

THE EFFECTIVENESS OF ROLE OF MICRO FINANCE ON ECONOMIC DEVELOPMENT: PAKISTAN'S PERSPECTIVE

Hasan Raza

Assistant Professor, Department of Commerce, University of Karachi,
PAKISTAN.

hasan.raza@uok.edu.pk

ABSTRACT

This Paper will highlight the significant importance of micro financing for the economic development as well as for economic growth. Most of the people living in Pakistan are unaware from the services offered by the financial institution including banks. Microfinance is the main source that is helping to expand the source of financing all over the world. Micro Finance is providing the platform to under develop as well as developing countries to make their economic growth more accelerated. Research is conducted through the survey, in which 350 participants was involved. Findings of survey is showing that Microfinance is providing opportunities to improve the living standards, reducing the crime rate, providing opportunity for better education facility, availability of healthcare facility, reducing poverty and stabilizing the economy of country through more employment opportunities. In Pakistan Manufacturing sector in the urban areas has 98% of manufacturing units operated by small and unregistered firms. Meanwhile, 51.4% of the employment in urban manufacturing is provided by the informal or small scale sector, if this area of manufacturing is financed through the micro financing schemes it will help the economy to grow more effectively. If Microfinance loans are provided with proper mechanism, it can bring much positive effect on the country's economy.

Keywords: Microfinance, Economic Development, Poverty, Micro Entrepreneurship

INTRODUCTION

More than one billion people of the world live in households that earn only one dollar a day. Most of these people are not likely to be able to get financial services from the formal commercial banks which demand collaterals. Therefore, it is needed that microfinance provides them with capital exclusive of these conditions. In developing countries rural population are often found engaged in financial activities – credit associations, rotating savings, savings clubs and mutual insurance societies – which are both informal and also tend to be erratic and insecure. Microfinance is now deemed as one of the most essential and effective mechanism for economic growth and its sustainability. By providing opportunities for self-employment many studies and researches have concluded that these programs have significantly improved employment rate, productivity, earning capacity, reducing poverty, living standards, empowerment, education, food, status and other social impacts.

In Pakistan, the microfinance sector comprises regulated and self-regulated organizations including MFIs, NGOs and Banks. The World Bank's Consultative Group to Assist the Poor states that microfinance sector entered Pakistan late but the country is not much lagging behind other countries of the region – South Asia as well as South East Asia as the country made considerable strides towards development after announcement of the Microfinance Ordinance in 2001. The country's policymakers appear to aim at creating a conducive environment for the MFIs to take roots, grow, spread branches and offer an extended range of monetary services to the poor. However, the sector is still plagued by a limited retail capacity, narrow institutional base, and little, if any, financial integration.

Pakistan has the sixth largest population in the world and a huge proportion of Pakistan's population is suffering from poverty problem. Pakistan has strong potentials to be an economic developed country because of its economic resources. Unfortunately, Pakistan has not attained any remarkable achievement due to socio economic instability. Pakistan has lagged far behind in economic sector and it could not achieve the economic growth, economic sustainability and development of entrepreneurial environment which it deserves.

According to an estimation, Pakistan has a target market of 25 to 30 million borrowers in the Microfinance industry and the Government of Pakistan had decided to enhance the outreach to 3 million borrowers at least by 2010 which later on taken to another advance level of 10 million by 2015.

REVIEW OF LITERATURE

Microfinance and Economic Development

There are two factors, which define a microfinance programs' effect on economic development. These are described as the growth potential of activities, which these programs finance and the extent of credit market imperfections which enhanced availability of credit resolves (Mudacumura, Mebratu, & Haque, 2005). Poor households as well as micro entrepreneurs' have strong demand for savings services as the demand for credit and they do respond positively to proper savings incentives and also the saving's instruments. Usually, these entrepreneurs make savings in non-financial forms and hoard or use arrangements of informal nature. This potential for savings by the poor has been largely neglected by formal financial institutions. Meanwhile, it is learning for the MFIs that in the long run they can get the major chunk of their resources from the savers themselves (Gulli, 1998).

