EFFICIENCY IN SOCIAL PERFORMANCE MANAGEMENT OF MICROFINANCE INSTITUTIONS: A CASE OF PAKISTAN

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EFFICIENCY IN SOCIAL PERFORMANCE MANAGEMENT OF MICROFINANCE INSTITUTIONS: A CASE OF PAKISTAN

by

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DEDICATION

I dedicate my whole efforts to my beloved husband Dr.Arslan Kibreay and my lovely daughters Inaya Noor and Meerha Noor.

Moreover, to my loving father Riaz Ahmad Tarar who has always been a source of inspiration and guidance for me, to my sweet mother Zahida Riaz and siblings Ayesha, Sadia, Mona and Tayyab.

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ABBREVIATIONS

AKRSP	Agha Khan Rural Support Program
ADB	Asian Development Bank
ASS	Assets
ALB	Average loan balance
BLUE	Best linear unbiased estimators
BOD	Board of Directors
CCR	Charnes, Cooper, Rhodes Model
CGPA	Cumulative group for poor assistance
CPB	Cost per borrowers
DEA	Data Envelopment Analysis
DMU	Decision making Unit
DFA	Distribution Free Analysis
EIU	Economic Intelligence Unit
FE	Financial Efficiency
FP	Financial Performance
FDH	Free Disposal Hull
FSS	Financial Self-Sufficiency
F-EXP	Financial Expenses
FIN-MAR	Financial Margin
F-EXP	Financial Expenditure
GOP	Government of Pakistan
GB	Grameen Bank

GBP	Grameen Bank Project
GLP	Gross Loan Portfolio
GNI	Gross National Income
HRM	Human Resource Management polices
KB	Khushali Bank
TL-OFF	Loan officers
MF	Microfinance
ML	Maximum Likelihood
MFBs	Microfinance Banks
MIX	Microfinance Information eXchange
MFPs	Microfinance Providers
MFIs	Microfinance Institutions
MFPs	Microfinance Providers
NRSP	National Rural Support Program
NLCL	Network Leasing Corporation Limited
NBFI	Non-Banking Finance Leasing
NGO-MFIs	Non-government microfinance institutions
NGOs	Non-Government Organizations
OSS	Operational Self Sufficiency
OPP	Orangi Pilot Project
OLP	ORIX Leasing Pakistan Limited
OLS	Ordinary least square
PPSB	Pakistan Post Savings Bank

POs	Post offices
PRSP	Punjab Rural Support Program
PPAF	Poverty Alleviation Fund
PKR	Pakistan Rupee
ROA	Return on Assets
ROSCAs	Rotating Savings and Credit Associations
RSPs	Rural Support Program
SRSP	Sarhad Rural Support Program
SE	Social Efficiency
SP	Social Performance
SPM	Social Performance Management
SPTF	Social Performance Task Force
SBP	State Bank of Pakistan
SFA	Stochastic Frontier Analysis
SDI	Subsidy Dependence Index
TFA	Thick Frontier Analysis
TE	Technical Efficiency Scores
TADM-EXP	Total administrative expenditures
USSPM	Universal Standard for Social Performance Management
VIF	Variance inflation factors

KECEKAPAN DALAM PENGURUSAN PRESTASI SOSIAL INSTITUSI PEMBIAYAAN MIKRO: KAJIAN KES DI PAKISTAN

ABSTRAK

Industri pembiayaan mikro di Pakistan telah menunjukkan perkembangan dan pertumbuhan yang berterusan sejak beberapa tahun yang lalu dan peminjam dalam kalangan wanita terus mendominasi penguasaan pasaran. Walaupun industri pembiayaan mikro berada dalam keadaan yang memberangsangkan dengan sokongan yang berterusan daripada penyumbang, namun sektor ini masih gagal untuk menangani masalah kemiskinan yang dihadapi oleh rakyat Pakistan. Meskipun digambarkan sebagai sebuah negara miskin, namun sumbangan sebanyak 11.5 peratus daripada sektor pembiayaan mikro masih tidak berupaya untuk membasmi kemiskinan. Mengapa paradoks ini timbul? Oleh yang demikian, kajian ini telah direka untuk menganalisis senario dan mempersoalkan kemampuan sektor pembiayaan mikro di negara ini. Objektif utama kajian ini adalah untuk menilai Kecekapan Kewangan (FE), Kecekapan Sosial (SE), untuk mencadangkan hubungan antara FE dan SE, dan Pengurusan Prestasi Sosial (SPM) daripada institusi kewangan mikro (MFI) di Pakistan. Bagi menjawab persoalan kajian; pendekatan kaedah campuran digunakan. Analisis *Stochastic Frontier* melalui pendekatan ekonometrik digunakan untuk menganalisis kestabilan kewangan serta status kecekapan sosial institusi yang berdasarkan skor kecekapan teknikal. Penentu kecekapan kewangan dan kecekapan sosial dan hubungan jangkaan antara FE dan SE juga dinilai menggunakan kaedah yang sama. Sebaliknya, untuk menilai fokus SPM industri, 15 pihak berkepentingan telah ditemu bual berdasarkan pendekatan kualitatif, iaitu dengan menggunakan teknik temu bual semi-struktur. Hasil kajian menunjukkan bahawa prestasi

