

Micro-Finance and Its Impacts on People and Societies

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Abstract

Microfinance origin has started in 1976 by Muhammad Yunus, it has positive impacts on poor and societies. In this article we have briefly described the microfinance and its impacts on people and society. We have also explained the Grameen Bank Model, the main purpose of the article is to provide the awareness about the microfinance, and how it can be helpful in well-being of the society and poverty reduction. In this first section we have describe the history of microfinance and Grameen Bank, next we have explained the impacts of microfinance, and in the last section we have discussed conclusion and suggestions.

Keywords: Microfinance, Grameen Bank, poverty alleviation, women empowerment, economic growth

1. Introduction

“Microfinance refers to an array of financial services, including loans, savings, and insurance, available to poor entrepreneurs and small business owners who have no collateral and wouldn't otherwise qualify for a standard bank loan”. Microfinance is a broad term to define financial services for people with low incomes or those who do not have access to traditional banking services. Microfinance is the awareness that people with low incomes can raise themselves out of poverty if given access to financial services. According to the Canadian International Development Agency (CIDA), "microfinance is the distribution of a wide range of financial services to poor families, poor micro-enterprises, which typically do not have access to the formal financial institution (Roy, 2003). The term micro-credit belongs to the micro-finance and is a continuation of small loans to entrepreneurs too poor to qualify for traditional bank loans. Especially in developing countries, microcredit allows poor people for self-employment projects that generate income, allowing them to improve the quality of life for themselves and their families (Khan & Rahaman, 2007).

1.1 HISTORY OF MICROFINANCE

Ideologies of microfinance are more closely associated with the Economist Muhammad Yunus, who in the early 70 was a professor in Bangladesh. He spread the concept of microfinance in the midst of a famine across the nation began to make small loans to poor families in nearby towns in an effort to break-down the circle of poverty. The experiment was an incredible success, Yunus, receive the timely return and observe significant changes in the quality of life for the borrowers. Muhammad Yunus presented a model which is called Grameen model on the base of this model he established a Grameen Bank. In order to focus on the poorest, the Bank has lent only to households have at least a half-acre of land. Reimbursement rates were kept high, and the Bank began to expand its activities to other regions of the country. In less than ten years, the Bank acts independently of the Government the founders and advertising fees for the return of 98 percent. In the year 2006, Yunus received the Nobel Peace Prize. The success of the Grameen Bank has not gone unnoticed. Institutions by copying the model jumped in almost all regions of the world. Between 1997 and 2002 respectively the total number of MFIs increased from 618 to 2572. In the collection of those agencies said about 65 million customers, in 1997 to 13.5 million and growth of 35% per year? The amount of money flowing to grow rapidly and even the Grameen Bank extended about \$ 750 million loans for the last two years (Kevin, 2015).

1.2 How Grameen Bank Model Works:

The Grameen model or Grameen Bank started by Prof. Mohammed Yunus in Bangladesh. It essentially adopts the following methodology:

A field manager and bank workers visited the villages and they cover the area of 15 to 22 villages, they find the clientele who can avail the microfinance services and started a movement to familiarize the people about microfinance. They explained local people about the Grameen Bank operation. Group of five borrowers were designed, first time only two of them can avail the loan facility. The group was monitored for regular repayment with interest and successful repayment of first loan make the other two members eligible for credit. All the members have collective responsibility to make their records clear for the next payment of credit therefore group work as collateral for loan (Hari).

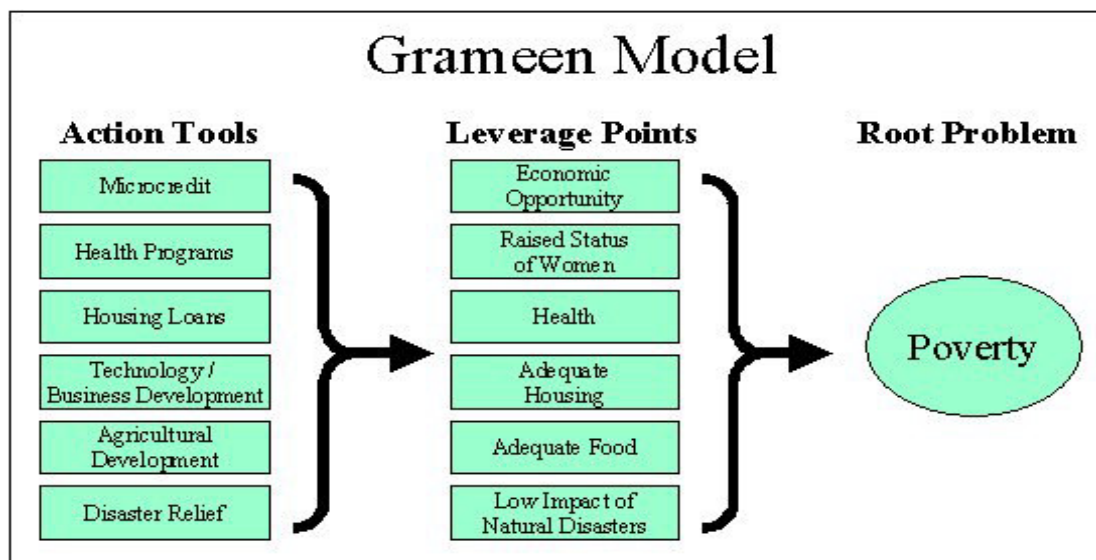


Figure: 1
 Source: (Garvin, 1999)