A sizable portion of the underprivileged people likes to initiate a micro project but is handicapped by lack of credit facilities. Such people are helped by microfinance which enables them to launch new production that translates into income and employment for them and other people (Amha, 2002). The owners of small businesses begin their rural and urban enterprises on a really micro scale and often without assistance. Such entrepreneurs manage to maintain their operating costs low by utilizing handmade or used equipment and family labor. While they also save rent often by using their houses as their factories. It is generally held that these entrepreneurs have usually no access to capital except for the resources offered by their family or friends or some professional moneylenders. However, substantial enterprises can be built only those, who get an access to productive resources. Meanwhile, it has been established that assistance of micro entrepreneurship can be an effective strategy in local communities for generating new income (Maier & Pischke, 2007).

The MFIs are a necessary part of any financial system as they specialize in retail credit advances for the poor customers' consumption and production needs and also mobilize their savings. With their growing economic viability, the microfinance institutions have started to get access to the capital markets' huge financial resources. These MFIs have also contributed in bringing betterment in the social and economic conditions of their respective areas (Karmakar, 2008).

A microfinance program facilitates economic betterment by offering financial services which ease liquidity constraint on production. The availability of finances encourages peoples to take production risk, which helps create a true class of micro entrepreneurs. This class in turn may change into an economy's backbone. The success stories from Japan and Middle East show that these small and micro projects financed by MFIs may evolve into medium sized enterprises and these medium sized businesses do play an important role in revival of economic activities. Microfinance programs may also enable borrowers to develop a new

technology at a small scale. Such innovation in turn may increase efficiency and productivity and also the income of the borrower (Berger, Goldmark, & San, 2006). Micro entrepreneurship also has the potential to generate economic activities (Gulli, 1998). Microfinance is therefore important to take forward and sustain the ongoing projects of small nature (Shonchoy, 2014).

The small-scale businesses facilitate in industrial growth while reducing income inequalities. This has been witnessed in Japan and Taiwan, where the SMEs have contributed in their economic growth and acted as their economy's backbone. Jones & Sakong (1980) has shown that these countries' micro environment – comprising government, private sector, nongovernment organizations, market as well as external institutional supports – have played a vital role in their success (Jones & Sakong, 1980). In the case Japan, this small scale business sector has continued to complement rather than compete with the larger businesses. It can therefore, be safely assumed that these MSMEs can also change into an important source of Pakistan's economic growth (Maier & Pischke, 2007).

Micro entrepreneurship's experience in countries like Japan, Korea and Taiwan manifest that such businesses can work in unison with large concerns by offering quality inputs while reducing costs of items of intermediate and semi-finished nature and also serving as a major source of technically sound human resource (Ledgerwood J., 2001). In Japan the contribution of micro and small scale sector is 52% in manufacturing value addition while in Korea the share is somewhere around 40%. In Pakistan, the small and medium enterprises do 35% value addition in the manufacturer sector. However, here the linkage among large, micro and small scale industries remains somewhat limited.

Pakistan Scenario

In Pakistan, government in the past provided credit incentives to large manufacturers and discriminated against smaller businesses. Naqvi (1990) says careful focus on micro and small scales units can lead to the capital's socially efficient allocation and may have the greatest potential for generation of productive employment. Even in the present situation Pakistan's small and medium-size enterprises including cottage industries make a significant contribution to the growth of GDP. This contribution of the MSMEs is about three times more than large industries. The MSMEs are definitely the capital's more efficient users and also labor intensive, employing the manufacturing sector's 80 % workforce. But in spite of that, this sector only gets 20% of the credit and has to depend on expensive non-institutional credit. The country's economy has grown at a rate of around 3.84% per year from 2009 to 2014 and MSMEs have contributed a great deal in this growth (www.finance.gov.pk).

