

Challenges and Opportunities to Microfinance Institutions in Khyber Pakhtunkhwa Province, Pakistan

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Abstract

This study explored the challenges and opportunities faced by microfinance institutions in Khyber Pakhtunkhwa province of Pakistan. For a developing country like Pakistan, the development of its microfinance sector is a step towards its sustainable development. This study identified various challenges face by the microfinance sectors, which includes social challenges, political instability, terrorism, low literacy rate, procedures and documentations, terms and conditions etc. There are also potential growth opportunities for this sector which includes poverty alleviation, economic development, Islamic financing and entrepreneurship. The development of this sector will further stimulate the economic development of the economy.

Keywords: Microfinance, Khyber Pakhtunkhwa, Pakistan, Challenges, Opportunities.

1. Introduction

The spirit of microfinance is to support those low income individuals and household for acquisition of funds for their small enterprises and business which can provide a self-employment and employer opportunity for the community. This source of financing is basically designed for the individuals who have lack of access to traditional banking system however; having some creative business ideas. This source of financing is very beneficial for weakening the difference between have's and have's not. As we are living in a world of having high rate of difference, those who have a lot of opportunities to nab because of their access to large sum of money, but on the other hand we have a bulk of population who are suffering from the scarcity of funds. Therefore microfinance shakes the existing gap and provides equal opportunity for those who don't have a free access to these funds.

The basic spirit of microfinance is to empower the poor community. This system of financing is to transcend the social status of the impoverished population, who can't benefit from their creativity through lack of resources. To up limit the social system, it contributes in material and nonmaterial aspects. Microfinance has helped in poverty reduction.

This sector has a positive impact on the community in terms of business opportunities beside this; it has some barriers which discourages this field and has negative consequences and impact. We have to know that why this field is not too much encouraging in Pakistan as compare to other emerging countries. The business community is not encouraging toward this sector instead of having multi opportunities in Pakistan and especially in Khyber Pakhtunkhwa and what are the socio cultural impact and unawareness of our community toward this sector in Pakistan and what policies should be adopted by financial institutions for the encouragements of this field and sector.

1.1. History of Microfinance in Pakistan

Microfinance has a very important position in any country economy. Microfinance existence came into being to give helping hand to needy and deprived people of the population, who don't have a free access to commercial banking sector. To improve the financial health of the community, this sector is being flourishing in a very rapid speed. This sector has the capability to reduce poverty and improve employment rate. Many countries have adopted microfinance to increase their social status in the comity of nation and in which Bangladesh came as an innovator followed by many underdeveloped countries like India, Malaysia and Pakistan.

In Pakistan, microfinance was only available for the agriculture sector till 1960's. In 1970's as major banks were nationalized and this responsibility was assigned to the newly opened Agriculture Development Bank of Pakistan, however this bank still focus on agriculture sector. With the passage of time many non-governmental organization stepped up in this sector. This was the era when Agha Khan Rural Support Program (AGRSP) start function in the Northern region of the NWFP now Khyber Pakhtunkhwa. The AGRSP spread into many other parts and starts its working very effectively, this start working through Pakistan in the shape of many microfinance programs like Sarhad Rural Support Program (SRSP), Punjab Rural Support Program (PRSP) and National Rural Support Program (NRSP). Many other programs including Poverty Alleviation Program were started by teses. Now microfinance in Pakistan has been exercised by many institutions viz. Khyber Bank, Khushali Bank, Kashf Microfinance Bank etc.

The poverty rate is still high in Pakistan. To eradicate poverty which itself is a difficult task and requires a lot of supplementary steps. The specialized institutions to pacify poverty are required to focus on two main issues. The issues can be classified into two segments universally and narrowly. The universally mentions includes health and education for the whole community, while narrowly are focused to give benefit to only the deprived community. Being focused on poor people, we should classify them in different classes which include the following.

- Landless households
- Small landowners and Sharecroppers
- In Rural construction industry having low wages
- Female headed households

The current situation of microfinance in Pakistan has some strong and weak points. In Pakistan, about 60 million people live below the poverty line which gives a very bad signal of Pakistan economic health. Pakistan has almost half of adult population which is a very good niche market for the microfinance institutions to exploit. The country like Pakistan requires many steps to tackle the issues of gender discrimination, poverty, and unemployment and the panacea for this is the spread of microfinance in our country.

A Chinese thinker quotes that “A journey of thousand miles begins with one step” and we think microfinance is one of the step towards a prosperous Pakistan. To support the micro financing, an ordinance named microfinance ordinance 2001 was passed. Many institutions like MFI, Ngo’s and commercial Banks in Pakistan are struggling to pacify poverty and reduce unemployment rate. The government of United Kingdom is struggling hard to uplift the social status of the under developed country like Pakistan through various development programs. UK aid has benefitted 1.23 million including only 60% of women. This will be distributed in the individuals to mount of their small business and entrepreneurial skill. The various programs were launched firstly, which has given 103000 loans to poor women in 2010-2012, which helped 1.23 million people for their small businesses.

