International Journal of Economics and Development Policy (IJEDP)
Vol. 6 No. 1, June, 2023
Print - ISSN: 2651-5644
Online - ISSN: 2651-5644

Microfinance Banks and Sustainable Poverty Reduction in Nigeria

Mustapha Hussaini

Department of Economics, Sule Lamido University, Kafin Hausa - Nigeria

*Corresponding Author's; E – mail: mustapha.hussaini@slu.edu.ng

Abstract

The paper examined the role of microfinance in providing sustainable means of poverty reduction in Nigeria. Microfinance has become an important tool in global poverty reduction and there have been a lot of debates on its sustainability in reducing poverty. The argument is that, allowing poor people access to financial services help them establish micro businesses and improve their income and eventually escape poverty. The paper employed both primary and secondary data to examine the impact of microcredit on the level of income of the poor. The finding shows that, microfinance institutions have positive and significant effect on poor clients who took loans to support their business although a number of challenges and institutional bottlenecks are still evident. The study therefore, recommends that government should increase funding to the microfinance sector to reduce the high interest rate charged by most of the MFIs and an effective awareness campaign on the activities of the microfinance institutions particularly in the rural areas to increase the beneficiaries.

Keywords: Microcredit, Microfinance, Poverty, Nigeria
JEL Classification: E22, E51, 055, I32

Contribution to/Originality Knowledge
The paper provided as its contribution to the literature two primary inputs. One, the paper provides an insight into the important role that microfinance provides in reducing poverty and increasing income and livelihood of the poor in Nigeria. Most studies on the topic are general studies that examined the roles of microfinance on economic growth and development, few scholars have paid attention to the specific roles of microfinance on poverty reduction.

1.0 Introduction

It is an established fact in the economic literature that, robust economic growth cannot be achieved without putting in place well focused programmes to reduce poverty through empowering the people by increasing their access to factors of production, especially credit. The latent capacity of the poor for entrepreneurship would be significantly enhanced through the provision of microfinance services to enable them engage in economic activities and be more self-reliant; increase employment opportunities, enhance household income, and create wealth.

Thus, Microfinance is about providing financial services to the poor who are traditionally not served by the conventional financial institutions. Three features distinguish microfinance from other formal financial products. These are: the smallness of loans advanced and or savings collected, the absence of asset-based collateral, and simplicity of operations.

In Nigeria however, the conventional financial system provides services to about 35% of the economically active population while the remaining 65% are excluded from access to financial services (CBN, 2005). This 65% are often served by the informal financial sector, through Non-Governmental Organization (NGO) institutions, moneylenders, friends, relatives, and credit unions. The non-regulation of the activities of some of these institutions has serious implications for the Central Bank of Nigeria's (CBN's) ability to exercise one aspect of its mandate of promoting monetary stability and a sound financial system. This however signaled the need for a microfinance policy that recognizes the existing informal institutions and brings them within the supervisory purview of the CBN. This will not only enhance monetary stability, but also expand the financial infrastructure of the country to meet the financial requirements of the Micro, Small and Medium Enterprises (MSMEs). Such a policy would create a vibrant microfinance sub-sector that would be adequately integrated into the mainstream of the national financial system and provide the stimulus for growth and development. It would also harmonize operating standards and provide a strategic platform for the evolution of microfinance institutions, promote appropriate regulation, supervision and adoption of best practices (CBN, 2005).

Against these backgrounds, Nigerian government in 2005 following the recommendation of the World Bank, Microfinance was officially introduced in Nigeria in 2005 through the establishment of Microfinance Policy, Regulatory and Supervisory Framework of 2005 (CBN, 2005). This policy provides a National Microfinance Policy Framework for Nigeria enhancing the provision of diversified microfinance services on a long-term, sustainable basis for the poor and low income groups with the target of covering the majority of the poor but economically active population by 2020. Thereby creating millions of jobs and reducing poverty, increasing the share of micro credit as percentage of total credit to the economy from 0.9 percent in 2005 to at least 20 percent in 2020. The policy sought to increase the share of micro credit as percentage of GDP from 0.2 percent in 2005 to at least 5 percent in 2020, promote the participation of at least two-thirds of state and local governments in micro credit financing by 2015. It aims at eliminating gender disparity by improving women's access to financial services by 5% annually; and increase the number of linkages among universal banks, development banks, specialized finance institutions and microfinance banks by 10% annually.

