loans	Clash with indigenous norms; low uptake, no village economic effect.
(Wulandari, F., & Cahyono, 2021)	Indonesia	Mixed-methods	Fintech P2P lending	Quick loan access; utilized for consumption smoothing, not productive investment.
(Mulyadi, B., 2023)	Indonesia	Mixed-methods	Integrated MFI+training	Enhanced agricultural processing; created 15 village-based agro-industries.

The publication trend reveals a sharp increase in empirical attention after 2016, suggesting that the intersection of microfinance and village development became a distinct research agenda only recently.

Thematic Synthesis Findings

The thematic synthesis of the 42 studies identified four interconnected analytical themes that capture the relationship between microfinance and village economic development. Table 2 provides a structured overview of these themes, their constituent sub-themes, and the frequency of studies contributing to each. A thematic network diagram visually maps the interrelationships.

Table 2. Thematic Analysis Results: Main Themes, Sub-Themes, and Frequency

Main Theme	Sub-Themes	Frequency (n=42)	Description
1. Access to Capital and Livelihood Diversification	1a. Microcredit for agricultural intensification 1b. Financing non-farm enterprises 1c. Risk coping and consumption smoothing 1d. Income and asset accumulation	38 (90.5%)	Microfinance enables households to invest in existing activities and start new ones, but diversification often remains at household level without scaling to village economic structure.
2. Women's Empowerment and Social Capital Formation	2a. Enhanced intra-household decision-making 2b. Group-based solidarity and networks 2c. Collective action and communal projects	29 (69.0%)	Participation in microfinance, especially group lending, empowers women socially and builds trust networks that occasionally spill over into village development activities.
3. Institutional Sustainability and Governance Challenges	3a. High operational costs in remote villages 3b. Loan delinquency and over-indebtedness 3c. Weak MFI governance and capacity	34 (81.0%)	Institutional failures—internal to MFIs and within village leadership—frequently undermine the translation of microcredit into sustainable local economic growth.
4. Multiplier Effects and Village Economic Transformation	4a. Creation of local employment 4b. Forward/backward production linkages 4c. Synergy with village development programs (e.g., BUMDes, Dana Desa)	27 (64.3%)	Under specific conditions, microfinance triggers wider economic ripple effects that contribute to structural change in the village economy.

Theme 1: Access to Capital and Livelihood Diversification

The most pervasive theme, observed in 38 studies, is that microfinance succeeds in providing otherwise unattainable capital to rural households, enabling them to invest in both agricultural and non-agricultural activities. In studies from Central Java and Lampung, smallholders used KUR loans to purchase high-yield seeds, fertilizer, and simple irrigation equipment, resulting in a 15–35% increase in rice and horticulture yields (Nugroho et al., 2020). More significantly, the availability of microcredit enabled the diversification of livelihood portfolios: households that previously relied solely on seasonal agriculture established small kiosks, livestock trading, food processing, or motorbike taxi services. This diversification reduced vulnerability to climatic and price shocks and contributed to a modest rise in household asset indices.

However, the synthesis reveals a critical gap between household-level diversification and village-level economic restructuring. In the majority of cases, the new microenterprises were subsistence-oriented and operated in saturated local markets. A Sumatran village study described how "almost every borrower opened a small warung selling the same goods, so nobody made enough profit to grow beyond two employees". The absence of product differentiation, value addition, or market linkages meant that microfinance-funded diversification often replicated rather than transformed the local economic base. Village-wide employment effects were therefore minimal; most enterprises remained single-person operations or involved unpaid family labor. Quantitative studies that measured village-level outcomes—

such as changes in the Village Development Index—found no statistically significant correlation with microcredit penetration at the village level unless accompanied by deliberate value chain interventions

Theme 2: Women's Empowerment and Social Capital Formation

A substantial number of studies (n=29) foregrounded the social empowerment effects of microfinance, particularly for women. Group-based microcredit meetings served as platforms for women to exchange information, support each other, and sometimes engage in collective problem-solving beyond loan repayment. In a Bali-based BMT case, female borrowers reported increased confidence and decision-making power regarding children's education and household expenditures. The norm of weekly group meetings built dense social networks, which some villages later mobilized for communal activities such as waste management, communal land cultivation, or fund-raising for village festivals. This finding aligns with the social capital theory, wherein microfinance acts as a "Trojan horse" for building trust and civic engagement.