industri adalah memuaskan, tetapi kurang daripada tingkat optimum kerana sumber potensi tidak digunakan sepenuhnya. Tambahan pula, prestasi sosial adalah lebih baik berbanding prestasi kewangan dan terdapat hubungan positif antara kedua-dua prestasi. Manakala melalui petunjuk SPM, pendapatan daripada industri adalah rendah tetapi memuaskan kerana terdapat beberapa petunjuk telah memberikan keputusan yang baik dan sedang dilaksanakan dalam industri. Selain itu, dapatan kajian menunjukkan bahawa wujudnya potensi yang besar bagi sesebuah industri untuk berkembang kerana terdapat banyak sumber yang kurang digunakan dan potensi pasaran bagi golongan miskin untuk diteroka. Pembasmian kemiskinan dan kemampanan kewangan adalah satu fenomena kecekapan dan bukan disebabkan oleh kekurangan dalam dasar kerajaan atau struktur ekonomi negara. Selain itu, kecekapan bukanlah titik akhir sebaliknya adalah perkara penting untuk mencapai matlamat sosial. Oleh itu, tumpuan yang lebih besar pada kecekapan MFI boleh menghasilkan keputusan yang lebih baik bagi mencapai sasaran yang dikehendaki. Begitu juga, beberapa inisiatif sedang dilaksanakan bagi meningkatkan implikasi SPM untuk memastikan industri pembiayaan mikro berada pada landasan yang betul dan MFI bertindak balas kepada matlamat FE dan SE dengan cara yang wajar.

EFFICIENCY IN SOCIAL PERFORMANCE MANAGEMENT OF MICROFINANCE INSTITUTIONS: A CASE OF PAKISTAN

ABSTRACT

The microfinance industry in Pakistan has demonstrated a continuous expansion and growth since few years back and women borrowers persistently dominate the market. Although the microfinance industry is intensively encouraging and attain perpetual support from contributors, but however this sector still fails to address the poverty problems faced by the people of Pakistan. Portrayed as a poor country, although there is a contribution of 11.5 percent of the microfinance sector, it is still insufficient to eradicate poverty. Why this paradox arises? Hence, this study has been designed to analyze the scenario and question the ability of the microfinance sector in this country. The main objective of this study is to evaluate the Financial Efficiency (FE), Social Efficiency (SE), to propose the relationship between FE and SE, and Social Performance Management (SPM) of the microfinance institutions (MFIs) in Pakistan. In order to answer the questions; a mixed method approach is applied. Stochastic Frontier Analysis, an econometric approach is used to analyze the financial stability as well as the social efficiency status of the institutions based on their technical efficiency scores. The determinant of financial and social efficiency and expected relationship between FE and SE is also being evaluated by the same method. On the other hand, in order to assess the SPM focus of the industry, 15 stakeholders have been interviewed based on a qualitative approach, i.e. by using semi-structured interview tool. The findings illustrate that industry performance was satisfactory, but less than the optimum level due to underutilizing its

potential resources. Furthermore, the social performance is better than financial performance and there is a positive association between both performances. While through the SPM indicators, the earnings from the industry is less, but satisfactory since there are some indicators has given good results and being implemented in the industry. Apart from that, findings reveal that there is an enormous potential in the industry to grow as there is plenty of underutilized resources and market potential for the poor to explore. Both poverty alleviation and financial sustainability is a competency phenomenon and not due to lacking in government policies or structure of the economy. Moreover, efficiency is not the end, but rather it is crucial in achieving social goals. Hence, a greater focus on the efficiency of MFIs may produce better results in order to achieve the required targets. Similarly, several initiatives being implemented to improve SPM implication in order to ensure the microfinance industry is on the right path and MFIs are responding to FE and SE goals in a sensible way.

CHAPTER ONE

INTRODUCTION

1.0 Introduction

The industry of microfinance (MF) has proven itself as an attractive business option, with more than 90% repayment rate, as well as an effective tool for poverty alleviation, (Weinberg, 2008). Muhammad Yunus, realized after the food shortage in Bangladesh in 1974s' that it is hard to instruct the usefulness of economic theory whilst the reality of poor conditions contradict to those theories (Yunus, 2003). Hence, believing the idea that giving the opportunity to poor will let them to be "architects of their own fate" originates microfinance. The entire tribute for this new paradigm of microfinance goes to Dr.Yunus. The impression of microfinance can be confined in common phrases like "a hand up, not a hand out" or "teaching one to fish."

Both the limits of income-generating opportunities and ability to respond to such opportunities are determined to a great degree to the access of affordable financial services. Increasing the access to poor households to MF is therefore being actively pursued internationally and would appear to have become the mantra of today's development orthodoxy. Once almost exclusively the domain of donors and experimental projects, MF has evolved during the last decade with prospects of viability, offering a broader range of services, and significant opportunities for expansion. Development practitioners, policy makers, and multilateral and bilateral lenders, recognize that providing efficient MF services is important for variety of reasons.

Improved access to MF services can enable the poor to smoothen their consumption, manage their risks better, build their assets, develop their micro-enterprises, enhance their income earning capacity, and enjoy an improved quality of life.