1.3 FEATURES OF MICROFINANCE

Microfinance provides access to financial and non-financial services for low-income individuals who want to get access to money to start or develop their income-generating activities. Individual loans and savings to poor customers are small. Microfinance has emerged with the satisfaction that the micro-entrepreneurs and some poor can be "bankable", i.e., that it is possible to pay both loan and interest on time and also make savings, financial services are designed to meet your needs. Microfinance has created financial products and services, which together enable people with low incomes to be a client of the bank (Khan & Rahaman, 2007).

The characteristics of microfinance products include:

- ❖ The Loan provides for short-term (for one year).
- ❖ Small amounts of loans and savings.
- ❖ Frequent Payment schedules or frequent deposits.
- ❖ Installments made up from both principal and interest,
- ❖ Higher interest rates on credit (higher than commercial bank rates but lower than loan-shark rates)
- ❖ Easy access to the microfinance services which saves the time and money of the client and provides better ideas to the clients for their financial and social status.
- ❖ Application procedures are simple.
- ❖ Short processing periods (between the completion of the application and the disbursement of the loan).
- ❖ The clients who pay on time become eligible for next time high amount of loans
- ❖ Without collateral lending to the poor (Khan & Rahaman, 2007).

1.4 IMPACTS OF MICROFINANCE

Potential impacts of microfinance are about understanding how micro-credit positively affects the lives of the very poor people in the area where they are under taken. It is very imperative to note that the rural poor and smallholder farmers in developing countries are severely affected by extreme poverty threats. Providing them microfinance services can be one of the effort to enable them escape from the poverty. Microfinance program have positive impacts on the lives of the poor. Microfinance has increased awareness on health and education in the community. It has been found supportive on improving the living condition of the marginalized groups. The access and control over resources and participation of women in decision-making have improved through Microfinance program. Microfinance program is dedicated to the women and marginalized segments of the community. But there is much to be done as still there is a low outreach of microfinance service to the poor from excluded community. They are very poor socially and economically. If the government supports such community on the social sector (health, education & others) MFI will provide them financial services to economically uplift them. Therefore these socially and economically deprived communities can be uplifted by forming cooperation with the government sector, donors and microfinance institutions (Chandra, 2008).

The impact is about understanding how financial services affect the lives of poor people. The impact can measure in terms of poverty reduction, health, education, household income and overall social improvement in the society.

Household level: By using the microfinance services at household level how much it increases the income of people. How many people becomes able to invest in education, health and income growth. Access to microfinance allows them to better manage risks and exploit the opportunities (Monique & Deena, 2003).

Individual level: Microfinance has empowered women because they do better money management, better resources controller, and women lead to greater choices in the family and community matters. Women can do better saving and invest wisely.

Enterprise level: Enterprise revenues increase as a result of microfinance services. Creation of job in single - person initiatives appears negligible. Though, when the total number of enterprises is combined, client family unit often create work for others. For example, in Peru, each microfinance client created three additional working days per month for non-household workers (Monique & Deena, 2003).

1.5 MICROFINANCE IMPACTS ON LOCAL ECONOMY

The microfinance services have potentially positive impacts on the local economy as well as on the agriculture sector. Small holder farmer's access to the microcredit can increase the productivity of the agriculture and they can improve the food availability. Beyond the enhancement of the food microcredit also allow them to invest in farming and generate income for the household members. The involvement of the local people in the microfinance activities contribute to local economic growth.

- Microfinance work as fuel to the local economy
- The poor becomes able to earn for their basic needs and they work as self-employed,
- Microfinance provides job to the people
- Reduce the poverty and other challenges
- It empowers the women and increases the household income
- Microcredit have increased the level of education, health and nutrition (Morduch & Haley, 2002).

DOES MICROFINANCE CONTRIBUTE TO ECONOMIC DEVELOPMENT

Microfinance program has a positive impact on the lives of the poor. Microfinance has raised consciousness in the areas of health and education of society. It was founded based on the improvement of the living conditions of the poor. Microfinance program improves access to and control over resources and the participation of women in decision-making. In the world where nearly half of the population resides in poverty, microfinance offers innovativeness, small loans for low-income groups, to generate income and employment for local authorities. So, microfinance has been processed as an important tool for economic development. Poor are forced one to wait a long time for the benefits of economic growth, which are separated by the distance from urban areas, where the economic activity is concentrated. It is important in this section of the society for less expensive conventional balanced growth take part for sustainability in the long term economic prosperity and social development is important. To strengthen the social, economic, financial services for low-income people who lives in rural areas (Singla, 2014). Microfinance plays vital role in economic development through following ways:

Poverty Alleviation: microfinance has been found an operational tool for lifting the poor by providing them financial services to start or expand a small business that enables them to break out of poverty. It enables poor to earn an income so they no burden to meet the expense of food, clean water, healthcare and education for their children. These small businesses also produce employment opportunities for such local societies where jobs are rare they can earn extra income.

