

Microfinance Works as a Tool for Poverty Reduction in Rural Bangladesh

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Abstract

Introduction: According to the World Bank, poverty is measured by income. Bangladesh uses microcredit as an anti-poverty tool for reducing poverty. The aim of the study is to find out the impact of microcredit on poverty reduction in rural Bangladesh. **Methods:** This study run by following qualitative and quantitative research process based on secondary data recorded from 2002 to 2012. Study data as number microcredit borrowers have been calculated from Microfinance Information Exchange (MIX) Market Database and rest of the data are collected from the World Bank, Household Income & Expenditure Survey Report and relevant literatures. **Result:** Microcredit has an impact on the income poverty reduction. During the last decade, income poverty had reduced 1.5% in Bangladesh. So, MFIs are not necessary for reducing poverty because if income is increased, it depends on the poor people how they will utilize their money. **Conclusion:** From this study we found that microfinance can reduce the poverty by giving credit loan and generating income.

Keywords: World Bank, income, Microfinance Information Exchange (MIX), microfinance.

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INTRODUCTION

It is difficult to define poverty. According to the World Bank, poverty is measured by income. People who live less than US\$ 1 a day are considered poor as they are living below the poverty line. According to the CGAP, people who live below the poverty line are eligible for microfinance clients. The aim of microcredit is to provide credit to the poor for reducing poverty through income generating activities. According to the UNDP, poverty is considered as income poverty and human poverty. Since independence in 1971, during the last 42 years the government of Bangladesh has tried to reduce poverty (income poverty and human poverty) by different initiatives with the NGOs including micro-credit. The rate of income poverty (poverty head count ratio) in Bangladesh is measured by the Cost of Basic Need (CBN) method which is considered that the upper poverty line is now reduced from 48.8% to 31.5% from 2000 to 2011 [1]. There are four types of microcredit programs in Bangladesh as Microcredit Programs of major NGOs, Microcredit Programs of State-Owned Commercial Banks (SOCBs) & Public Specialized Banks, Microcredit Programs of Other Commercial & Specialized Banks and Microcredit programs of different Ministries of the Government. Government of Bangladesh has initiated micro-credit program for self-

employment of women to reduce poverty (income poverty and human poverty) and to generate self-employment opportunities. The government of Bangladesh, NGOs and different Banks has disbursed total \$10092.28 billion microcredit as a revolving fund till June, 2012 [1]. The major NGOs are BRAC, ASA, PROSHIKA, Thangamara Mohila Sobuj Sangha (TMSS), Society for Social Services (SSS), BURO Bangladesh, PKSF, Grameen Bank, which distributed total \$8544.72 billion microcredit, 84.66% of total microcredit to 40.64 million borrowers [1]. In these circumstances Bangladesh uses microcredit as an anti-poverty tool for reducing poverty (Microcredit Summit, 1997). Microcredit Regulatory Authority (MRA, 2013) mentions that by using microcredit, poor people are engaging themselves in various income generating activities for sustaining their livelihood and it helps to reduce poverty to a certain level.

Thus, the aim of the study is to find out the impact of microcredit on poverty reduction in rural Bangladesh.

OBJECTIVES

a) General Objective

- To examine the relationship between microcredit and poverty reduction as well as to identify its influential effect on income

generation activities in rural Bangladesh.

b) Specific Objectives

- To observe the relationship between microcredit and poverty reduction.
- To explore the role of microfinance on income generation activities.

METHODOLOGY & MATERIALS

This study run by following qualitative and quantitative research process and secondary data have been used from 2002 to 2012. Relevant data of microcredit have been collected from the Microfinance Information Exchange (MIX) Market Database and Household Income & Survey Report of Bangladesh. Data as a poverty headcount ratio (national line and \$1.25 per day), which means that the poverty headcount ratio (national line) is measured by CBN (Cost of Basic Need) method in Bangladesh and poverty headcount ratio (\$1.25 per day) is measured by income, which is an international standard to measure poverty. Study data as number microcredit borrowers have been calculated from Microfinance Information Exchange (MIX) Market Database and rest of the data are collected from the World Bank, Household Income & Expenditure Survey Report and relevant literatures. Data from the World Development Indicator of World Bank have collected by the estimated average method because the time series data of some years are not available there. Besides that, twenty-one microcredit institution's microcredit average data are used in this study and calculate this data to estimate its contribution to GDP. Other information is gathered from the relevant literatures.