While poverty is a curse, poor economic performance is slavery. Poverty yields individual human indignity, and economic decline causes national misery. Therefore, it is no wonder that many great philosophers, economists and social activists have been pressing for the alleviation of poverty and acceleration of economic growth. However, the quality of life and economic growth have circular cause and effect relationship with human dignity, education, healthy living, skills and business opportunities. Unfortunately, one third of the world's population is still suffering from hunger, draught and lack of basic necessities of life.

The governments in the third world are waging a war against poverty through the microcredit scheme. Microfinance program is being used as an instrument for poverty alleviation, employment generation and economic revival. To help the poor this movement is revolutionizing international development, and the governments with microcredit facilities.

Globalization and free market system has provided the upper hand to the developed countries. At the same time, natural tendencies in the free market system have brought about an enormous concentration of economic gains in very few hands. Despite the great social and technological strides of the past a few decades, the absolute number of poor people on the globe has never been decreased. More than a billion people live on a less than 1$ a day. Every day, one hundred thousand people enter the global labor force, but only one in five is expected to find a formal employment. The persistence of mass unemployment and poverty remain the most pressing problems in the world. Even as we witness the fall of authoritarian regimes and the burgeoning democracy throughout the globe, one third of the world's population has yet to attain the most rudimentary levels of economic wellbeing and security in their lives.

In this situation, microcredit seems to be essential for the alleviation of poverty and revival of economic growth in part through promoting human settlements, education, agriculture, skill development, small business, and healthy living. A key ingredient of poverty alleviation is human dignity. These programs ensure human dignity through pledge free loans, simple procedures, new social contract, right to counseling, fair earning, and is devoid of bureaucratization. In the current global economic climate, microcredit is a remarkable poverty alleviation tool.

The concept of microfinance is not a merely newly born as it is considered; it has been practiced in different forms and mode among poor communities for centuries in order to fulfill the pertinent demand of credit. The modern definition and application came to scene at the end of last century and afterward this notion is continuously under discussion. Debates are going on in reference to its optimistic and pessimistic consequences having with a lot of interpretation and arguments. It had gained popularity due to its promise to help the poor while keeping their dignity and self-respect.

1.1 Background of the Study

This research study intends to analyze the performance/efficiency of microfinance industry in Pakistan from diverse prospective; including financial performance/efficiency (FE), social performance/ efficiency (SE) and social performance management (SPM). Hence, this section of the study introduces the concept of microfinance and its evolution, financial performance/efficiency in microfinance, social performance/efficiency in microfinance, social performance management and background of the economy and microfinance in Pakistan.

1.1.1 What is microfinance?

Microfinance is a unique type of aid, granting to the poor in the shape of cheap credit when they are unable to manage it from their own resources. Aghion & Morduch (2005) recognized microfinance as an activity of small financial support to develop and facilitate scarce resource to embark on self-employment and financial strengthening and to commence small entrepreneurial conduct, granted to a particular group of individuals. Currently, microfinance modified into more than plain credit dealing to stipulation of advance financial services. Asian Development Bank (ADB) formally defined microfinance as:

"*The consistent stipulation of a wide array of financial services to poor that comprises of deposits, loan Payment, money transfers, insurance and many other services related to microenterprises*".

The perception of microfinance has gone through the evolutionary process in implication and programs[1] since the time of its initiation in 1976. It is modified from the basic deliverance of small loans without collateral or with little guarantee occasionally to the advanced methods of group lending, saving and insurance conveniences, and continuous access to quality and affordable financial services[2] to finance low income community for income generation and better living standard.

The composition of microfinance institution (MFIs) consists of formal as well as semi-formal and informal association, banks, rural banks and cooperatives, non-government and government organization, respectively. They can be distinguished on the basis of products or services they choose to offer to clients. For instance, one group of MFIs may focus the maximization of operational efficiency and prefers to offer only financial range of services to their customers primarily in the shape of small loans. Whereas, other groups of MFIs may decide on to consider complementary way of economic and social development within their horizon offering auxiliary services beyond standard credit products, such as life insurance products, educational programs, and direct health care, etc (Microfinance Gateway, CGAP).

In short, the industry of microfinance has shown a tremendous enlargement during the last two decades; Cedric Lutzenkirchen & Weistroffer (2012) reported the expansion in microcredit disbursement through MFIs by the end of 2010, around more than 200

[1] Programmes consist of the provision of subsidized credits, development of rural and community banks, the liberalization of the financial sector, establishment of different types of non-bank financial institutions including savings and loans companies, finance houses, and credit unions etc (Microfinance gateway)
[2] These services include savings, credit, insurance, remittances, payments, money transfers, and other financial products (Microfinance gateway).

million clients and its impact on the lives of poor around 1 million clients in developing world.

"*There are likely 10,000 MFIs, of which 3,652 are accounting for 205 million clients, and 2,000 MFIs accounting for 100 million clients*" (p. 4), while the rest of MFIs did not report.

Over the last few years, this industry has experienced the distinguished intensification in terms of number of borrowers and assets volume showing a constant return on assets of 2-3%.