Nevertheless, for almost fifteen years after the formal introduction of microfinance banks in Nigeria, eight hundred and eighty-two (882) Microfinance banks were officially licensed by the Central Bank of Nigeria as at October, 2018 (CBN, 2018). The distribution of which is highly concentrated in few states of the federation as from the records, one hundred and seventy (170 or 19.3%) of the microfinance banks (MFBs) operating in Nigeria are in the city of Lagos, Anambra followed closely with seventy-five (75) microfinance banks operating in the state while Oyo (53), Abuja (49) and Ogun (49) complete the list of the top five (5) States with the highest number of Microfinance Banks as at Sept 30, 2018. Yobe State has the least with one (1) microfinance bank only operating in the state. Notwithstanding the modest achievement recorded by MFBs in Nigeria, the poverty rate in the country remains daunting such that majority of the disadvantaged and economically active poor remain financially excluded and more importantly, the sustainability of microfinance as a strategy for poverty reduction. This however motivates the study.

The paper provided as its contribution to the literature two primary inputs. One, the paper provides an insight into potential sustainability of poverty reduction through microfinance in Nigeria. Most studies on the topic has been mainly confined to a limited examination of the roles of microfinance on poverty without paying attention to the sustainability of the strategy. Two, the paper focused on Nigeria which was declared as the poverty headquarter of the world in 2018 (i.e the country hosting the largest number of people living in poverty) the paper will provide a unique case study given the vast size of populations and the range of economic and social crisis its facing such as extreme poverty and high rate of unemployment, and lacking in the necessary number of financial infrastructure to promote its business opportunities. The rest of this article provides an overview of microfinance activities in Nigeria, challenges of microfinance in sustainable poverty alleviation, method of data analysis followed by findings and finally conclusion and recommendations.

2.0 Overview of Microfinance Activities in Nigeria

The practice of microfinance in Nigeria is culturally rooted and dates back several centuries. The traditional microfinance institutions provide access to credit for the rural and urban, low-income earners. They are mainly of the informal Self-Help Groups (SHGs) or Rotating Savings and Credit Associations (ROSCAs) types. Other providers of microfinance services include savings collectors and co-operative societies. The informal financial institutions generally have limited outreach due primarily to paucity of loanable funds.

In order to enhance the flow of financial services to Nigerian rural areas, Government has, in the past, initiated a series of publicly-financed micro/rural credit programmes and policies targetted at the poor. Notable among such programmes were the Rural Banking Programme, sectoral allocation of credits, a concessionary interest rate, and the Agricultural Credit Guarantee Scheme (ACGS). Other institutional arrangements were the establishment of the Nigerian Agricultural and Co-operative Bank Limited (NACB), the National Directorate of Employment (NDE), the Nigerian Agricultural Insurance Corporation (NAIC), the Peoples Bank of Nigeria (PBN), the Community Banks (CBs), and the Family Economic Advancement Programme (FEAP). In 2000, Government merged the NACB with the PBN and FEAP to form the Nigerian Agricultural Cooperative and Rural Development Bank Limited (NACRDB) to enhance the provision of finance to the agricultural sector. It also created the National Poverty Eradication Programme (NAPEP) with the mandate of providing financial services to alleviate poverty.

Microfinance services, particularly, those sponsored by government, have adopted the traditional supply-led, subsidized credit approach mainly directed to the agricultural sector and non-farm activities, such as trading, tailoring, weaving, blacksmithing, agro-processing and transportation. Although the services have resulted in an increased level of credit disbursement and gains in agricultural production and other activities, as of 2018 The Central Bank of Nigeria has released the list of 882 licensed Microfinance banks in Nigeria. From the records, one hundred and seventy (170 or 19.3%) of the microfinance banks operating in Nigeria are in the city of Lagos, Anambra state. These are followed closely with seventy-five (75) microfinance banks operating in the state while Oyo (53), Abuja (49) and Ogun (49) complete the list of the top five (5) States with the highest number of Microfinance Banks as at Sept 30, 2018. Yobe State has the least with one (1) microfinance bank only operating in the state as shown in the table below:

Table 1: Distribution of Microfinance Banks in Nigeria

Number of Micofinance Banks per State in Nigeria			
State	Number	State	Number
Lagos	170	Abia	12
Anambra	75	Kebbi	12
Oyo	53	Plateau	12
Abuja	49	Adamawa	11
Ogun	49	Benue	11
Kano	46	Cross River	11
Imo	37	Bauchi	10
Osun	29	Ebonyi	9
Delta	27	Ekiti	8
Kwara	27	Jigawa	8
Niger	27	Nassarawa	8
Enugu	25	Borno	4
Kaduna	23	Gombe	4
Katsina	23	Sokoto	4
Edo	20	Zamfara	4
Akwa Ibom	17	Bayelsa	3
Ondo	17	Taraba	3
Rivers	17	Yobe	1
Kogi	16	**Total**	**882**

Source: CBN, 2018

However, the CBN gave an indication in late September 2018 to revoke the operating licenses of 154 microfinance banks. The CBN said 62 of the microfinance banks had already closed shop; 74 became insolvent; 12 were terminally distressed; while six voluntarily liquidated (CBN, 2018).

Microfinance Banks and the Challenges of Sustainable Poverty Reduction in Nigeria

Microfinance banks are in most cases established with the sole aim of providing credit access to the poor. Exploration into the literature has shown that development specialists have debated on whether micro finance has provided the needed financial support required by the poor to venture into business and other income generating activities. Or the poor are using the credit for consumption smoothing purpose only. In most cases, the rural poor who are predominantly engaged in seasonal farming activities will at the initial stage start some income generating activity with the loan to improve their cash flows. But eventually, the beneficiaries would end up using the loan in satisfying their immediate consumption needs and thereby defeating the objective for which the credit is offered.

More also, the literature pointed out as to whether the poor can be good entrepreneurs if provided with credit. The issue is that, in most developed countries people usually prefer jobs to entrepreneurships as they are riskier. Therefore, the assumption that the poor would possess better entrepreneurial skills is provided with capital may not necessarily hold.

Other crucial issues identified in the literature are those other factors that hindered the effectiveness and efficiency of micro-finance on poverty alleviation. These factors as explained by Ahmed (2002) are as follows:

a) **Non-Conforming to Islamic Religious Beliefs:** the major problem that limit the performance of conventional MFIs in northern Nigeria in particular is the nonconformance of the credit system to the popular religious beliefs. This is because Riba (Usury) is prohibited in Islam. Most of the practicing rural Muslims have exhibited high resistance to conventional micro-financing because of this fact. Another issue is the focus of credit to women. In some cases, this focus has created social conflict in conservative populations. In extreme cases, although women are the recipients of credit, the credit ends up with the male member of the family, leading to misappropriations and credit diversion.
b) **Asymmetric Information Problems:** information about the existence and the availability of different credits in the available microfinance banks are very scanty and even nonexistent in some cases. Although the focus of these conventional micro-financing institutions is to encourage the participation of women in entrepreneurial development, in most cases, the loans end up in the hands of the male counterpart and are used for other purposes. This has to a greater extent limit the performance of microfinance institutions in reducing poverty in Nigeria.
c) **Charging Fixed Interest Rates:** Although, MFIs are in most cases charging relatively lower interest rate compared to the conventional commercial banks, they are also pursuing a standard and generalized policy of lending rates across loan categories. This however, posed a greater challenge as profitability may differ across investments and because of differences in geographic or demographic conditions. For instance, an investment located in an urban area with an improved infrastructure may be more profitable than a similar investment in a rural area with inadequate infrastructure. Therefore, charging a fixed interest rate across investments might be counter-productive and hence, demoralize poverty alleviation objective.
d) **Low Rate of Return on Investment:** Given that most of the activities financed by the micro finance banks are activities that usually substitute the agricultural or farm activities and require fewer skills. The beneficiaries mostly engaged in the production of basic commodities, transportation, and trading at smaller scale ventures which always have low return. Therefore, as more and more households become involved in

such ventures, return on such loans decreases as the supply side of such activities increases (Osmani, 1989).

e) **High Dropout Rate and Non-Graduation from Poverty:** The objective of micro-finance is to enhance micro-businesses and eventually alleviate poverty through ensuring a sustainable growth in their income level (Hassan, 2010). Most of the beneficiaries of these micro credits engaged in very basic activities that possess low returns, therefore, they fail to attain desired income growth that will successfully graduate them from poverty. As many failed to graduate from poverty, this result in higher dropout rates and hence compound the poverty situation.