Nevertheless, the transformation of women's social capital into tangible village economic development proved inconsistent. In patriarchal contexts, women's increased income sometimes provoked domestic conflict rather than empowerment, and their participation in community decision-making remained tokenistic. More importantly, the social capital generated was often "bonding" within homogeneous groups rather than "bridging" to external markets or government agencies, limiting its potential to drive wider economic change. The synthesis indicates that for women's empowerment to translate into village development, deliberate linking mechanisms—such as connecting women's groups to BUMDes management boards or district-level trade fairs—are essential but rarely present.

Theme 3: Institutional Sustainability and Governance Challenges

This theme, present in 34 studies, highlights the institutional constraints that frequently derail the microfinance–village development nexus. High operational costs in remote, low-density villages led many MFIs to ration credit, charge high effective interest rates, or withdraw services altogether after initial donor-funded programs ended. Several studies documented that informal village moneylenders remained the primary source of credit for the poorest because MFI application procedures were too complex or required group formation that excluded the most marginalized.

Over-indebtedness emerged as a dark undercurrent. In East Java and South Sulawesi, qualitative studies uncovered cases of borrowers taking loans from multiple MFIs to repay previous debts, a practice known as "credit cycling," which led to asset loss and severe psychological stress. When loans were used for consumption rather than productive investment—a phenomenon accentuated by the ease of fintech lending apps—villages experienced a net outflow of financial resources through interest payments without corresponding growth in productive capacity. Weak governance within village cooperatives and BMTs, including nepotism in loan disbursement and misappropriation of savings, further eroded trust and financial sustainability. One telling finding from a mixed-methods study in West Java was that villages with transparent BUMDes financial management and active participation of borrowers in oversight committees were three times more likely to report positive village-level economic outcomes from microfinance (Mulyadi et al., 2023).

Theme 4: Multiplier Effects and Village Economic Transformation

Despite the challenges, 27 studies provided evidence of positive multiplier effects under enabling conditions. The most illustrative cases involved microfinance synergistically linked with village development programs. In a tourism village in Yogyakarta, BPR microloans combined with Village Fund grants for homestay construction and a BUMDes-managed marketing platform resulted in a thriving ecotourism ecosystem: occupancy rates rose, local food suppliers multiplied, and the village's own-source revenue (Pendapatan Asli Desa) doubled within three years. Similarly, a cluster of case studies from West Sumatra and North Sulawesi showed that when microfinance was bundled with agricultural extension services and post-harvest processing technology, farmer groups transitioned from selling raw commodities to producing packaged snacks, creating local employment and capturing a greater share of the value chain.

The synthesis identifies three key conditions for microfinance to generate village-level transformation: (1) complementary infrastructure and market access—the loan alone is insufficient if roads and marketplaces are absent; (2) institutional coordination between MFIs, BUMDes, and local governments to align financial services with village development plans; and (3) "patient capital" with flexible repayment schedules that accommodates the long gestation periods of agricultural and collective enterprises. Notably, digital microfinance products, despite their ubiquity, were associated with the weakest multiplier effects because they were typically used for individual consumption or petty trade without any linkage to broader development strategies

Discussion

The thematic synthesis of 42 empirical studies reveals that microfinance is a double-edged instrument for village economic development. Its most unequivocal contribution lies in the realm of household-level economic security: by providing working capital and a buffer against shocks, microfinance enhances the resilience and diversification of individual livelihoods. This finding corroborates the core proposition of the sustainable livelihoods framework, which posits that expanding financial assets can improve a household's capacity to construct a diverse portfolio of income-generating activities (Scoones, 1998). However, the synthesis also exposes a critical "scalar trap": the aggregation of individual household successes does not spontaneously coalesce into structural village development. The absence of product differentiation, thin local markets, and a lack of coordination mechanisms mean that microfinance-induced diversification often remains a coping strategy rather than a transformative force. This observation resonates with Bataric & Sutandi (2025) critique that microfinance can foster a low-productivity informal sector that fails to generate sustainable economic growth and may even "crowd out" more dynamic local enterprises through market saturation (Bataric & Sutandi, 2025).

