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Effectiveness of Microfinance Loans in Pakistan (A Borrower Perspective)

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Abstract - Purpose: The purpose of this paper is to examine the effectiveness of microfinance loans in Pakistan. The purpose is that how much the microfinance loans are effective in Pakistan from the borrower perspective. The loan which is took by the client of Micro Finance Tamer Bank how that loan amount has been used in the projected business and whether the income has been increased by the loans utilization.

Research methodology: The purpose is to find different factors which are affecting the effectiveness of the microfinance loans. Three variables have been identified to examine the effectiveness of the loans that are procedure, loan consumption and income. To study these factors a logically questionnaire has been developed by the researcher herself and floated to the Microfinance Timer Bank borrowers and the data is analyzed by the regression analysis.

Keywords : *microfinance, effectiveness, loans consumption.*

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EFFECTIVENESSOFMICROFINANCELOANSINPAKISTANABORROWERPERSPECTIVE

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Effectiveness of Microfinance Loans in Pakistan (A Borrower Perspective)

Beenish Ameer [α] & Dr. Moazzam Jamil [σ]

Abstract - Purpose: The purpose of this paper is to examine the effectiveness of microfinance loans in Pakistan. The purpose is that how much the microfinance loans are effective in Pakistan from the borrower perspective. The loan which is took by the client of Micro Finance Tamer Bank how that loan amount has been used in the projected business and whether the income has been increased by the loans utilization.

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Findings: Data findings are procedure is affecting the loan consumption but income does not depend on the consumption of the loans.

Conclusion: Microfinance institution should extend its reach by providing information and should consider the core to make the microfinance loans more effective as it for the low income households.

Keywords : microfinance, effectiveness, loans consumption.

I. Introduction

"Microfinance" is very much defined as financial services for poor and low-income clients offered by different types of service providers. In practice, the term is often used more narrowly to refer to loans and other services from providers that identify themselves as "microfinance institutions" (MFIs).Microfinance is usually understood to entail the provision of financial services to micro-entrepreneurs and small businesses, which lack access to banking and related services due to the high transaction costs associated with serving these client categories. The two main mechanisms for the delivery of financial services to such clients are (1) relationship-based banking for individual entrepreneurs and small businesses; and (2) group-based models, where several entrepreneurs come together to apply for loans and other services as a group.

No doubt, microfinance is very powerful tool to alleviate the poverty and empowerment to women and poor populations. There are numerous NGO's, MFI's, MFB's and other welfare trusts that are operational for the poverty alleviation and they are annoying to attain their goals and assignments. State Bank of Pakistan (SBP), Pakistan Microfinance Network (PMN), Pakistan Poverty Alleviation Fund (PPAF) and other frames are also working for attaining the Millennium Development Goals (MDG's) and contributing for the economic development of the nation. Microfinance in Pakistan is in its very early stage. There is 33% to 35% population living below the poverty line in Pakistan. It means one third of the population of 150 Million people of Pakistan is below the poverty line. These statistics shows situation of the society is very unpleasant. There are number of organizations like Kasha Foundation and Kasha Microfinance Bank, Tamer Microfinance bank, Akhuwat, First Microfinance Bank, Khushhali Bank etc working with the government of Pakistan to reduce it doing their efforts to increase their outreach.

Presently, there are three different models of microfinance services in Pakistan, i.e.6 Micro Finance Banks (MFBs), 10 Micro Finance Institutions (MFIs) and 4 Rural Support Programmers (RSPs), all the three models started with small size short term group lending policy of working capital loans.

Some MFIs and MFBs like Tamer Bank and FMFB have diversified into individual based large loans relative to market average loan size. However, RSPs provide multi product microfinance services including infrastructure development projects like health, education, insurance, mobilization of savings and primarily operate in rural areas.