The Central Bank, State Bank of Pakistan's policies has enabled the banking sector to undergo significant growth. In the last two years, the foreign investors as well as international players have entered the densely populated and largely untapped market and reached an all-time high gross loan portfolio (GLP) of the microfinance sector Rs. 93 billion with 39.3% increase in year on year. By end of the 2015', the numbers of microfinance sector active borrowers have reached the figure of 3million which is a milestone achieved (www.pmn.org.pk).

In the recent year, Pakistan has seen a number of developments in terms of MFIs. Pakistan Telecommunication Company (PTCL) acquired Rozgar Microfinance Bank, Orascom Telecom Holdings and Advans Pakistan Microfinance Bank set up Waseela Microfinance Bank. Telenor Pakistan was also all set to buy a big ratio of shares in Tameer Bank. Meanwhile, FINCA and Apna Microfinance Bank also proactively worked together with 38 MFIs and set lending limit for individuals at Rs. 150,000 and for MSMEs at Rs. 500,000.

Prime Minister's Youth Business Loan Scheme is one of the initiative of the government to promote the micro finance in Pakistan, “promotion of micro finance schemes is to attract the youth entrepreneurs for establishing their own businesses” Prime Minister’s Youth Program (PMYP).

The microfinance sector has a huge potential of growth in Pakistan. Pakistan Microfinance Network has estimated that there are around 27 million clients while all the MFIs put together serve only about 13.71% of this market only (PMN, 2015). Apparently to tap this market, a number of commercial banks, including Allied Bank, National Bank, Bank of Khyber and Bank of Punjab, have entered into MSME financing, in spite of the fact that commercial banks do not tend to deal in small loans. Here, it is needed that banks develop proper understanding of the dynamic of microfinance, which will include culture to open up of special windows. Even if a small portion, 10%, of the banks’ portfolio, is disbursed in micro financing, it may have a significant effect on Pakistan’s economy and result in providing millions of employments as well as creating a culture of entrepreneurial development and wealth generation.

RESEARCH OBJECTIVE

The main objective is to carry out this research on the effectiveness and efficiency of Microfinance on the economic development. Microfinance seems to be one of the most effective solutions to augment economic activities on micro level. It can help to improve their income of core lower class of the society. It can help them establish their own business and decrease their vulnerability. People with low income do not have access to formal financial institutions, are the main clients of microfinance, hence Microfinance can also be considered to be an important tool for poverty reduction, improvement of living standard, reduction in socio-economic problems and contribution towards economic growth and development in Pakistan.

- i. To know the perception about microfinance that it can become a very handy tool for economic uplift, growth and development in Pakistan.
- ii. To evaluate the role of microfinance in economic development.

METHODOLOGY

The first part comprises of a survey which was held in the form of a methodically developed questionnaire. It was designed with the view that the researcher was able to collect precise, accurate and relevant information from the respondents. The questionnaire had a range of close-ended questions each requiring responses on a liker scale of 1 to 5, with 1 showing strong disagreement to 5 showing strong agreement to the question. Additional space for comments was also given for the respondents. A total of 350 filled questionnaires were collected.

Due to time limitations, the researcher applied cluster sampling. This sampling method was deemed as most suited given the varying nature of microfinance institutions, geographical dispersions, and costs involved to reach clients, especially in cases where they happened to reside in exceedingly distant or suburb areas. A plausible way to group or cluster the clients was through geographical divisions, wherein each sampling cluster represents one area.

ANALYSIS AND DISCUSSION

The analysis of the study was based on primary data set collected by a sample survey which was similar to or the representative of population. The analysis focuses the objective of the study and the study attempts to explain the following hypotheses.

HYPOTHESIS

There was a significant positive impact of provision of microfinance facility on the Economic Development in Pakistan.