1.1.2 Evolution of Microfinance Industry

The evolution of microfinance attributed to the informal reinforcement of special type of banking to the poor (during 80's and 90's) in European world, which initially played a role as financial intermediation between micro savings and microcredit. Nonetheless, Asian world is demonstrating a longer history regarding microfinance operation. Several societies have been working in this region since centuries; For Example, in China-Hui, India-Chitfunds, Indonesia-Arisan, Phillipines-Palugwagan, Ghana-Susus, Mexico-Tandas, Sri-Lanka-Cheetu, in West Africa-Tontines, and Bolivia- Pasanaku (Seibel, 2005 and Global Envision, 2006).

Digging into the Asian, African and European history of rural microfinance, Seibel (2005), found that in Nigeria microfinance was subsisted at least as early as 500 years back in the shape of rotating savings and credit associations, named "Enusu". Whereas, in India foundation of microfinance and banking dates back to 3000 years, had three main strands; moneylenders, chit funds/rotating savings & credit associations (ROSCAs), and merchant bankers.

After several alterations and episode of the hit and crash, at last, the contemporary concept of microfinance came into front in 1976, not deliberately. This happened in 1974, when Muhammad Yunas lent only US$ 27 to the poor in Jobra (Bangladesh) to provide them interest free credit. The successful recovery of his loan and an experimental project Grameen Bank Project (GBP) became the base of microfinance execution. GBP transformed into Grameen Bank (GB) afterward, and became the reason of beginning of this concept formally. GB principally endeavoured to provide microfinance support to the deprived individuals; Besides, it acquired the burden of generating public resources to realize its invariable objective of poverty reduction. Ultimately, after three decades of persistent struggle GB has established the concept of bottom-up microfinance approach, which raised the underserved from scarcity and guaranteed a sustainable expansion. Moreover, poor rural women accessed a possibility of acquiring skills and a sustainable upgrading in their living with self-respect and self-reliance, owing to participatory, peer supported and multi segment strategy of microfinance. (Grameen Bank, 2010).

Now generally speaking more than ten thousand organizations, in more than sixty countries around the world, are working for microfinance programs, and around fifty million people worldwide are receiving the benefits of such loans. GB in Bangladesh, ACCION International in Latin America, and many other global NGOs are playing very important roles in the economic revival and poverty alleviation through the provision of small loans (Global Envision, 2010). GB has lent more than $2 billion, and ACCION International has $485 million to 310,000 to low-income entrepreneurs in different countries during the last decade (Microfinance Information Exchange). Microfinance is one of the major innovations in the past 30 years, the annual spending on this main innovation in the past a few years is amounted between US$800 million and $1.5 billion worldwide (Hartarska & Holtmann, 2010).

1.1.3 Financial Performance in Microfinance

The notion of performance has been employed extensively in different connotation in different discipline. A general attribute of performance is its sound mechanism that helps to achieve the objectives. Performance of an organization is about; how well the organization is managed, and organization's value that it carries for customers and other stakeholders" (Moullin ,2007). Organizational performance has two dimensions such as "effectiveness and efficiency" effectiveness is organizational goal while efficiency is the way to achieve this goal in an optimal way (Neely, Adams, and Kennerley, 2002).

Financial performance of an organization is also defined as "the capability to face costs and to maintain function without having option of gifts, subsidies and debt relief (Crombrugghe et al., 2008).

Regarding microfinance, the ability of microfinance institutions (MFIs) to get better loan payments, face operating cost and well-organized use of resources to accomplish organization goal correspond to financial performance, it enables MFIs to develop into operationally self-sustainable, that happens considering financial revenues or/and minimizing cost.

The most enviable and perhaps the most valuable approach for MFIs is to lessen the prevalence of absolute poverty via generating self-employment prospect, and upgrade the socioeconomic wellbeing of the poor communities through targeting the financially marginalized communities in a financially efficient way. In this way, self-sufficiency and profitability of MFIs will be guaranteed. Whereas, the insufficiency of MFIs in terms of lower financial performance will probably mess up the two-fold target of microfinance; enriching the well-being of the poor communities socioeconomically and commercial success of the MFIs. Hence, exploration of the financial performance/efficiency of MFIs help to yield the most constructive approach for sponsoring the non-bankable poor in a successful way.

1.1.4 Social Performance in Microfinance

In the perspective of microfinance, social efficiency refers to those activities of MFIs that fundamentally instigate to augment the socioeconomic welfare of patrons in operational areas of an MFI (Nieto, 2009). The MFIs having social motives focus more on the poor as compared to profit, although financial sustainability remains the part of their objectives also. This characteristic draws a line of segregation between MFIs and conventional banks (Gutiérrez et al., 2007).

Since last decade, the microfinance industry has given more importance to the transformed thought of social performance as compared to financial performance. The twofold foundation intuition proposed that a MFI should endeavor at becoming both a sustainable commercial institution (indicating financial performance) and a driving force for social development (indicating social performance) (Tulchin, 2003; Copestake et al., 2005). Recently, MFIs faced the pressure especially from donors, governments and shareholders to present evidence that microfinance services are actually sustainable to support the poor in their economic progress. Therefore, the increasing digit of inventiveness to measure social performance is the heightened interest in the industry.