Besides the three main groups of microfinance other institutions that also provide microfinance services include, commercial banks and government owned institutions etc. Although the main product of these institutions is not microfinance, the government-owned institutions that provide microfinance services to the poor include: micro credit and saving services and subsidized credit for government's Rodger Scheme by National Bank of Pakistan (NBP); credit and saving services by ZTBL; special microfinance services by government owned First Women's Bank, Bank of Khyber, SME Bank, financial savings and money transfer services provided through countrywide network of 7,500 branches of Pak Post Saving Banks, the seven National Saving Schemes (NSS) of Central Directorate of National Savings (CDNS) which accept deposits of about 4 million account holders and the Zakat office that provide charity funds as a social objective. Some

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commercial financial institutions including ORIX leasing also extend microfinance services to their poor customers (CLEAR, 2007).

This research will be used to examine the effectiveness of microfinance loans in Pakistan. The loan which is took by the client of Micro Finance Bank how that loan amount has been used in the projected business and whether the income has been increased by the loans utilization. To investigate the current issues linked with microfinance loans. To find out the areas this can be addressed to improve the microfinance loans.

a) Significance of Study

Despite the importance of micro finance in Pakistan no study is conducted on current issues linked with microfinance loans. The central objective of the study has been to discover the hidden realities related to effectiveness of microfinance loans in Pakistan (borrower perspective). This research is an important advancement in literature of factors affecting on micro finance loan. Microfinance, with the core objective of provisioning of financial services to the pool segments of the society, contributes its role in the form of financial development with primarily focus on poverty alleviation. Most of the people perceive microfinance in narrow sense that it is about micro-credit but for poor people but it has broader extent including, micro-insurance, transactional services and most important are the savings.

b) Literature Review

Raff and Mahmud (2009) examined the Growth and performance of microfinance. The study was conducted in Pakistan for the period of 2004-2007. The considerable variables were subsidized fund, recruitment of new fund, external support, opening of new branches and outreach (to other aspects of outreach). The results told that that sector should more focus on accessible human resources and targets can simply be achieved by adopting an intensive growth strategy. Kondo (2007) conducted research on the impact of microfinance on rural households in the Philippines (A Case Study from the Special Evaluation Study on the Effects of Microfinance Operations on Poor Rural Households and the Status of Women). The variables determined were interest, consumption and per capita income. The findings of this research showed that microfinance loans were shown positive to the per capita income, it also increased the consumption capability and improved saving ability and microfinance can also be proved as an effective poverty alleviation tool. Deventer and Huybrechts (2005) studied the impact of microcredit on the poor in Bangladesh. Income, poverty alleviation and consumption were used as dependent variables and family support as intermediate variable. The findings of this research showed as microfinance institutions have positive role on income, consumption, poverty reduction and having positive influence on female members and their positive influence could be seen through their decision making role, expanding knowledge and awareness. Bi and Panda (2011) studied on the Comparison of performance of microfinance institutions with comercial banks in India. Poverty alleviation, empowerment of women was used as variables. The findings were that microfinance institutions were reporting an impressive growth and India had the largest number of households that were not included in banking system. The results of this research show that microfinance loans were proved as economic tool to alleviate poverty and empowerment of women.

Jagged et al (2011) studied Impact of microfinance on poverty alleviation in Nigeria: An empirical investigation. The study was conducted in Nigeria, poverty was taken as dependent variable and microfinance loans were taken as independent variable. The findings were that there was a significant difference between those persons who used microfinance loans and those who didn't use them. The paper concluded that MFI having significant impact in reducing poverty by increasing income and microfinance could be proved as the more powerful source if program started on depth and outreach than the present outreach. Akram and Husain (2011) studied on the role of microfinance in uplifting income level: A study of District Okara – Pakistan. Microfinance was taken as independent variable and income was determined as dependent variable. The conclusion was that microfinance was proficiently serving the poor by increasing their income level. Mostly respondents conclude that their income level increase after getting microfinance loan and improving their living standard. Charles, James and Hammed (2011) examined the Impact of microfinance on poverty alleviation in Nigeria. Two variables were used, poverty as dependent and microfinance as independent variable. The result findings revealed that there was a vital effect of MFI in reducing poverty by rising income. It also concluded that microfinance institutions having powerful strategy of poverty reduction. However, microfinance can be more effective tool if work is done on outreach. Shiraz and Khan (2009) examined the Role of Pakistan poverty alleviation fund's microcredit in poverty alleviation. Poverty alleviation was taken as variable. The study was conducted in 2005. The paper concluded that microcredit has reduced poverty and loan taking clients had been converted to higher income groups and there was a positive impact of microcredit program on poverty of the country.

