Role of Micro Finance Institutions in Poverty Reduction

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Abstract: This study examines the relationship between microfinance and poverty reduction in Pakistan. We viewed significant literature for the study. We use these hypothesis to measure the relationship between dependent and independent variables. Target people for this study was low income households and women involved in small scale business in Pakistan. We examine this affiliation through primary data. To analyze the data generated, ANOVA and descriptive statistics test were used on SPSS. The analysis revealed that there is a significant relationship between microfinance and poverty reduction. In the pursuit for solutions to the country’s development and poverty alleviation microfinance is becoming one of the most popular choice as credit has been found as obstruction facing by the poor people.

Keywords: Micro Finance, Poverty Reduction, Households, Micro Credits.

INTRODUCTION

Microfinance is a kind of banking service which delivers financial service to jobless or low income individuals or the type of peoples who have no other means for acquisition of financial services (Mutesasira and Wright, 2001). The ultimate purpose of these banks is to provide financial support to the low income people and assist them by providing an opportunity to become self-sufficient by the various means of saving money, borrowing money and insurance. Micro Finance even certainly plays an important role in providing a safety net and consumption smoothing. The research is mainly conducted to understand the role of Micro Finance banks in alleviating poverty in Pakistan.

“The credit policy for the poor involves many practical difficulties arising from operation followed by financial institutions and the economic characteristics and financing needs of low-income households. For example, commercial banking institutions require that borrowers have a stable source of income out of which principal and interest can be paid back according to the agreed terms. However, the income of many self-employed households is not stable. A huge number of micro loans are needed to serve the poor, but banking institution prefers dealing with big loans in small numbers to minimize administration expenses. They also look for collateral with a clear title—which many low income households do not have”.

Reduction of poverty is partly a process of increasing income and economic stability which enables fulfillment of basic needs and access to different kinds of services. This may also be understood in the form of developing a range of assets that will reduce the vulnerability of the poor of physical, economic and social shocks. Therefore, several studies have been published on microfinance and poverty reduction. In some of these studies, microfinance has brought positive impact to the life of clients, boost the ability of poor individuals to improve their conditions and others have indicated that poor people have taken advantage of increased earnings to improve their consumption level, health and build assets. However, other studies have shown that microfinance is said to play insignificant role towards poverty reduction.

LITERATURE REVIEW

Asemelash (2003) EthiopiaThe microfinance provided to the poor has brought a positive impact on the life of the clients as compared to those who do not get access to these microfinance services. He showed that microfinance has brought a positive impact on income, asset building, and access to schools and medical facilities in the study area

Alemu (2006)The study has found out that the poor have smoothed their income in the study area. However, there was fungibility in the sense that clients were using the loan for unintended purposes.

Rajendran and Raja (2010)Microfinance and self-help groups are effective in reducing poverty, empowering women, creating awareness and ensure sustainability of environment which finally results in sustainable development of the nation.
Imai, Arun and Annim (2010) The study show that loans for productive purposes were more important for poverty reduction in rural than urban areas and significant positive effect of Microfinance Institution productive loans on multidimensional welfare indicators.

Green Kirkpatrick and Murinde (2006)The causal linkages among financial policy, enterprise development and poverty reduction remain a key challenge given the commitment to achieve the MDGs by 2015.

PROBLEM STATEMENT

There is no study conducted on the role of microfinance institutions in poverty reduction in Pakistan. The problem of this research is to checking out the impact of microfinance on poverty reduction.

OBJECTIVES

The aims and objective of the research is to understand the impact of microfinance loans in poverty reduction of the Pakistan.

Objective of our research is:

- To understand the role of Micro Finance Banks in poverty reduction.
- To identify and analyze the factors affecting the working of Micro Finance Bank.

METHODOLOGY

A cross sectional self-administered questionnaire consisting of precise the point questions which covers all the aspects of the research proposal are thoroughly filled comprising of 80 targeted respondents, out of which 60 are our best responses for analysis. These questions are filled out by customers of Micro Financial Institutions which had obtained and willing to obtain short term microloans and microcredit.

Some of the main institutions from which questionnaires are filled from the customers of FINCA Micro Finance Bank, First Micro Finance Bank, KHUSHAKLI Bank Ltd, APNA Micro Finance Bank Ltd, and kashaf foundation.