Social performance configure is regarded as aspiration at structuring microfinance more valuable in realizing its social mission. So far, social performance incorporation into MFI philosophy and procedure has been uneven. A number of microfinance players consider it as a development device accordingly social performance have been evaluated generally in the course of outreach[3] (including depth of outreach) and impact assessments. While, impact assessment was based on client-based impact that revealed the benefits reached to poor by MFI services (Zeller & Meyer, 2002) and the wider impact assessments revealed the benefits to the society.

Apart from it, there are a few microfinance players who consider the process approach ampler in estimating social performance and valuable to MFIs. The procedure and actions of an MFI are examined by process approach direct to social impact. Similarly, for a number of others, assessment of social performance has wider connotation. It helps MFIs to assess their products that are adapted to clients' needs and about the

[3] Outreach refers to the number of poor reached who were previously considered as bankable by formal institutions while the depth of outreach refers to the level of poverty and exclusion by MFIs.

institution's contribution to improve the social situation of its clients. It may plead with organizations to be more watchful of achieving their affirmed social mission and objectives particularly nowadays when more and more MFIs are converting into banks.

Hence, analyzing the social performance of MFIs help to promote the rural and agricultural development with excellent social outcomes, these programs may have moderate financial return, but it will be justifiable to obtain support expecting that they will become sustainable at a gradual rate. Furthermore, it may allocate MFIs to exhibit social performance and transparency, directing to donors and investors for reallocation of funds towards socially oriented MFIs and give a helping hand to them in making resolution about which institutions still need subsidies.

1.1.5 Social Performance Management in Microfinance

As discussed in the last section, in the previous a few years the client in the microfinance has occupied the central position. The requirement of client protection with accountable finance and social performance came up to the scene as a repercussion of a few catastrophes[4] in microfinance industry. The growth-related dilemma and failure of client focus experienced in several countries globally originated a move to make certain that client protection and social performance ideology are compactly entrenched in microfinance sector. These initiatives appeared in the arrangement of designing, executing, and measuring tools for assessing consumer protection.

[4] for example; Andhra Pradesh (AP) crisis in India.

Apart from that, tools were also required to be duly taken up by the MFIs to assess whether social performance principles have been incorporated in governance and operational systems, whether staff behavior is accustomed to field sensitivities, whether basket of products are in accordance with the customers' requirements and whether the MFIs are achieving what they set out to achieve. As a whole, considering the benchmark to design these tools, the Social Performance Task Force (SPTF), SMART Campaign and Microcredit Summit are keenly engaged in several parts of the world for the solution of these problems. Hence, after several hit and trial methods currently in the sector, social indicators and yardstick are available against which MFI can measure their performances. SPTF defines social performance as;

"The useful conversion of an institution's social mission into practice in accordance to established social values such as serving larger numbers of poor and excluded people, improving the quality and appropriateness of financial services, creating benefits for clients, and improving social responsibility of an MFI"(p.3).

Social Performance Task Force (SPTF) and Microfinance Information Exchange (MIX) have formulated 11 indicators to quantify the social performance of microfinance institutions (MFIs). These particular indicators are used to accumulate social performance data from MFIs around the world and to provide a platform for benchmarking and analysis of these MFIs as well.

Industry stakeholders have established consensus on these standards as well as on this core set of 11 social performance indicators (reference Appendix D). MIX has integrated this core set into its reporting platform that can enhance the transparency on social performance and help retail providers to benchmark themselves and improve practices over time.

The implementation of this Universal Standards for Social Performance Management (USSPM), and their integration on the MIX reporting platform, stand for a significant landmark in creating universal industry standards in microfinance. These developments are the outcome of numerous feedbacks to develop the SPM content and quality in the sector. Due recognition of the positive and responsible role played by some of the MFIs would be a good starting point to search good practices in Social Performance Management.

1.1.6 Economy of Pakistan

According to Government of Pakistan (GOP) Survey report 2013-2014, probable population of Pakistan was accounted around 190.7 million. It was shown that it might touch the figure of 205 million by 2020 resting on 2.03 percent average annual growth rate. Pakistan stands at the sixth position among most populous country in the world even though it has controlled its birth rate. Total urbanized population is 36 percent of the total population while the rest 74% approximately are still living in rural areas (GOP, 2014). Total area is 796,095 square kilometers having 214 people per square kilometer population density depicting 2 percent of the world’s inhabitants breathing on less than 0.7 percent of the world’s territory (The Library of Congress 2010).

The economic and political situation in Pakistan is extremely miserable though it has started a revival in recent year. According to provisional estimates the GDP growth was 4.24 percent during 2014-15 as compared to 4.03 percent in 2012-13 revised estimates. The per capita income was 1,512 in 2014-15 in dollar terms that increased from $ 1,333 in 2012-13. Fiscal deficit was restricted to 3.8 percent and Government borrowing for budgetary support stood at Rs. 601.1 billion during 2014-15 against Rs. 240.2 billion in the same period of fiscal year 2013-14. During July-April 2014-15, Consumer Price Index (CPI) was averaged at 4.8 percent against 8.7 percent in the same period of last year. The current account deficit in 2014-15 stood at US$ 1.4 as compared to the deficit of US$ 2.9 billion in Jul-Apr 2013-14, showing remarkable improvement. However, documented Public debt was Rs. 16,936 billion or 61.8 percent of GDP as at the end of March 2015.