Swope (2010) studied microfinance and poverty alleviation. The study was conducted for the period of 2005. The study showed the conclusion that the microfinance loans may be the source of increasing income and poverty alleviation. The outreach problem can be solved by village banks that microfinance institutions reached the poor by implementing integrated

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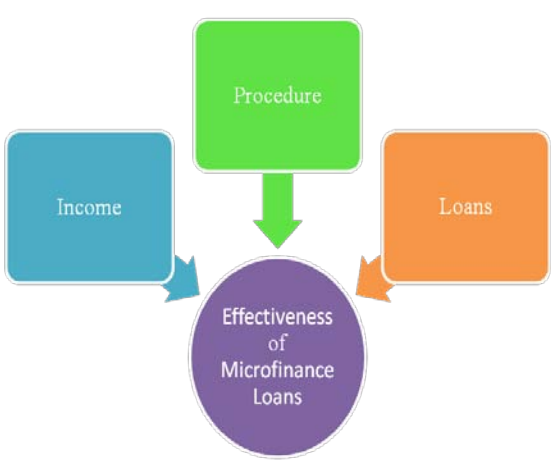
programs. MFI allowed women to be independent and entered in society as more confident and skilled. Jagged et al (2011) conducted research on Influence of loan disbursement by microfinance and non microfinance institutions on poverty alleviation in Nigeria. Data was collected to determine the relationship between microfinance as an independent variable and poverty as a dependent variable. The research concluded that MFI were the effective tool in reducing poverty by increasing the income level thus people economic capability increased and brought sustainable development. Onwumere, Ibex and Guam (2012) studied the impact of micro-credit on poverty alleviation and human capital development: Evidence from Nigeria from 1999-2008. Microfinance was taken as the independent variable while poverty alleviation was treated as dependent variable. The OLS regression technique was used in this study. The study concluded that microfinance banks increased micro financing activities ultimately did not increase the human capital development however microfinance provided support in eradicating poverty. Thus the experience of Nigeria could be effective for other developing countries.

Mawa (2008) studied the impact of micro-finance toward achieving poverty alleviation.

Poverty alleviation, women empowerments were taken as variable and poverty could be reduced by increased in income. The conclusion drawn from the study that financing on women were more poorer than men and especially in rural areas, microfinance could be the source of reducing poverty and this research suggested that MFI focused on needs of more diversified groups and targeted the most poor. Bakhtaran (2006) studied that Microfinance and poverty reduction: Some international evidence consumption, poverty reduction were used as variables. This paper argued that reducing of poverty alleviation could be done through microfinance loans and by providing access to poor might smooth their Consumption.

II. Theoretical Framework



a) Dependent Independent Variables

The past studies find three factors which can affect the effectiveness of microfinance loans which are procedure, loan consumption and income. Microfinance loan efficiency depends on above three variables. We take microfinance loans as dependent variable while income, procedure and loan consumption as an independent variable.

III. Research Objectives

The research objectives are as follows:

a) Main Objective

The main objective of this study is to examine the factors affecting the effectiveness of microfinance loans (borrower perspective).

b) Sub Objectives

The sub objectives include:

- To investigate the current issues linked with microfinance loans.
- To find out the areas this can be addressed to improve the microfinance loans.
- To study the effectiveness of microfinance loans.
- To make recommendations for improvements in existing lending procedure microfinance loans, if required.

c) Research Questions

In order to determine to determine the effectiveness of microfinance loans. a model was adopted and based on that model, the following questions must be addressed.

- What are the factors which directly or indirectly affect effectiveness microfinance loans?
- Which factors can be changed to achieve success in microfinance loans?