In undeveloped country like Pakistan, the people are facing a lot of crisis at the same time. The ever increasing inflation is also among the main issue for the poor population because due to less economic activity and continues business failures. The country is also facing a huge threat of security in which a large portion is under the control of army and continues skirmishes takes place between security forces and culprits. The function of the microfinance institutions is uneven in the different province of Pakistan. There are few microfinance institutions that are functioning in KPK and Baluchistan province, while the situations in Punjab and Sind province are satisfactory. The main reason of not having much market in the former is of security issue. The other issue which is also worthy of notice is that microfinance institutions only operates in urban areas not paying much heed to rural population.

The religion factor can’t be ignored in any society. If we see microfinance as an emerging sector in our society, the answer is in negative because those institutions which are exercising microfinance is on the hit list of our religious institutions. The religious institutions called them the institutions which are cursed by God due to Riba (interest). The microfinance institutions needs to be in harmony with our society and make their institutions interest free. The KPK government has taken a very welcoming step establishing an Islamic Microfinance Bank on May 2014.

Several programs have been launched by different institutions in KPK for the development of this sector. The first program launched was Bacha Khan Poverty Alleviation Program initiated in four different districts with annual budget of Rs. 501 million. The Bacha Khan Scheme is converted into Wasil-e-Haq Rozgar Scheme and is operating effectively in the terrorism stricken society of KPK. The amount needed to establish a microfinance bank is Rs. 1000 million in Pakistan. The Pakistan Poverty Alleviation Fund has given Rs.14 billion to this sector.

The government’s policies and program is to alleviate poverty during the Musharraf regime where most of the inhabitant were victim of terrorism, microfinance was selected as the key objective to control poverty and a tool for the victim of terrorist compensations. This motive of the government resulted in the establishment of Pakistan Poverty Alleviation Fund (PPAF) in 2000 in coordination with World Bank, while establishing a microfinance bank namely Khushali Bank simultaneously. Microfinance institutions have extended their product and services portfolios by identifying and exploring new areas as a niche markets, which deliver enterprise and business loans, housing and auto finance, personal loans and deposits, leasing, insurance and remittance services. Tremendous and huge developments have been made in the microfinance sector. Government initiatives deserve greater appreciation and credit which caused number of clients to increase from just 100,000 in 2001 to 1.4 million in 2007 (Khushahali Bank Annual Report 2007 – Page No. 4).

1.2 Key principals of microfinance

The following are the key principles of microfinance

- Low income individuals and poor people needs a portfolio of services which is even more than

advancing loans by financial institutions to the individuals and households.

- Micro Finance is a useful tool and practice to empower poor's through financing.
- Micro Finance sector can be exploited by encouraging financial institutions in our community.
- The key bottleneck is the shortage of strong financial institutions, managers, and their practice.
- This sector will be encouraged when we encourage social responsibilities, social awareness and participation of religious scholars in this field.
- Interest rate making it harder for poor people to get loans for the financial institutions.

This study aims to explore the challenges and opportunities to microfinance sector in Khyber Pakhtunkhwa (KPK) province of Pakistan. This study will explore the current situation of microfinance in KPK. This study will provide information about the challenges to the microfinance sector. The opportunities will be explored for the sector, which may boost this sector through various initiatives. Furthermore, this study will discuss the benefits that will be received by the community from the development of this sector.

The rest of the study is organized as follows. The second section discusses the methodology. The third section presents challenges faced by microfinance sector. The fourth section discusses the opportunities. The fifth section concludes.

2. Methodology

In this study, we designed questionnaire to identify the opportunities and challenges faced by the Khyber Pakhtunkhwa province Pakistan. The data was collected from the respondents having specialized knowledge in the microfinance sector. The information was collected mostly from the government employees, who were working in the microfinance sector.

3. Challenges faced by Microfinance sector

The following are the challenges faced by the microfinance sector in Khyber Pakhtunkhwa province.

3.1 Social challenges and people perceptions towards the sector

According to the respondents, the social factor is a big challenge for the microfinance sector in KPK. One of the important factors includes religion beliefs. The interest bearing transactions are prohibited in Islam and therefore interest bearing financing is a big challenge to the microfinance sector in KPK. Most of the people are Muslims in KPK and therefore they avoid such kind of transactions.

3.2. Political Instability

The political instability is also a big problem for microfinance sector in KPK. The government focus on this sector is not so much satisfactory. According to the respondents, the changing governments also influence the sector. The political parties only support short term aids for their political goodwill.