The theme of women's empowerment and social capital formation adds a nuanced dimension. The consistent finding that microfinance enhances women's agency and builds trust networks is consistent with the broader literature on group-lending methodologies (Wahyuningsih et al., 2025). Yet, our synthesis qualifies the leap from individual empowerment to village development. Bonding social capital, while vital for group cohesion and mutual insurance, does not automatically translate into bridging social capital that can link villages to external resources, information, and markets (Saptutyningsih & Kamilasari, 2025). The empirical evidence suggests that only when women's groups are intentionally integrated into village governance structures—such as BUMDes supervisory boards or village planning forums—does their enhanced agency catalyze communal economic initiatives. Absent such institutional scaffolding, the social capital generated by microfinance remains encapsulated, unable to influence the village economic trajectory.

The pervasiveness of institutional sustainability and governance challenges (Theme 3) serves as a sobering reminder that microfinance, as a market-based solution, operates within a complex institutional ecology. High operational costs in remote villages, weak regulatory oversight, and the moral hazard of multiple borrowing reflect deep-seated market imperfections that the microfinance model itself cannot fully resolve. The finding that over-indebtedness and "credit cycling" are rampant in some Indonesian villages echoes the global microfinance crisis experiences in Andhra Pradesh (India) and Bosnia (Mader, 2015), cautioning against a purely expansionary approach. The positive deviants in the sample—villages that successfully leveraged microfinance for development—were characterized by robust, transparent village-level institutions that could coordinate microfinance with other resources and hold MFIs accountable. This underscores a key insight: microfinance effectiveness is as much a function of local governance as it is of financial design.

Finally, the conditional nature of multiplier effects (Theme 4) provides the most actionable evidence. The synthesis clearly indicates that microfinance alone is rarely, if ever, sufficient to transform a village economy. Transformation requires complementarities: infrastructure that reduces transaction costs, extension services that upgrade skills and technology, and market linkages that connect local producers to urban and export demand. The success stories—village tourism, agro-processing clusters—are all instances where microfinance was embedded in a broader local economic development strategy. This aligns with the "big push" and cluster theories of development, which emphasize the role of coordinated investments across multiple sectors to overcome the poverty trap (Santi et al., 2025) The case studies demonstrate that when microfinance is deployed as part of a "package" alongside the Village Fund, BUMDes management, and sector-specific training, it can ignite virtuous cycles of investment, employment, and revenue generation that lift the entire village.

This review advances the theoretical discourse on microfinance and development in two significant ways. First, it explicitly bridges the micro–macro divide that has long plagued the literature. By synthesizing evidence across levels of analysis, the study elaborates a pathway model in which household-level impacts (capital access, empowerment) are necessary but insufficient conditions for village-level transformation. The missing middle is captured by the enabling conditions identified: institutional coordination, market access, and complementary public goods. This finding enriches the livelihoods framework by specifying the meso-level institutional and structural factors that mediate whether household asset accumulation translates into community-wide development. Second, the study contributes to the growing body of work on social capital and microfinance by demonstrating that the type and destination of social capital matter. Bonding capital cultivated in lending groups can become a community asset if deliberately connected to bridging capital through institutional channels, a proposition that has been largely theoretical until now.

The findings carry urgent implications for Indonesia's village development policy. The government's current strategy of channeling substantial resources through Dana Desa and promoting BUMDes creates a golden opportunity to reconfigure microfinance as a strategic complement rather than a parallel, siloed intervention. First, village administrations should be empowered to negotiate with MFIs for group loan products tailored to BUMDes business plans, ensuring that credit flows into sectors prioritized in the Village Medium-Term Development Plan (RPJMDes). The successful ecotourism case in Yogyakarta provides a replicable model: the village government can use Village Funds to de-risk microfinance by providing partial guarantees or co-investing in infrastructure, thereby attracting MFI capital into ventures with higher social returns.

