ECONOMICS AND SOCIAL IMPACT OF MICROFINANCE ON RURAL HOUSEHOLDS

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Introduction

Financial service sector is one of the key elements that plays vital role in controlling and determining the economic growth of a country. Financial service institutions primarily generate capital by means of deposits and lend or invest it on economic activities. During 1950s and 1960s, it was felt that the usual financial institutions were unable to reach the population in the grass root level (Husain, 1999), where the financial services are expected by the needy people. As a response to this situation, there were new developments in the sector all over the developing parts of the world, which is known as 'Micro Finance'.

The word microfinance is being used very often in development vocabulary today and has become very important in global poverty reduction debates. In recent years, micro finance has gained growing recognition as an effective tool in improving the quality of life and living standards of very poor people. This recognition has given rise to a movement that now has a global outreach and has penetrated in the remote rural areas, besides slums and towns.

The term Microfinance refers to "the provision of a broad range of financial services such as deposits, loans, payment services, money transfers and insurance to poor low income households and their micro enterprises'. (Asian Development Bank) The idea of providing credit to the poor as a tool for increasing their income and thereby reducing poverty is not new. What is new is in microfinance is the innovative methods of providing credit to the poor. (eg. Usage of social collateral such as group guarantee instead of physical collateral, progressive lending approach, peer pressure and peer monitoring), mobilization of savings from the poor and linking credit provisions to savings, social mobilization process that involves awareness building and formation of self-help groups and provision of other services such as insurance to cover risks and distresses faced by the poor.

in reducing poverty. Many policy makers are therefore engaged on how to make microfinance sustainable and available to many poor households in the future Other donor organizations that embrace "best practice microfinance" include, United States Agency for International Development

(USAID) and the United Nations Development Programme (UNDP) among other key donors. The popular assumption is that enabling poor households access to credit, helps households begin micro entrepreneurship which would enable them improve their incomes and eventually escape poverty. However, evidence from research so far has been scanty, and many results have been highly contested.

Methadology

Literature review is the main data accumulation methods in this research .Data analysis and conclusions in this research paper had been done in accordance with a comparative approach.

Impact on poverty

Microfinance can be an effective instrument to raise income, production and employment of the poor households. Lack of access to credit has, therefore, been considered as a major obstacle for them to raise their income and production levels. The formal institutions such as banks have bypassed the credit needs of the poor due to lack of credit worthiness, higher transaction cost or perceived higher default rates. The lenders in the informal sector are often considered to charge exorbitant rates of interest. Therefore, in the developing countries the concept of microfinance is being used as an effective tool to alleviate the poverty.

The poverty is the one of the major problems that is faced by the third world countries. It is widely accepted that one major cause of poverty in developing countries is lack of access to productive capital, with formal financial institutions mostly excluding the poor in their lending activities (Chirwa, 2002). One strategy in many developing countries has been to implement Microfinance programs to offer credit to the poor. Through a number of impact analyses it has been proved at international levels that Microfinance programs contribute to the achievement of several aspects of the Millennium Development Goals (MDGs) including poverty reduction; and from the success stories of countries like Bangladesh, many developing countries have formally introduced microfinance as one of the interventions to reduce poverty.

Many studies have also found that microfinance is relevant to poverty reduction not just for the beneficiaries but also there are positive spillover effects to the rest of the community (Khandker 2003). In his study Khandker (2006) uses a panel household survey from Bangladesh and observes that access to microfinance contributes to poverty reduction, especially for female participants, and to the overall poverty reduction at the village level. Pitt and Khandker (1998) find using data from three programs in rural Bangladesh, that borrowing from group-lending schemes increased consumption of poor households. There are also other studies that seem to support to some extent the relevance of microfinance in poverty reduction.