This set of questions discussed the potential challenges to Microfinance sector in Pakistan in order to promote economic development. The section contains the responses related to microfinance and economic stability in Pakistan according to the understanding and perception of respondents. It is based on nine different questions concerned to the issue of economic stability with the provision of microfinance loans to the poor and core poor class.

Tables 1. Descriptive Statistics

	<i>Statement</i>	<i>N</i>	<i>Mean</i>	<i>Std. Deviation</i>
1	MF provides opportunities for improving the standard of living of the family	350	3.62	1.092
2	Family enjoys higher self-esteem / social status after commencing or expanding business through MF schemes	350	3.60	1.007
3	MF schemes may reduce crime levels by providing opportunities for earnings through establishing micro entrepreneurship	350	3.92	1.014
4	MF provides opportunity for better education facility to the children through enhanced economic position of the family	350	3.88	.953
5	MF enables the family to have more access to healthcare facility	350	3.61	.971
6	MF helps in reducing poverty level by raising income level	350	3.96	.903
7	The roots of MF enhance outreach to alleviate poverty for a foundation of economic development of country	350	3.68	.978
8	MF supports and stabilizes the economy of country through more employment opportunities	350	3.93	.929
9	Efficient MF schemes provide opportunity for economic growth and prosperity of the country	350	3.97	.956
	Valid N (list wise)	350		

Tables 1 shows the result of descriptive statistics on the question asked above. The answer is scaled between 1 to 5 values.

1. Microfinance provides opportunities for improving the standard of living of the family has a mean 3.62 and standard deviation of 1.092.
2. Family enjoys higher self-esteem / social status after commencing or expanding business through Microfinance schemes has a mean of 3.60 and standard deviation of 1.007.
3. Microfinance schemes may reduce crime levels by providing opportunities for earnings through establishing micro entrepreneurship has a mean 3.92 and standard deviation of 1.014.
4. Microfinance provides opportunity for better education facility to the children through enhanced economic position of the family has a mean 3.88 and standard deviation of .953.
5. Microfinance enables the family to have more access to healthcare facility has a mean 2.61 and standard deviation of .971.

6. Microfinance helps in reducing poverty level by raising income level has a mean 3.96 and standard deviation of .903.
7. The roots of MF enhance outreach to alleviate poverty for a foundation of economic development of country has a mean 3.68 and standard deviation of .978.
8. Microfinance supports and stabilizes the economy of country through more employment opportunities has a mean 3.93 and standard deviation of .929.
9. Efficient microfinance schemes provide opportunity for economic growth and prosperity of the country has a mean 3.97 and standard deviation of .956

The values of mean and standard deviation on the questions provides the basis to approve and accept the third hypothesis on the analysis and confirms that there is a significant positive impact of provision of microfinance facility on the Economic Development in Pakistan.

CONCLUSION AND RECOMMENDATIONS

Pakistan holds a population of more or less 192 million which subsumes a larger portion with rural population, of nearly two third parts. Due to an elevated rate of poverty, the requirement of microfinance becomes higher as compared to other countries. Pakistan is considered as one of most unequal region for income distribution in the world. According to the World Bank, in 2013, nearly 29.5% of total population comes under the line of poverty, while approximately 7 percent in the total poor population are ultra poor in Pakistan. Conditions of the poor is getting worst day by day as a result of increasing rate of illiteracy, worse physical infrastructure and poor health facilities.

The accessibility to finance is much limited to poor, In order to facilitate poor people in such circumstances, the requirement for microfinance increases vitally. If microfinance sector is provided with full support of Government, it can improve living standards of people, enhanced status in society, education, better health care, and reduction in crime rate, minimization of socio economic problems, raising income level, generating employment and supporting economy of country. . It will also reduce poverty by producing new entrepreneurs and as a result of it generating the opportunities for employment in Pakistan.

The network of Microfinance Institutions should be expended as there is huge potential available in the market. Internationally recognized Microfinance Providers (MFPs) should also be offered incentives for commencing their operations in Pakistan in order to get advantage from their experiences.