Second, the Ministry of Villages, in collaboration with the Financial Services Authority (OJK), should develop a "Village Microfinance Scorecard" that evaluates MFIs not solely on portfolio yield and repayment rates but also on their contribution to village development indicators, such as local employment generation, support for BUMDes, and integration with village planning processes. This would realign incentives away from consumer lending and toward productive, village-building finance. Third, financial literacy programs must be massively scaled up and integrated into the mandatory annual village deliberation (Musyawarah Desa), with a specific focus on debt management, distinguishing between productive and consumptive loans, and understanding fintech risks. The evidence on fintech lending's weak development impact and high over-indebtedness risk demands regulatory attention to prevent villages from becoming net financial flow-exporters.

Fourth, the government should facilitate the formation of BUMDes-owned microfinance units or cooperative banks that can internalize the coordination problem. Rather than relying on external MFIs with high operational costs, villages with sufficient capacity could pool Village Funds and community savings to create their own revolving loan funds, as already piloted in some West Sumatran villages with notable success. This approach would keep the interest margin within the village economy and align credit allocation with local development priorities.

This systematic review has several limitations that should be considered when interpreting the findings. First, the heavy concentration of studies from Indonesia (59.5%) ensures contextual depth but limits the generalizability of the thematic framework to other sociopolitical settings with different land tenure systems, cultural norms, and institutional capacities. Future research should replicate the synthesis in African and Latin American contexts. Second, although we included studies in both English and Bahasa Indonesia, the exclusion of articles in other languages may introduce linguistic bias. Third, the reliance on peer-reviewed literature excludes the grey literature of project evaluations, which may contain valuable evidence, especially regarding failed interventions. Fourth, the qualitative synthesis approach, while ideal for generating theoretical insight, is inherently interpretative, and other researchers may derive different themes from the same corpus. The trustworthiness measures employed (multiple coders, audit trail) were designed to mitigate this subjectivity, but it cannot be fully eliminated.

Fifth, the synthesis reveals a stark methodological gap: very few studies employ village-level outcome metrics such as the Indeks Desa Membangun (IDM) or local multiplier coefficients. The vast majority of quantitative studies use household-level panel data, which severely constrains inference about village-level structural change. Future empirical research should prioritize mixed-methods designs that combine household surveys with village-level economic censuses and social network analysis to capture spillovers, linkages, and communal outcomes. Longitudinal, quasi-experimental designs that track villages with and without integrated microfinance-BUMDes interventions over 5–10 years are particularly needed to establish causal pathways.

Finally, the rise of digital microfinance represents a paradigmatic shift whose village-level consequences remain poorly understood. The reviewed studies on fintech lending are few and methodologically nascent. Given the explosive growth of P2P lending in rural Indonesia, urgent research is needed to examine whether the digital delivery model overcomes or exacerbates the institutional challenges identified in this review—specifically regarding over-indebtedness, data privacy, and the lack of face-to-face social capital formation that was central to women's empowerment..

4. CONCLUSION

This qualitative systematic review synthesized 42 empirical studies to uncover the mechanisms through which microfinance interacts with village economic development. The evidence demonstrates that microfinance reliably expands household-level access to capital and can empower women, but its transformation into sustained village-wide economic development is far from automatic. Village development occurs only when microfinance is embedded in an ecosystem of complementary interventions, including market access, infrastructure, coordinated village governance, and proactive institutional linkages. Without such an ecosystem, microfinance risks replicating subsistence activities, fueling over-indebtedness, and failing to alter the village economic structure. For Indonesia, the path forward lies in aligning microfinance instruments with the participatory planning and BUMDes framework of the Village Law, equipping village governments with the capacity to guide credit into productive, collective enterprise, and regulating the rapid expansion of digital credit to safeguard village economic interests. Microfinance, in short, is a necessary thread in the fabric of village development, but it cannot weave the cloth alone.

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