3.0 Method of Analysis

Three Local Government Areas were selected in Jigawa State namely Auyo, Roni and Buji Local Government Areas. The Local Governments which were all rural areas and were chosen one per each of the three Senatorial District of the State using purposive sampling. This is because studies showed that poor people in Nigeria lack access to credit facilities and mostly live in rural areas (Adeola 2000). Primary data collection instrument was employed. Data was collected through structured questionnaire that was administered to the microfinance bank clients for at least 3 years while secondary data were sourced from the records of the microfinance banks through administration of questionnaire in the selected Local Government Areas.

Table 2: Objectives, Data and Analytical Tools

S/N	Objectives	Required Data	Source of Data	Tool of Analysis
1.	Examine the impact of microfinance credit on the standard of living of the beneficiaries	Head count of poor before and after loan, total income before and after loan and other demographic characteristics of the respondent	Administration of questionnaire to the customers of microfinance banks for at least five years	Foster Grear-Thorbecke Poverty index
2.	Establish the relationship between the size of loan and the standard of living of the beneficiaries	The size of loan obtained by the respondents in Naira and income after loan collection	Administration of questionnaire to the customers of microfinance banks for at least five years	Partial correlation

Source: Researchers Compilation (2019).

4.0 Results and Discussion

In order to achieve objective one of the study, which was to examine the impact of microfinance bank on standard of living? Foster-Greer-Thorbecke (1988) was used to measure poverty index.

Table 2: Poverty head count before and after loan collection

Period	P_0	P_1	P_2
Before	0.0076	0.1668	0.0562
After	0.0076	0.1551	0.0503

Source: Field survey (2019)

Using Foster-Greer-Thorbecke (1981) poverty index which is given as

$$FGT = \frac{1}{N}\sum_{i=1}^{H_1}\left[\frac{z - y_1}{z}\right]\alpha \tag{1}$$

and

$$FGT = \frac{1}{N}\sum_{i=1}^{H_2}\left[\frac{z - y_2}{z}\right]\alpha \tag{2}$$

Where:

N = No of Respondents (360)

H_1 = Head count of poor before loan

H_2 = Head count of poor after loan

y_1 = Income before loan

y_2 = Income after loan and

z = Poverty line using $1 per day

Table 3: Poverty Headcount

Period	**Head Count**	**Percentage**
Before (H_1)	216	60%
After (H_2)	193	53%

Source: Field survey (2019)

Using the international poverty line of $1 per day per person which is equivalent to N129,600 per annum at the exchange rate of N360 per dollar, therefore any respondent whose income is below N10,800 per month or N129,600 per annum is considered poor.

The result showed that the head count of poor people among the respondents before collecting loan (H_1) is 60% (216 respondents), while after collection of loan (H_2) the head count is 53% (193 respondents) which showed a 7% reduction in the number of people that are poor as a result of taking a loan from microfinance bank institutions.

This result is in consonance with UNDP (2016) publication that reported that about 53% of Nigerians lives below the international income poverty line of (USD 1) per day.

The findings of the paper are in conformity with a number of previous studies on similar topics such as that of Yunus (2003), Mohammad and Mohammed (2007); Yeshiareg (2009); Idowu and Salami (2010) Yahaya *et al.,* (2010) and Idowu and Oyeleye (2012) who also reported that collecting credit from micro finance impacted positively on the income and standard of living of the rural poor.