Since independence, Pakistan has been facing great challenges of survival due to weak economic base. It has to confront several issues simultaneously ranging from regional conflicts, economic crises, natural disasters, governance issues, conflicts with adjacent countries, etc. At the same time inherent issues within the structure of the economy cannot be ignored such as corruption, nepotism, misusage of resources and powers, political instability, violence, terrorism and almost no accountability and poor governance. The exceedingly unstable security situation, rising energy shortage, a weak tax structure, declining trade share with a declining investment in a deteriorating economy, and food price inflation are worsening the situation day by day and causing the major threats to the stability of this nation. In addition to all these issues rising poverty in Pakistan is a big concern.

Besides having low income, the poor people in Pakistan also lack access to basic needs such as health, clean water, education and proper sanitation. This deprivation and lack of access to these facilities decreases their potential and opportunities. All this results in their social exclusion, vulnerability and exposure to many social exogenous risks. The vicious circle of poverty further perpetuates when these poor are not considered at the time of making policy decisions.

By the ADB's estimates, as cited by the Ministry of Finance, every 10% increase in food prices pushes 2.2% of Pakistan's population below the poverty line. The Ministry estimates that food prices have risen 94% since its last poverty survey in 2011. If the ADB's estimates hold across several years, poverty in Pakistan has increased to an astonishing 43%. Data from the Finance Ministry suggest that nearly 75% of the population lives very close to the poverty line. Since the last poverty survey in 2011, "there are no new figures on poverty," said Finance Secretary, Waqar Masood, during a press conference that marked the release of the Economic Survey 2013.

Poverty in Pakistan is deep rooted and multifaceted, it eradication has become a challenge for every government. In spite of substantial caution from beginning to end in a mixture of poverty alleviation programs, it still seems hard to combat the pervasive social and economic poverty in the country.

Among all the well-known strategies to defeat poverty, microfinance has been considered as one of the most influential weapons in the fight against poverty due to its plain and effectual structure (Roodman, 2012). Several studies (Baido, 2008; Johansen

& Nilsson, 2007) at the international level as well as in Pakistan (Qayyum and Ahmad, 2006; Tariq and Ahmed ,2010) have proven the verity of microfinance as an appropriate technique to empower the underprivileged and to enlarge their earning propensity. The success of microfinance is attributed to its fundamental role of easy credit provision to the poor, economically active but financially constrained, that had been ignored by the commercial banking sector. Moreover, microfinance supportive services have revealed a sound effect on the domestic level of the poor that lead to the economic development.

1.1.7 Microfinance in Pakistan

Microfinance in Pakistan emerged as a promising segment, developing at a faster speed by means of innovative contestant and products. Though microfinance sectors are considered only formal organizations for services to poor, nevertheless apart from these formal institutes there are also some informal traditions through which poor people employ themselves in financial activities, such as Rotating Savings and Credit Associations (ROSCAs), moneylenders, and stores that are most popular informal method of financing amongst them. Although Microfinance in Pakistan dates back to the 1960s when Comilla Project was experimented with microcredit initiatives yet it gains popularity in the current decades owing to adopting new strategies and active participation by the State Bank of Pakistan(SBP) for the improvement of this sector.

Microfinance sector in Pakistan operates in both formal and informal markets. The informal marketplace comprises the feature of high interest rates, prevalent expense, segmentation, and a large gap between loan and deposit rates. Nevertheless, it is popular among poor communities. Formal schemes are structured yet poor consider its modus operandi hard to follow. There are various formal and informal microfinance providers (MFPs) in Pakistan; we divide MFPs based on its characteristics into different classes. The figure 1.1 will make the classification easy to understand;