Micro finance does not only provide financial assistances to the poor but also it generates employment opportunities which make them so independent and promotes income. Morduch (1999) argues that microfinance has had positive impact on poverty reduction. However, he is keen to add that "Even in the best of circumstances, credit from microfinance programs helps find self-employment activities that most often supplement income for borrowers rather than drive fundamental shifts in employment patterns. It (microfinance) rarely generates new jobs for others and success has been especially limited in regions with highly seasonal income patterns and low population densities (Morduch 1999)". Thus, it is argued that microfinance, by providing financial services to individuals, households and micro-entrepreneurs, promotes income and employment generation opportunities for the poor.

Impact on Social empowerment

In addition to its economic impact, Micro finance has an impact on the social aspect. Changes in the physical, social and human assets that arise from micro finance activities will affect community's production, consumption and management of resources. Interventions have an impact on social relations partly through their economic effects. In many instances implementers of Micro Finance have claimed that the work will lead to progressive social change. For example by empowering women and changing gender relations in the household and in the community (Ackerly, 1995)

Tackling poverty has taken a new and broader dimension which advocates that increasing income and savings and helping build assets are not the only means to combat poverty. Consider the World Bank's (World Bank 1980, in Rawson 2001) definition of poverty: 'a condition of life so characterized by malnutrition, illiteracy, and disease as to be beneath any reasonable definition of human decency'. Quite evidently, this definition does not mention anything about material gains, income, savings or assets; it focuses more on the state of poverty: it refers to human rather than income poverty, which points to a multidimensional concept going beyond the mere shortage in income, unemployment or scarcity of resources, but extends to deprivations in areas of essential healthcare, sanitation and basic hygiene, gender weakness and repression, illiteracy, infant mortality, food and malnutrition, etc.

Conclusion

There is ample evidence to support the positive impact of microfinance on poverty reduction. In particular, there is overwhelming evidence substantiating a beneficial effect on income smoothing and increases to income. There is less evidence to support a positive impact on health, nutritional status and increases to primary schooling attendance. The rigorous impact studies of microcredit conducted in the past 10 years show mixed results regarding impact on income and expenditure. Some studies show a significant, positive impact on beneficiaries while others show no significant impact. Nevertheless, the evidence that does exist is largely positive.

Empirical indications are that the poorest can benefit from microfinance from both an economic and social well-being point-of-view, and that this can be done without jeopardizing the financial sustainability of the Micro Finance Institutions. While there are many biases presented in the literature against extending microfinance to the poorest, there is little empirical evidence to support this position. However, if microfinance is to be used, specific targeting of the poorest will be necessary. Without this, Micro Finance Institutions are unlikely to create programs suitable for and focused on that group.

Micro credit programs, thus, assume significance since they facilitate poverty reduction through promotion of sustainable livelihoods and bring about empowerment through social and collective action at the grassroots. In addition, micro finance interventions lead to increased social interaction for poor within their households and in the community, besides, greater mobility that increases their self-worth and self-assertion in the social circle. It has been realized as an effective tool and a development approach to reduce poverty worldwide. There are successful Microfinance interventions in poverty-stricken areas of South and East Asia, Africa and Latin America. Hussain (1999) estimates that about nine million poor people in the world have taken collateral free loans from different Microfinance Institutions (MFI). There are appreciations as well as critical views about Microfinance interventions. But in overall, the Microfinance Industry is growing all over the world and the figures outstretch of successive periods are the evidence for the growth(Daley-Harris,2006;UNCDF,2006).

More research should therefore be directed towards not just specific results but also the context within which particular results are expected. What worked in a particular socio cultural and economic context may not necessarily work the same if the socio cultural and economic conditions are changed in another context. This kind of focus for future research will contribute more to knowledge, for the purposes of policy. Also it was emphasized by several researchers that repayment of loan is the crucial for the success of microfinance programs. Therefore further researches should be more focused on loan repayment systems.

Therefore, while much debate remains about the impact of microfinance projects on poverty, we have seen that when MFIs understand the needs of the poor and try to meet these needs, projects can have a positive impact on reducing the vulnerability, not just of the poor, but also of the poorest in society.

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