3.3. Terrorism

The terrorism is also a big challenge not even for the country but also for the microfinance sector as well. The KPK province is facing the severe problem of terrorism and also the microfinance sector is facing the same for its development. The low law and order situation is a big hurdle for the development of this sector.

3.4. Low literacy rate

The low level of education is also a big problem for this sector. The low borrowing in this sector is due to low level of education of the people. In KPK, mostly microfinance sector are devoted to give loans to farmers. The low level of knowledge of farmers discourages them in borrowing loans from this sector.

3.5. Procedures and documentation

One of the reasons that have slow down the speed of loans advancement from the microfinance institutions to the borrowers is the procedures and large set of documentation in borrowing of loans. It takes more time and involves many procedures in taking the loan from the institutes, which has slow down the process of borrowing loans.

3.6. Terms and conditions of loan

The respondent suggested that due to the terms and condition of loan like penalty in case of default, schedule of installments, installment amount etc also discourage the customers to take loan from the banks.

3.7. Availability of Alternative sources

The availability of alternative source of funding is also a big challenge to this sector. The source of funding like non-government organization, societal funding etc may be used by the customers to avail the funds easily and

cheaply.

3.8. Gender Discrimination

According to the respondents, the source of funds is mostly offered to the male customers. In such situations, females are discouraged for non-availability of the funds. The female customers should be also encouraged equally like males and the funds to be distributed equally between male and female customers.

4. Opportunities

The following are the different opportunities to the microfinance sector in KPK province.

4.1. Poverty Alleviation

The main advantage that can bring the microfinance sector is alleviation of poverty. The KPK is facing a challenge of poverty. The microfinance is one of the important tools in helping poor people's by providing loans to them.

4.2. Economic Development

According to the most of the respondents, microfinance is helpful in development of the KPK province and ultimately the country. Providing loans to the people will boost the economic process of the country, which will further enhance the economic development of the country.

4.3. Islamic Financing

The Islamic mood of financing is a good opportunity to this sector. Most of the people in KPK are strong believers of Islam. In such situation, providing loans on Islamic mode of financing will boost this sector. In the opinions of the respondents, this is a good opportunity for the microfinance institutions to encourage people towards this sector.

4.4. Entrepreneurship

The microfinance sector can be also helpful in developing the entrepreneurship field in the economy. The loans can be provided to those people having unique ideas, so new business will emerge and in that case, the entrepreneurship field will be simultaneously developed.

5. Conclusion

Microfinance services implication is a tool to reduce poverty and compensate the war affected families and communities in the province of KPK. The adoption interest free micro financial practice will easily overcome the negative perception against this sector because Islam is not against the trade or businesses for any community; however Islam is against the exploitation of the community through interest and other illegal means which are prohibited by Islamic principles. The government contributions are not too much appreciated for the development of this sector as compare to other developed and emerging countries. For the encouragement of this sector in KPK province, the borrowing rate is lower as comparing to other province. Microfinance institutions advancing rate has a positive correlation with literacy rate of KPK because every educated community has strong ethics, norm and standard and can respond to available opportunities more than an ordinary person. Security issues have an impact and discourage this field in KPK because security is very essential in the development of this sector. For costs and benefits analysis perspective any loan free of interest or having low cost of capital is good for a business. For responding opportunities, the inhabitants especially businessmen of KPK are interested to take loans from financial institutions and banks for micro finance schemes for lower rates of interest. Individuals desire to have a good bargaining power which has a low costs but high benefits. So much of the individuals are satisfied from the loans terms and conditions. For quick and timely recovery the debtors should be motivated by offering good incentives and benefits. For social point of view all the micro finance programs launched are encouraging sympathy in the communities whose are victim of terrorism etc can reform our society up to a great extent.

5.1. Recommendations

The following are the recommendations which are based on the above study of the project.

- The Microfinance institutions should broader their facilitations, services etc to show opportunities for the individuals and to provide a best course of action for the development of that opportunities.
- The religious factor has the capacity to create chaos in any smooth function of a society. As the society motivates interest free society, therefore microfinance institutions should make their institution interest free to comply with the society.
- The Microfinance institutions are required to encourage and train individuals having business plans.

- Government and Financial institution should encourage those small businesses which are involved in semi-finished goods by doing so, it will benefit the household individually and the whole industry as a whole. This process is very common in Japan, China and Bangladesh.
- The institutions which are directly and indirectly involved in microfinance have to give social awareness and responsibility to the public by conducting seminars and advertisement on Radio and Television etc.
- The financial institutions have to launch such type of projects where the inheritance is to create commercial electricity through solar systems and grades.
- The institution should encourage those projects which can be made successful by use low energy and low cost as the under developed country like Pakistan lack both of these.

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