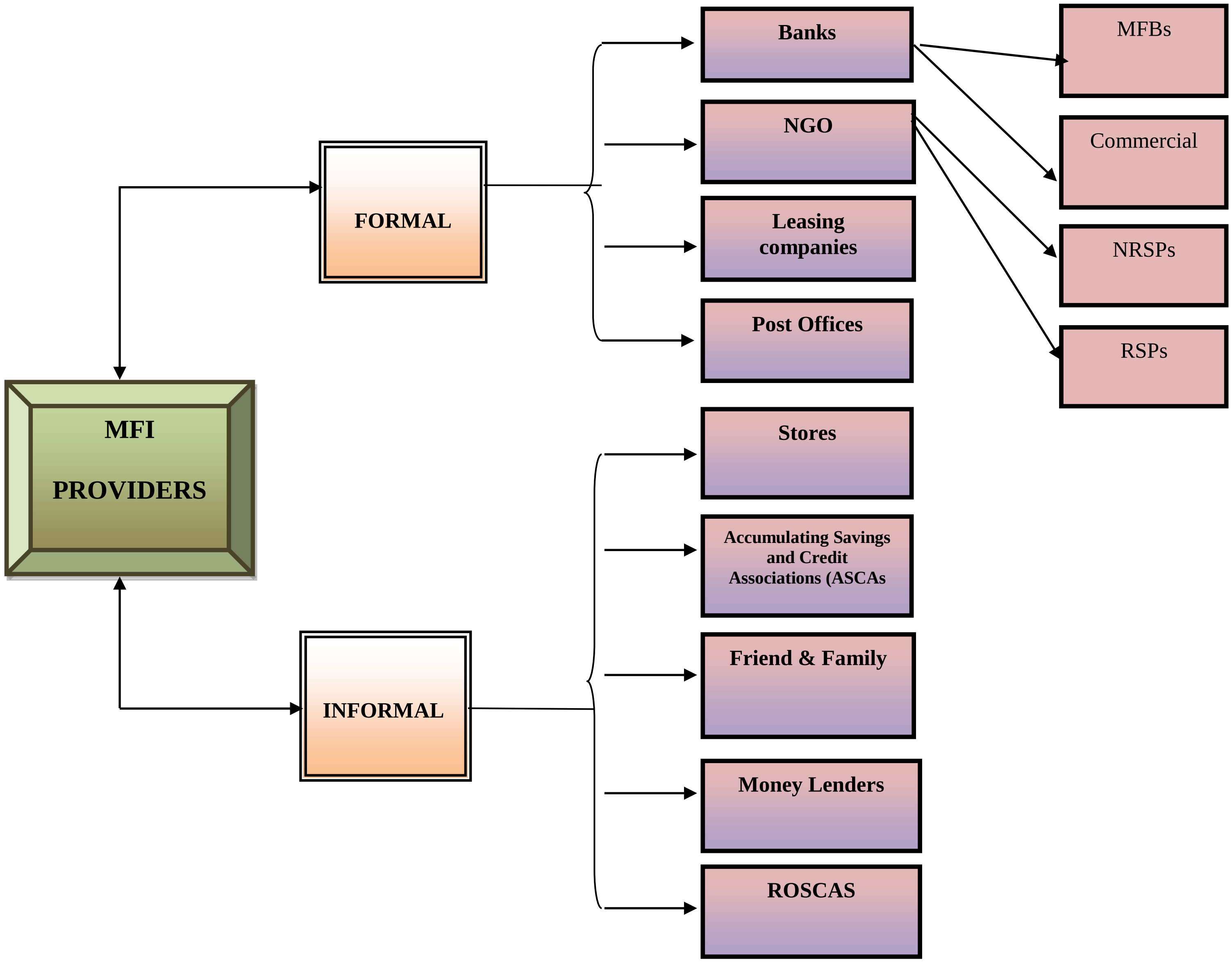

Figure 1.1 Classification of microfinance provider in Pakistan

1.1.7 (a)Formal Microfinance Providers

a) *Non-Government-Organizations (NGOs)*

According to the Pakistan Microfinance Review, 2013, there are three groups of NGOs working in Pakistan. This classification is based on their working at Regional, District and Village levels.

i-Group 1

Group 1 comprises the NGO's working at national level.Regional-Rural-Support Programs are among the prominent groups of NGOs. The first NGO in this group is the Aga Khan Rural Support Program (AKRSP)working in the Frontier and Northern Areas. The Government of Pakistan established National Rural Support Program (NRSP) stimulated by AKRSP, based on the same model of AKRSP. NRSP operates all over the country; further division is based on the geographical provinces of Pakistan known as Punjab Rural support program (PRSP), Sarhad Rural Support Program (SRSP) etc. All these Rural Support Programs (RSPs) are operating by establishing the organizations of 20 to 40 people, village or community based, that are the distribution channels for a wide range of economic and social development programs. RSPs are particular type of not-for-profit rural development organizations that together have a large range all over the country.

ii-Group 2

Several District level active NGO's within a province comprises the second group of NGOs. The most popular one includes the Orange Pilot Project (OPP), working in slums in Karachi and the Kashf Foundation that is working in Lahore.

iii-Group 3

The third group consists of thousand-village level NGOs with a small understanding for advance concept of microfinance. These particular NGOs provide only microcredit services. They only provide loans without activating deposits.

b) Microfinance Bank (MFBs)

MFBs have to follow a defined ordinance of a country that is to provide microfinance services to the poor community for the alleviation of poverty (SPB). The GOP recognized 'Khushali Bank' (KB)[5] as first Microfinance bank under the ordinance of KB 2000, to provide the microfinance services in the country. It has MFB set up through a special ordinance. Afterward; it followed the MFIs ordinance 2001[6]. Now, MFBs in Pakistan are licensed following the MFI Ordinance 2001, regulated by SBP. Licenses are permitted for district, regional, provincial, and national level banks that are satisfying the criteria defined in the Ordinance. Size of loan is currently limited to a ceiling of Rs 150,000, savings are permissible to systematize from any shape, services for remittances within the country are also allowed. MFBs working in Pakistan currently include; Kashf Bank, Khushali Bank, NRSP Bank, Network Microfinance Bank, Pak-Oman Microfinance Bank, Rozgar Microfinance Bank, Tameer Microfinance Bank, The First Microfinance Bank, (PMN, 2013).

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[5] This bank was envisaged to strengthen community-based lending activities in collaboration with the existing well-functioning NGOs and by expanding its own branch network.