For the relevant topic of the research proposal i.e. Role of Micro Financial Institutions for Poverty Alleviation in Pakistan. We select Lahore Pakistan as our targeted area and conduct our respective research.

Data mainly primary in nature are collected, summarize and analyzed through questionnaires and discussions and are then completely analyzed statistically through SPSS software for which the statistic results like Regression, Standard Deviation, Mean Deviation etc. are derived to prepare conclusion and to test the correctness of our hypothesis.

Significance of Study

The significance of this study is to establish whether Micro Finance actually reduce poverty or there are other mediating factors that produce and impact.

Limitations of the Study

Limitation of this study is that we have focused on a small and specific location of Pakistan i.e. Lahore which is a limited area of Pakistan. Research should be done on whole Pakistan to get better and proper results.

Hypothesis

H1: There is a significant relationship between microfinance and poverty reduction.

Variables

Micro Finance Loans is an independent variable. Poverty Reduction is a dependent variable as it is depending on Micro Finance Loan.
DATA ANALYSIS

Descriptive Statistics (micro loans)

<table>
<thead>
<tr>
<th></th>
<th>N</th>
<th>Minimum</th>
<th>Maximum</th>
<th>Mean</th>
<th>Std. Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average ML</td>
<td>60</td>
<td>1.40</td>
<td>3.40</td>
<td>2.3233</td>
<td>.45858</td>
</tr>
<tr>
<td>Valid N (list wise)</td>
<td>60</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

The variable satisfaction standard deviation lies between -1 and +1 that means the variable have a good relation with other variable poverty reduction. And also the mean of this variable are closer to each other.

Model Summary

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
<th>Durbin-Watson</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.723</td>
<td>.522</td>
<td>.514</td>
<td>.78382</td>
<td>1.883</td>
</tr>
</tbody>
</table>

In this test the Adjusted R square is 0.514 it means that 51.4% the independent variables have effect on dependent variable. And also shows that positive relations of dependent variable (poverty reduction) with independent variables (microloans).

In this test the Durbin-Watson also shows values 1.883 also lies under the Durbin Watson values 1.5-2.5. It also shows that the relation is very good and variables are true.

ANOVA

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>Df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Regression</td>
<td>1</td>
<td>38.950</td>
<td>63.399</td>
<td>.000b</td>
</tr>
<tr>
<td></td>
<td>Residual</td>
<td>58</td>
<td>.614</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Total</td>
<td>59</td>
<td>63.950</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

This above model shows that sig 0.000 it means that this value is below than threshold beta value 0.005 it means this test is valid and the variables can play a role in poverty reduction.

Correlations

<table>
<thead>
<tr>
<th></th>
<th>Poverty reduction</th>
<th>Microloans</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pearson Correlation</td>
<td>1.000</td>
<td>.723</td>
</tr>
<tr>
<td></td>
<td>.723</td>
<td>1.000</td>
</tr>
</tbody>
</table>

This correlation test between microloans and poverty reduction shows that these independent and dependent variable very correlate with each other the poverty reduction value is 1.000 and microloans value is 0.723. It means that 72.3% microloans independent variables have correlate with poverty reduction.

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Conclusion:

From above analysis we conclude that there is significant relationship between Micro Finance and Poverty Reduction. The significance level is 0.00 that is less than threshold value which shows that Micro Finance has positive relationship with poverty reduction. Further the analysis shows that our adjusted R square is 51.4% which indicates dependent variable depends on independent variable. Correlation test between microloans and poverty reduction shows that these independent and dependent variable very correlate with each other the poverty reduction value is 1.000 and microloans value is 0.723. It means that 72.3% microloans independent variables have correlate with poverty reduction.
Recommendations:

It is now necessary from Micro Financial Institutions that they should expand their services covering all aspects of society. So, that more and more poor people of Pakistan can be easily aided from these Micro Credits and Loans. Moreover they should develop separate departments for proper guidance and information about attaining and usage of this loan.

Government of Pakistan should pay utmost attention and impose those regulations that moderates interest rates on microloans.

References:

- Graham A.N., Wright and Mutesasira L., 2001, the relative risks to the savings of poor people, Micro-Save Africa.