If Microfinance loans are invested with proper guidance, it can bring multiplier effect on the country's economy. Therefore, aggregate macroeconomic results can be achieved through micro level actions of the individuals; hence, they should be motivated towards small investment activities.

Islamic Banking being Interest free be made popular for the satisfaction of religious beliefs. Islamic banking offers Asset based Lending which increases the assets of clients and thus a reason to increase income and stability in business activities. This methodology of Islamic lending is an exceptional technique to create employment by means of establishing new micro businesses and to revitalize existing ones and thus a way to aid economic development and its sustainability.

Special dedicated funds should be allocated in the budget each year by the Federal and Provincial Government, either interest free or on subsidized interest rates, for core poor people to be provided with microfinance loans to earn their bread and butter.

Finance Ministry of Pakistan, State Bank of Pakistan, Commercial Banks and Microfinance Banks should formulate friendly and accommodating policy which can augment the outreach of microfinance to a remarkable point so as to contribute in the economy of Pakistan. There should be steps taken to increase the accessibility of microfinance on public as well as private sector.

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APPENDIX

Tables of Responses

Table 1.1: MF provides opportunities for improving the standard of living of the family

		<i>Frequency</i>	<i>Percent</i>	<i>Valid Percent</i>	<i>Cumulative Percent</i>
<i>Valid</i>	<i>Strongly Disagree</i>	19	5.4	5.4	5.4
	<i>Disagree</i>	41	11.6	11.7	17.1
	<i>Neutral</i>	63	17.8	18.0	35.1
	<i>Agree</i>	158	44.8	45.1	80.3
	<i>Strongly Agree</i>	69	19.5	19.7	100.0
	<i>Total</i>	350	99.2	100.0	
<i>Missing</i>	<i>System</i>	3	.8		
	<i>Total</i>	353	100.0		

Table 1.2: Family enjoys higher self-esteem / social status after commencing or expanding business through MF schemes

		<i>Frequency</i>	<i>Percent</i>	<i>Valid Percent</i>	<i>Cumulative Percent</i>
<i>Valid</i>	<i>Strongly Disagree</i>	13	3.7	3.7	3.7
	<i>Disagree</i>	40	11.3	11.4	15.1
	<i>Neutral</i>	78	22.1	22.3	37.4
	<i>Agree</i>	163	46.2	46.6	84.0
	<i>Strongly Agree</i>	56	15.9	16.0	100.0
	<i>Total</i>	350	99.2	100.0	
<i>Missing</i>	<i>System</i>	3	.8		
	<i>Total</i>	353	100.0		

Table 1.3: MF schemes may reduce crime levels by providing opportunities for earnings through establishing micro entrepreneurships

		<i>Frequency</i>	<i>Percent</i>	<i>Valid Percent</i>	<i>Cumulative Percent</i>
<i>Valid</i>	<i>Strongly Disagree</i>	13	3.7	3.7	3.7
	<i>Disagree</i>	16	4.5	4.6	8.3
	<i>Neutral</i>	69	19.5	19.7	28.0
	<i>Agree</i>	141	39.9	40.3	68.3
	<i>Strongly Agree</i>	111	31.4	31.7	100.0
	<i>Total</i>	350	99.2	100.0	
<i>Missing</i>	<i>System</i>	3	.8		
	<i>Total</i>	353	100.0		

Table 1.4: MF provides opportunity for better education facility to the children through enhanced economic position of the family

		<i>Frequency</i>	<i>Percent</i>	<i>Valid Percent</i>	<i>Cumulative Percent</i>
<i>Valid</i>	<i>Strongly Disagree</i>	5	1.4	1.4	1.4
	<i>Disagree</i>	31	8.8	8.9	10.3
	<i>Neutral</i>	59	16.7	16.9	27.1
	<i>Agree</i>	161	45.6	46.0	73.1
	<i>Strongly Agree</i>	94	26.6	26.9	100.0
	<i>Total</i>	350	99.2	100.0	
<i>Missing</i>	<i>System</i>	3	.8		
	<i>Total</i>	353	100.0		