IV. Research Design/Methodology

a) Data Collection/Population

This research is empirical in nature and it is conducted through questionnaires. This study measures the effectiveness of the microfinance loans has been measured towards the clients of the Timer Microfinance Bank in the city Gujarat which is the city of Punjab province. It will be answered with the help of a questionnaire in which all the important variables are included. Since the study is related to the effectiveness of microfinance loans of the consumer so the targeted population in order to collect the data, is the clients of Microfinance Tamer Bank. For the collection of error free data the respondents were asked to fill the questionnaire with complete sincerity & honesty, & not leave any part of the questionnaire unanswered. For the ease of respondents the questionnaire was personally administered where the respondents completed the questionnaire. Using personally administered questionnaires has different advantages such as it reduces the biasness of

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the respondent, it is reasonably brief & economical & lastly it allows the respondent to give an open response.

b) Sampling

Random sampling technique is adopted in which 40 clients were chosen and participated in the research. The main target population was the individual clients who have taken the loan from the bank in which both males and females are included. In order to collect data, the borrowers from the bank were asked to cooperate by filling the questionnaire. Their answers for the questions reflect different characteristics of the consumers towards the effectiveness of the micro-finance loans which is the focal point of the study. The loan borrowers were chosen on the basis of convenience sampling method. The reason for so was because of the scattered & huge population, restricted time & limited budget since it would be quite difficult to study all the branches of Microfinance Timer Bank in such a limited time & with limited resources. A sample of 40 clients was taken for the test and the respondents were approached individually. A total of 62 questionnaires were distributed, out of which 22 questionnaires were filled either improper or were incomplete. Rests of 40 questionnaires were useable.

c) Research Instrument

A logical questionnaire is used for data collection. The research instrument is developed by the researchers themselves. The questionnaire has three variables each variable has its separate questions which are used to record individual response. The first variable which has the three questions is about the procedure of getting the loan and repayment to the bank this part of the questionnaire asks the respondent for their measure on the procedure, in second variable is about the loan it has five questions in which the respondent is asked to the size of the loans and its consumption on the projected business, in the last variable which is about the Income in this there is three questions in it which ask the respondents to give its response whether after using the loan the their income increased or decreased. This questionnaire is not basically on the liker scale. For our ease and for the data analysis we have converted into the liker scale with the dummy questionnaire in this we use the scale of 5 in which 1 show the highest value and 5 show the lowest value.

V. Data Analysis & Findings

Data analyzed by using software, SPSS version 16 by applying following techniques: Cranach's alpha and Regression analysis.

a) Reliability of Variables

Reliability means consistency. It is the degree to which an instrument will give similar results for the same individuals or variables at different times. Reliability can take on values of 0 to 1.0, inclusive. The reliability of variables and their Cranach's are provided in given table.

Table 1 : Reliability Result

Variable	No. of Items Alpha	Cronbach's
Procedure	3	.763
Loans	5	.671
Income	3	.724

b) Regression Analysis

Regression analysis of the variables has been made to check that variables are dependent on each other. At first the two equations has been made

Micro Finance Loan= f (procedure) (1)

Microfinance loan variable take as a dependent variable and the procedure is taken as independent variable. We want to see that how much loan consumption is dependent on the procedure.

ß	t	sig
4.60	3.148	.003

The fact shows that data is significant and Beta is positive it means procedure is significantly affecting the loan consumption. It also justifies as we are expecting if the procedure is good the loan consumption in the projected business will be high. Now, the result which has been analyzed in the equation 1 we will put this data into another equation called equation 2. This equation tells us that how much the income dependent on the consumption of the loan.

Income = f (microfinance loan) (2)

ß	t	sig
-.179	-1.105	.276

The result shows that although the Beta is negative but it is insignificantly affecting the results. It means income does not dependent on the loan consumption it can be increased or decreased by other factors.

VI. Conclusion

The results show that income does not dependent on the loan consumption. There are lot other variables that should be considered when measuring the impact of the income on the households and the SME because the history of the microfinance loaning in Pakistan consists of almost ten years. So, it is not necessary that income is only increased by the loan consumption. It can be increased by the running business also. Secondly, the microfinance should extend its reach to cover the core poor. Most of the people do not know about the procedure of getting the loans from the microfinance institution. They should

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provide more information to the people to aware them about the microfinance schemes. The most important thing is the microfinance institution should provide some training to the lay man so that they must be able to use the loan in more efficient manner. Micro financing institution should consider the core poor the poor is not only which hasn't any rupee but also that one who hasn't any type of training or asset.

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