[6] Ordinance 2001 stated, MFIs has permission for the formation of MFBs following the rules given by SBP.

c) Commercial Banks in Microfinance

Since 2000, soon after the initiative captivated by SBP for microfinance industry expansion, the prudential regulations of SBP has enabled banks to make uncollateralized loans. The customary obstacle of security is no more applicable by hard and fast rule for a smaller loan amount, due to which access to bank finance for micro entrepreneurs is trouble-free now. The chief commercial banks that are offering financial services to micro entrepreneurs in various shapes consist of, Agricultural Development Bank of Pakistan, Bank of Khyber, Bank of Punjab, First Women Bank Ltd, First Investment Bank Ltd, Habib Bank Ltd, and National Bank of Pakistan. The sole purpose of their operation for microfinance is social commitment rather than a business stance (Microfinance Department SBP).

d)Leasing companies in Microfinance

ORIX Leasing Pakistan Limited (OLP) and Network Leasing Corporation Limited (NLCL) are two recognized leasing companies targeting microfinance market, scheduled on the stock exchange index of Pakistan. OLP is prime, older and among one of the most prominent Non-Banking Finance Leasing (NBFI) companies, established on 1986 in Pakistan. It is providing the customers all over the country cost effective value-added products and has been modifying it services for 25 years. It helped to grow several small businesses into medium sized venture that embodies almost 80% of the entire business in the country. Around 100 billion value finance in Pakistani Rupees has been predominantly granted to the small medium enterprises with a practically worthy recovery ratio. The Company's strength has been widely recognized by its paid dividends for 19 years in the range of 10% to 45% and by the buildup of capital growth from Rs. 10 million in 1986 to Rs 2.2 Billion, in shareholders' equity of the Company, until 2011 (ORIX Network).

Network Leasing Corporation Limited (NLCL) is a private leasing as well as Non-Bank Financial institution, regulated by the Securities & Exchange Commission and the State Bank of Pakistan, established in 1993. It is playing a crucial role in the support and development of micro and small enterprises and lease financing of assets to them. The company provides services to the microfinance sector, and work for empowerment of women enterprises. It is a pioneering institution among leasing companies. According to Annual Audit report[7] published in 2002, The Company was in a good position having total assets of amount RS 895.696, net investment in the lease amount RS 531115 and having profit of amount Rs 11,483 (Annual Audit report 2002 NLCL).

d) Post Offices

Post offices (POs) in Pakistan are also serving the poor by supplying small credit and other financial services; including savings, insurance, and remittances thus performing the job of micro financing. All over the country, POs structure comprises of 13,419 and 7,276 branches and bank branches respectively. The Ministry of Finance is utilizing the Pakistan Post Savings Bank (PPSB), as an agent for financial services in some isolated areas of Pakistan, where it might be the only banking service available. In 2004, the

[7] This is the latest audit report which is published and available according to best of our knowledge.

Postal Life Insurance proposed 10 insurance alternatives and reached 252,810 active policies. Whereas, PPSB account holders for several savings schemes reached at 4.6 million in 2013.Recently, Khushali Bank and First Micro Finance Bank have connected their services with POs (SBP Microfinance Division).

e) *Different Schemes*

In Pakistan, some private Banks and Government owned institutions are also providing the services of microfinance under several schemes, however MF is not the main product of their institution. The major schemes working under different institutions are; National Bank of Pakistan-government's Rozgar Scheme, Zarai Taraqaite Bank Limited credit and saving services, and Government owned First Women's Bank Limited is providing special microfinance services. Whereas, the seven National Saving Schemes of the Central Directorate of National Savings (CDNS)[8], Benazir Income Support Program and the Zakat office are offering charitable funds as a social objective (Pakistan Microfinance Network).

1.1.7(b) Informal Microfinance Providers

There is no rule or regulation for informal microfinance providers except that they fulfill the demand of credit for underserved at the time of need. Moneylenders and Store may exploit the poor community by charging a high interest rate but people trust them because of easy and on time availability of credit. ROSCAS is an informal way of saving and group help, to get the credit at the time of credit shortage. Several members join a group, contribute a specified fixed amount of money each month/week (according

[8] CDNC had deposits of about 4 million account holders(PMN)

to cycle decided) and all group members get the total amount of money turn by turn. It is very popular among Pakistan's women.

1.2 Current Scenario of Microfinance in Pakistan

The background of MFIs in Pakistan was primarily non-regulated but after 2000-01 due to the enforcement of microfinance ordinances by SPB, a pattern has emerged for regulation.

There are three peer groups of retail players in overall Pakistan's microfinance industry: microfinance banks (MFBs), non-government microfinance institutions (NGO-MFIs) and rural support programs (RSPs). MFBs are licensed under the Microfinance Institutions Ordinance 2001, and have been working under the regulatory and supervisory framework of SBP. The MFBs has been broadly acknowledged with reference to Pakistan's regulatory framework, for that it got appreciation in 2010 by the Economic Intelligence Unit (EIU) and ranked fifth among 54 countries in terms of the overall environment for doing microfinance business (Microfinance Microwatch Report 2011).

The other two categories, NGOs and RSPs, are scheduled under one of these separate legislative frameworks that include; the Societies Registration Act, 1860, The Voluntary Social Welfare Agencies Ordinance, 1961, The Trust Act, 1882, and the Companies' Ordinance, 1984. There are, at least five types, including 2001 ordinance, of legislative