Table 1.5: MF enables the family to have more access to healthcare facility

		<i>Frequency</i>	<i>Percent</i>	<i>Valid Percent</i>	<i>Cumulative Percent</i>
<i>Valid</i>	<i>Strongly Disagree</i>	9	2.5	2.6	2.6
	<i>Disagree</i>	37	10.5	10.6	13.1
	<i>Neutral</i>	95	26.9	27.1	40.3
	<i>Agree</i>	150	42.5	42.9	83.1
	<i>Strongly Agree</i>	59	16.7	16.9	100.0
	<i>Total</i>	350	99.2	100.0	
<i>Missing</i>	<i>System</i>	3	.8		
	<i>Total</i>	353	100.0		

Table 1.6: MF helps in reducing poverty level by raising income level

		<i>Frequency</i>	<i>Percent</i>	<i>Valid Percent</i>	<i>Cumulative Percent</i>
<i>Valid</i>	<i>Strongly Disagree</i>	7	2.0	2.0	2.0
	<i>Disagree</i>	20	5.7	5.7	7.7
	<i>Neutral</i>	48	13.6	13.7	21.4
	<i>Agree</i>	181	51.3	51.7	73.1
	<i>Strongly Agree</i>	94	26.6	26.9	100.0
	<i>Total</i>	350	99.2	100.0	
<i>Missing</i>	<i>System</i>	3	.8		
	<i>Total</i>	353	100.0		

Table 1.7: The roots of MF enhances outreach to alleviate poverty for a foundation of economic development of country

		<i>Frequency</i>	<i>Percent</i>	<i>Valid Percent</i>	<i>Cumulative Percent</i>
<i>Valid</i>	<i>Strongly Disagree</i>	8	2.3	2.3	2.3
	<i>Disagree</i>	34	9.6	9.7	12.0
	<i>Neutral</i>	90	25.5	25.7	37.7
	<i>Agree</i>	147	41.6	42.0	79.7
	<i>Strongly Agree</i>	71	20.1	20.3	100.0
	<i>Total</i>	350	99.2	100.0	
<i>Missing</i>	<i>System</i>	3	.8		
	<i>Total</i>	353	100.0		

Table 1.8: MF supports and stabilizes the economy of country through more employment opportunities

		<i>Frequency</i>	<i>Percent</i>	<i>Valid Percent</i>	<i>Cumulative Percent</i>
<i>Valid</i>	<i>Strongly Disagree</i>	7	2.0	2.0	2.0
	<i>Disagree</i>	23	6.5	6.6	8.6
	<i>Neutral</i>	52	14.7	14.9	23.4
	<i>Agree</i>	172	48.7	49.1	72.6
	<i>Strongly Agree</i>	96	27.2	27.4	100.0
	<i>Total</i>	350	99.2	100.0	
<i>Missing</i>	<i>System</i>	3	.8		
	<i>Total</i>	353	100.0		

Table 1.9: Efficient MF schemes provide opportunity for economic growth and prosperity of the country

		<i>Frequency</i>	<i>Percent</i>	<i>Valid Percent</i>	<i>Cumulative Percent</i>
<i>Valid</i>	<i>Strongly Disagree</i>	8	2.3	2.3	2.3
	<i>Disagree</i>	19	5.4	5.4	7.7
	<i>Neutral</i>	59	16.7	16.9	24.6
	<i>Agree</i>	152	43.1	43.4	68.0
	<i>Strongly Agree</i>	112	31.7	32.0	100.0
	<i>Total</i>	350	99.2	100.0	
<i>Missing</i>	<i>System</i>	3	.8		
	<i>Total</i>	353	100.0		