DISCUSSION & RESULTS

Poverty is seen as lack of income and microcredit is used as a tool to combat against poverty. According to Hulme and Mosley [2], microcredit increases the level of income among the microcredit borrowers. They also mentioned that Microfinance Institutions (MFIs) such as the Grameen Bank and Bangladesh Rural Advancement Committee (BRAC) in Bangladesh provided credit to the poorest households who were able to raise their income and assets. In contrast, there is a contention that poverty is more than simply a lack of income [3].

Actually, there is an argument on the effect of microcredit in reducing poverty. Some studies believe that the expansion of microcredit programs reduce poverty and promote human, social and economic welfare [4-12]. Likewise, another study supports that at the macro level, microfinance has reduced poverty significantly and worldwide microfinance expansion has a sizeable effect on poverty and hunger as well [13]. On the contrary, there is a finding in Hyderabad, India that microcredit has a moderate impact on household welfare [14].

Some studies show doubt on the effects of poverty reduction because the survey data which is used for analysis is non-experimental [15]. Moreover, Roodman [16] gives evidence that microcredit has no impact on poverty reduction. He also gives evidence from those studies which focus the positive impact of microcredit on poverty reduction and mentions that 'poverty reduction disappears after dropping outliers' [17]. This means that when one variable is dropped from the econometric model, it shows that microcredit has no impact on poverty reduction. The major argument on microcredit is that it cannot reach to the poorest of the poor especially the most vulnerable people in the society [18-20]. Another argument is that the evaluation pattern of microcredit programs has a methodological weakness [21-23]. This indicates that the selection of methodology (self-selection bias and influences of other variables) influences poverty reduction results because by using the same data and different methodology authors get different impact of microcredit on poverty reduction.

The special microcredit programs, which is designed for the ultra-poor that provides flexible credit and non-credit services. This specialized program shows that microcredit influences to increase income, consumption and raise physical assets [24, 25]. Likewise, Norma and Jarita²⁶ mentioned that according to United Nations microfinance is recognized as one of the most effective tools which have contributed to reduce poverty and create job opportunities for the poor.

Rahman and Ahmad [27] have collected primary data to assess the income generation through microcredit. They collected data from 1,020 borrowers across the country and they find that microcredit has significantly increased 'household income, productivity of crops and livestock, expenditure and employment' [27] and reduce income poverty (Table-1). Association of Social Advancement [28] conducted a primary survey to assess the impact of microfinance on its borrower's livelihood during the period of 2008 to 2012. They select four economic parameters (business capital, monthly income, family asset and employment opportunity) to assess whether the borrowers can increase their income or not by using their microcredit. They mentioned that the selected four economic parameters are increased from 83% to 97% among the microcredit borrowers. They found that among the 7168 borrowers only 6937 (97%) borrowers have been able to increase their business capital by using microcredit. The trend of their savings and their business capital are increasing continuously during this period including monthly capitals. The rest of the 231 borrowers (3%) could not invest their microcredit to generate income, 232 (3%) borrowers cannot improve monthly income and 1188 (17%) borrowers cannot improve family assets because of the unavoidable situation as illness and natural calamities. Besides, family assets have

improved among 5980 (83%) borrowers and employment opportunities have increased among 6727 (94%) borrowers (Table-2). Among the microcredit borrowers of the Association for Social Advancement (ASA) who have participated in the survey, 98% of them are women and they invest their microcredit to generate income by the following way (Table-3). Biswas, Kabir and Roy [29] conducted another field survey to collect the primary data among the microcredit borrowers of the microcredit institutions of the Grameen Bank and the Bangladesh Rural Development Board (BRDB) to assess the impact of microcredit on poverty reduction. The borrowers who are the members of the Grameen Bank up to more than 6 years and BRDB up to more than 4 years are selected for the interview. They select 400 microcredit borrowers to assess the impact of microcredit in income generation (Table 4, 5). Biswas, Kabir and Roy [29] mentioned that by utilizing microcredit borrowers of Grameen Bank and BRDB also increased per capita capital formation as \$107.22 and \$83.83 respectively. They also collected the information from the microcredit borrowers that borrower's involvement in

the microcredit program improved their economic condition. Borrowers of the Grameen Bank 93% and borrowers of the BRDB 94% improved their economic condition by utilizing microcredit. However, 7% borrowers of Grameen Bank and 6% borrowers of BRDB mentioned that they cannot improve their economic conditions by utilizing microcredit.

