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MICROFINANCE AND POVERTY REDUCTION IN NIGERIA: A Critical Assessment

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ABSTRACT

This paper attempts to provide a critical assessment of microfinance as a strategy for poverty reduction in Nigeria. It argues that while microfinance has developed some innovative management and business strategies, its impact on poverty reduction remains in doubt. Microfinance, however, certainly plays an important role in providing safety-net and consumption smoothening. However, for any significant dent on poverty, the focus of public policy should be on growth-oriented and equity-enhancing programs, such as broad-based productive employment creation. There is also need to design financial sustainable models that increases outreach and scale up operations for the poor. More so, financial inclusion agenda should be considered and adopted in a concerted manner.

Key words: *Microfinance, Poverty, Nigeria.*

INTRODUCTION

The universal objective of [1]microfinance is to make it possible for large numbers of low-income people to access institutional financial services, hence the potential benefits of microfinance has accounted for its widespread adoption as an economic development, job creation and poverty reduction strategy.

In Nigeria, the microfinance policy regulatory and supervisory framework was launched in December, 2005. The framework provides a roadmap for the participation of stakeholders in microfinance provision. The concept of microfinance was well received in Nigeria, culminating in the conversion of 606 erstwhile community banks to microfinance banks (MFBs) at the end of December, 2007 and licensing of 363 de novo MFBs, resulting in a total of 969 MFBs as at August 31, 2010 (The Nigerian Microfinance Newsletter, 2010). Furthermore, the Microfinance Policy that was launched in 2005 created the framework for licensing, regulation and supervision of privately owned microfinance banks. The policy also provides for the participation of various institutions such as deposit money banks, non-governmental organizations-microfinance institutions and financial cooperatives in the provision of financial services.

The microfinance banks are licensed by the Central Bank of Nigeria (CBN), to conduct microfinance operations such as mobilizing [2]micro-savings and deposits from the public, extending credit and other financial services to them. The institutions are supervised by the CBN and are required to comply with the Supervisory and

[1] Microfinance refers to loans, savings, insurance, transfer services and other financial products targeted at low-income clients.
[2] Micro-savings are deposit services that allow people to store small amounts of money for future use, often without minimum balance requirements. Savings accounts allow households to save small amounts of money to meet unexpected expenses and plan for future investments such as education and old age.

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Regulatory Guidelines for MFBs. The MFBs also set up their apex association known as "National Association of Microfinance Banks" (NAMBs) to create the platform for capacity building, generic product development and marketing, as well as information/resource sharing and promoting best practices, among members.

There are facts that poverty is indeed increasing in Nigeria, based on the poverty assessment study commissioned and sponsored by the World Bank in 1995 (Akanji, 2006). Attacking 'poverty' is based on a deeper understanding of the meaning and causes of poverty. In the opinion of Akanji (2006), the World Bank report shows that economic development continues to be central to success in reducing poverty, but that poverty is also an outcome of economic, social and political processes that interact with and reinforce each other in ways that can ease or exacerbate the state of deprivation in which poor people live. Effectively functioning financial markets have fundamental roles to play in fostering development. At the level of individual livelihoods, financial markets can perform very crucial functions. They can be a principal means for the poor to get access to financial assets; through facilitating savings, they can be of importance in reducing the vulnerability associated with uneven and unpredictable year-to-year changes in circumstances, and they can help convert illiquid assets into liquid ones in the event of emergencies (Olomola, 2008).

Nonetheless, any poverty reduction programme must seek to address the inefficiency and inadequacies of financial markets since they rarely effectively discharge the expected functions. The credit policy for the poor involves many practical difficulties arising from the operations of financial institutions and the economic characteristics and financing needs of low-income households. For Example, commercial banking institutions require that borrowers have a stable source of income out of which principal and interest can be paid back according to the agreed terms. However, the income of many self-employed households is not stable. A huge number of micro loans are needed to serve the poor, but banking institutions prefer dealing with big loans in small numbers to minimize administration expenses. They also look for collateral with clear title-which many low-income households do not have. In addition, bankers tend to consider low income households a bad risk, imposing exceedingly high information monitoring costs on operation (Shastri, 2009). This paper therefore, will critically assess how the poor has been empowered through the operation of microfinance as a strategy for poverty reduction in Nigeria.

THE NIGERIAN MICROFINANCE CONTEXT

Microfinance is often advocated as a solution to multiple social problems in Nigeria. Poor persons with access to credit can make investments in enterprises that could bring them out of poverty. By the understanding of the level of poverty in Nigeria, Government attempted with several [3]micro-credit programs to alleviate poverty programs/projects such as Agricultural Development Programs (ADPs), National Directorate of Employment (NDE), Better Life for Rural Dwellers (Later named Family Support Programs), the Directorate of Food, Roads and Rural Infrastructure (DFRRI), which were pursued during 1986 to 1999. Other institutions that have also attempted purveying micro-credit were the rural banking scheme (1977-1990); People's Bank (1987-1990); Community Bank (1990-2007). It would be good to note that, according to the Microfinance Policy Framework that was launched in 2005, the erstwhile community banks that met the requirement of increasing their capital base to N20 million by the end of the year 2007, were converted into microfinance banks.