Women Empowerment: Microfinance is an important tool for empowering the women same as poverty reduction. Poor women use small loans to start a small business activity and raise their income.

Financial Inclusion: Microfinance has made unbanked people to bankable through financial services such saving and money lending etc.

Mobilization of Savings: Microfinance develops the saving habits of the people. Now low-income people also save money and become bankable

Financial Stability: Microfinance provides financial stability to individuals which contributed to local economies significantly. Small loans have presented chances to earn an extra income so that people can pay for their extreme needs.

Development of Skills: Microfinance has assisted in finding the potential rural entrepreneurs. SHGs inspire its members to establish their businesses mutually or independently (Singla, 2014).

MICROFINANCE SERVICES ARE TARGET CLIENTS AND BEST ABLE TO CONTRIBUTE TO ECONOMIC GROWTH

Microfinance services are basically target clients because these services are provided to the poor, in terms of micro-credit, micro saving, and insurance, Which helps the poor to improve their financial status, as they can get rid of from poverty. Microfinance services empowers the poor, financial stability and savings which may lead the poor to economic growth because when poor are able to fulfill their basic needs and become bankable so its

means they can survive in the society, on the other hand, microfinance is contributing to the economic growth. Therefore we can say that microfinance is best able to contribute to the economic growth.

WHY LENDING TO THE POOR IS DIFFICULT

Now a day's microfinance has been growing rapidly, it did lots of work for the alleviation of poverty and economic development but there is still a risk to giving the loans to the poor because of some typically reasons which are:

- Mostly poor don't have collateral
- High risk
- The credit repayments rate of poor is very low therefore lending to them is costly
- Significant gap between lending rates and deposit rates within the same sub-economy
- Extreme variability in the interest rate within the same sub-economy:
- The poor get smaller loans and pay higher interest rates
- Production and trade finance are the main reasons given for borrowing, even in cases where the rate of interest is relatively high
- Informational asymmetries (Moral hazard: the monitoring cost multiplier)

How Microfinance Solves the Moral Hazard Problem?

Esther, 2011 describes in a study, that if moral hazard is genuine, then credit market can lead to a poverty trap, at the individual level, and at the societal level. On the other hand adverse selection, if interest rates are high which may discourage those clients who are planning to repay, and encourage those clients who have a low cost of default and were planning to default anyway.

Microfinance has solved the moral hazard problem by adopting the Grameen model. The model of microcredit (Grameen Bank) has the following elements:

- ❖ Without collateral lending
- ❖ Loans provide almost only to women.
- ❖ Weekly biases repayment schedule
- ❖ Group lending (a group of 5 women who know each other).
- ❖ Regular meetings at centers, where members can be discussed their business, take advice for business and households.
- ❖ On initial stage very small loans provided, which can be increased over time.
- ❖ Regular monitoring of clients by credit officers.
- ❖ High-interest rates (at least 20% a year, often much more)

Why Lending to Women ratio is high than men?

Women are basically more trustworthy than men, lending to women is empowering the women domestically so that is an objective to improve the household. Women have high repayment ratio because they don't have other access to credit. So, therefore Muhammad Yunus focus more on women.

Microfinance Revolution and innovation?

Microfinance revolution is basically a way to helps the poor in the society. Microfinance has brought the hope for the poor, it doesn't only run the poverty reduction programs but also provide other facilities to the destitute people in terms of savings and insurance. Through microfinance services we can help the poor that they can help themselves and get rid of poverty without spending too much money. The worldwide success of this vision appealed to replicate the model in other areas through social enterprise. The response against micro-credit was no less extreme: new lenders, investors from short-sightedness of the poor. The evidence leads to a far more nuanced conclusion: financial innovations were given access to credit for some families that may start a new business. It helps others to save or charming surprises. However, not everyone is a natural businessman and the poor face other barriers to accumulation (time inconsistency, endogenous discouragement). Microfinance is a great innovation, it should be supported and we should continue to develop new projects to improve financial access. However, it cannot replace antediluvian ways to help the poor (Esther, 2011).

Conclusion

From the above discussion about the microfinance it show that microfinance is an innovative way to poverty reduction. Through microfinance services poor people can utilize their skills for enhancement of household economic growth, educate their children and enhanced quality of life. Poor can contribute to economic development and can fight against hunger and poverty alleviation. Microfinance empower the women so women can also contribute in the economic growth as well. Therefore Muhammad Yunus mostly focused on women

because women are more trust worthy than men and manage household better than men. Many people accepted that microfinance is not a magic bullet to reduce the poverty however, it is way to improve the living stander of the poor. Microfinance institutions should conduct micro credit awareness programs for the poor people because mostly poor don't have the knowledge about the micro finance services so that poor can be attracted by the microfinance services. MFIs and poor's mutual effort can reap the benefits of microfinance services and win the battle against poverty.

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