To establish the relationship between the size of loan and the standard of living of the beneficiaries. The paper estimated a partial correlation between the size of loan obtained by the respondents in Naira and his income after loan collection. The result shows that there was a moderately, positive correlation between the two variables, $r = .038$, $N = 360$; however, the relationship was also significant ($p = .32$). Thus, the size of loan collected by a small business owner appear to be associated with his standard of living as it improves his income.

5.0 Conclusion and Recommendations

As can be deduced from the findings of the paper, microfinance is an important tool of poverty alleviation among the economically active poor and can help in improving their standard of living by increasing their income level. However, there are still a number of challenges that are limiting the proposed benefits of microfinance on poverty reduction that requires a sustain effort by the government. And all other stakeholders. Against this backdrop, the paper recommends that;

1. Government should through the Central Bank of Nigeria (CBN) make provision for

   adequate funding for MFIs and establish more Microfinance Institutions particularly in the rural areas where majority of the poor are located and provide adequate information and awareness with regards to the services they provide

2. MFIs should also endeavor to design better products that will attract the poor and embark on public campaigns, advertisement and enlightenment with regards to the availability of funds and their benefits because most of the poor are unaware of the benefits of MFIs to the poor.

3. The current study was based on a smaller scale the result cannot be generalized in the analytical term. Further study needs to be done on a large scale to determine how microfinance operations reduce poverty.

REFERENCES

Adewole, E.A (2008). The Contribution of Microfinance Bank to the Development of Nigerian Economy. An unpublished MBA thesis, Ladoke University of Technology, Ogbomoso.

Ahmed, Habib (2002). 'Financing Microenterprises: An Analytical Study of Islamic Microfinance Institutions'. *Islamic Economic Studies* 9(2): 27-64.

Central Bank of Nigeria (2005) CBN Briefs: 2004 – 2005 Edition, Abuja: Research and Statistics Department, CBN

Dichter, Thomas (2007), "A second look at Micro-finance: The sequence of Growth and credit in economic history", February 15, 2007. Downloaded from Internet (http://www.cato.org/pub_display.php?pub_id=7517)

Hassan M. K. (2010) an integrated poverty alleviation model combining zakat, awqaf and micro-finance *Seventh International Conference – The Tawhidi Epistemology: Zakat and Waqf Economy, Bangi 2010.*

Hassan, M. K. (2003): "Financing the Poor: Towards an Islamic Micro-finance",

Mimeo, University of New Orleans, Novmeber, 2003.

Hossain, F. & Rahman, M. (2001). Microfinance and Poverty: Contemporary Perspectives. University of Tampere. [Online] Available pdj.sagepub.com/content/9/2/115.reds Assessed (November, 4 2009).

Idowu. A. & Salami A. (2010). Impact of Microfinance Bank on Standard of Living of Hairdresser in Ogbomoso North Local Government. *American Journal of Social and Management Sciences.* 2(1) pp 34-40. Assessed May 23, 2011.

Idowu, A. Oyeleye, O. A. (2012) Impact of Microfinance Banks on Poverty Alleviation in Selected Local Government Areas of Oyo State, Nigeria European Journal of Business and Management www.iiste.org Vol 4, No.21, 2012

Mohammad A.K & Mohammed A.R (2007). Impact of Microfinance on Living Standards, Empowerment and Poverty Alleviation of Poor People, A Case study of microfinance in Chittagong District of Bangladesh, unpublished Master Thesis, Department of Business Administ rat ion, Umea School of Business. [Online] Available www.scihub.org (Dec.23, 2009).

Yahaya, K.A, Osemene, O.F & Abdulraheem A. (2010). Effectiveness of Microfinance Bank in Alleviating Poverty in Kwara State. *Global Journal of Management and Business Research Vol 2 issue 4 pp 9.*

Yeshiareg, D. (2008). Promoting Women's Economic Empowerment in Africa. [Online] Available http:www.org/aee/document/Yeshaireg%20Dejanepdf. Accessed (Aug. 6 2009).

Yunus, M. (2003). Banker to the Poor Micro-Lending and the Battle against World Poverty". Pinoy-business.com

Zaman. H. (2000). Accessing the Poverty and Vulnerability Impact of Micro Credit in Bangladesh. A Case Study of Brae Publication of World Bank http://book.google.com/books pp 296- 302