Thus, field survey reports mention that microcredit has an impact on the income poverty reduction. During the last decade, income poverty had reduced 1.5% in Bangladesh [29] However, Wright [30] found a significant difference between increasing income and poverty reduction. He also argues that MFIs are not necessary for reducing poverty because if income is increased, it depends on the poor people how they will utilize their money, whether gambling away or spend money on alcohol otherwise invest it in income generating activities. Thus, it is necessary to provide 'sustainable level of well-being' [30] by providing financial services tailoring according to their needs to secure their income and net wealth.

Table-1: Impact of Microcredit on Income Generation

Sources of Income	Borrower's Income (\$)		Changes of Income	
	After join	Before join	\$	\$
crops	168.96	141.7	27.39	19.33
fruits selling	21	12.59	8.4	66.33
vegetable	27.14	18.84	8.3	44.06
livestock	52.37	36.55	51.81	43.26
poultry	21.47	15.38	6.1	39.67
small business	412.52	325.5	87.02	26.73

Source: Rahman and Ahmad [26]

Table-2: Microcredit and Borrowers Income

Economic Parameters	% borrowers increase income
Business capital	97
Monthly Income	97
Family Assets	83
Employment Opportunities	94

Source: ASA [27]

Table-3: Sectors to Invest Income Generation

Sectors to invest for Income generation	% microcredit borrowers
Business	40
Agriculture	23
Livestock	13
Transportation	8
Fishries	8
Poultry	2
Others	6

Source: ASA [27]

Table-4: Annual Income of Per Household by Utilizing Microcredit

Microfinance Institutions	Per household total annual income (\$)	Annual income derived from the utilization of micro-credit (\$)	% of annual income by utilizing microcredit to the total household income
Grameen Bank	987.86	79.2	8.2
BRDB	896.17	56.01	6.25
All(average)	942.02	67.6	7.18

Source: Biswas, Kabir and Roy [28]

Table-5: Income Generation by Investing Per \$ 1.29 Microcredit

Investment Sectors	Number of respondents		Income generation by investing per \$ 1.29 microcredit (\$)			
	Grameen Bank	BRDB	Grameen Bank (\$)	% increase	BRDB (\$)	% increase
Cow rearing / beef fattening	105	89	.84	65.11	.72	55.81
Small business	116	97	.89	68.99	.79	61.24
Land lease / mortgage-in	58	59	.58	44.96	.58	44.96
Purchasing rickshaw / van	32	13	.35	27.13	.84	65.11
Purchasing land	5	6	.19	14.73	.05	3.87
Agriculture (rice, potato, etc.)	27	27	.68	52.71	.59	45.74
Bamboo works	37	20	1.12	86.82	.80	62.01
Purchasing tempo and tractor or repair	4	9	.74	57.36	.85	65.89
Purchasing sewing machine	4	12	1.14	88.37	.71	55.03
Poultry rearing	5	16	.76	58.91	.57	44.19
Goat rearing	-	4	-	-	.75	58.14
Fish cultivation	5	4	1.55	120.15	.76	58.91

Source: Biswas, Kabir and Roy [28]

Limitations of the study

Time series data of microcredit is not available because most of the microcredit institutions did not preserve their data. They do not monitor and keep information regarding microcredit that how much borrowers generated income by using microcredit. There are no specific data that microcredit has improved education and health conditions of the borrower's children. Very few microcredit institutions preserve their data in regular basis and for that reason the number of observations used in this study is very small. Besides that, Household Survey report has the limitation because most of the survey reports are based on the randomly interview method. Thus, it is not possible to take interview of each and every people of a country. Sometimes respondents do not provide the accurate information. For example, when asked to respondents that how much they earn and how much they spend in a month, they cannot provide the exact amount about their income and expenditure. The reasons behind that they have no regular income and for that reason they may forget this or cannot preserve their information regarding income and expenditure like any formal sectors. So, the survey reports do not provide the accurate information.

CONCLUSION AND RECOMMENDATIONS

From the study we found by secondary data analysis (qualitative and quantitative) and from the field survey study, it can be said that microfinance is one of the tools, which contributes significantly to reduce human poverty more than income poverty. The data analysis showed that microcredit has made a significant contribution to reduce human poverty by giving credit, increasing income sectors. But the important questions, which still remain unanswered, are that to what extent microcredit reduces income poverty by generating

income. Further study can try to find out these answers through field surveys for the better availability of data.

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