Although all the programs were directed at improving the productive base for sustainable growth, most of the efforts at purveying micro credit to alleviate poverty were largely irrelevant, urban-structured from the standpoint of the realities of (who is the poor?)- understanding the poor (Akanji, 2006). There are basically [4]formal and [5]informal models of purveying microcredit to the target group. The most successful had been the informal model because in Nigeria and several developing economies where poverty is high, some individuals, households and regions remain isolated from markets and from mechanisms for borrowing and lending or insuring against risk (Aryeety, 2005). Consequently, informal lenders tend to target the poor (including women), although not always successful; attempts by better financed innovative schemes to target the same poor people have not been more successful (Akanji, 2006). The issue there is no longer a simple one of targeting or not targeting, but of how to equip institutions that can reach the poor at least cost (that is, informal lenders) to extend their reach.

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[3] Micro-credit is a small amount of money loaned to a client by a bank or an institution. Microcredit can be offered, often without collateral, to an individual or through group lending.

[4] The formal micro-finance model is built around formal financial institutions such as the commercial banks, micro-finance banks etc.

[5] Informal finance operates outside the purview of the legal, fiscal, regulatory and prudential framework of the monetary and financial authorities.

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Most of the formal institutions that purvey credit to the poor had not been successful. The reasons adduced for their failure had been limited knowledge of the poor and no closer relationship between the formal institutions and the informal institutions. The framework for linking informal savings collectors to the formal institutions is a welcomed development. The banks' readiness to acquire more information about the informal sector and making serious efforts at strengthening group schemes encouraged the successful turnaround of micro-credit programmes in Nigeria. An example is the merger of the Nigerian Agricultural and Cooperative Bank (NACB), Peoples Bank of Nigeria and Family Economic Advancement Program (FEAP), to form Nigerian Agricultural Cooperative and Rural Development Bank (NACRDB) in 2001.

Income in Nigeria is closely linked to social and economic status: whilst the upper and middle classes inhabit the 'formal income from their formal ventures and employment, on the other hand, the poorest and low income status are largely 'informally' employed. Low income households are not usually involved in regular income occupations and therefore wait for job creation strategies to absorb them; they 'permanently inhabit' a dependent segment of the so called developing Nigerian economy, in which opportunities for jobs, or for independent and self-sustaining entrepreneurial capital accumulation, are minimal.

Though poverty reduction has long been a high priority for the Government of Nigeria, microfinance is still an experimental tool in its overall strategies. The Federal Government of Nigeria has over the years demonstrated strong commitment to the provision of financial services and economic empowerment of the poor and low income groups. The critical role of finance in the realization of the goals motivated the government, in collaboration with the Central Bank of Nigeria, to formulate the Financial System Strategy (FSS) 2020 in 2007, as part of an overall National vision, which aims to make Nigeria one of the 20 largest economies in the world by 2020.

UNITED NATIONS MANDATE FOR MICROFINANCE AND POVERTY ALLEVIATION

The World Summit for Social Development (WSSD) in March 1995 articulated a global commitment by Governments to eradicate poverty as an ethical, social, political and economic imperative. Poverty eradication was one of three core themes of WSSD. The Programme of Action affirmed the primacy of national responsibility for social development, including poverty eradication, but also called for international support to assist governments in developing strategies. The Programme of Action suggested ways to involve civil society in social development and to strengthen their capacities. It called on Governments to mobilize resources for social development, including poverty alleviation. The WSSD Programme of Action was to be implemented within the framework of international cooperation that integrated the follow-up to recent and planned UN conferences relating to social development, for example, the Children's Summit in 1990, the Environment and Development Conference in 1992, the Human Rights Conference in 1993, the Population and Development Conference in 1994 and the Women's Conference in 1995.

The United Nations System Conference Action Plan (UNSCAP) designated poverty alleviation as the integrating theme for follow-up to world conferences. It called for UN system action in five areas:

- Jobs and sustainable livelihood.
- Regenerating the environment issues.
- The enabling environment.
- Social service for all.
- Arrangement of women and gender mainstreaming.

UNDP and UN Resident Coordinators were asked to coordinate UN system efforts in the five areas. UN development organizations have their own individual mandates.

Microfinance is one tool for poverty alleviation. The enabling environment influences the effectiveness of microfinance in the other four areas of poverty alleviation interventions. The UN organizations' mandates in the area of microfinance primarily lie in the area of technical assistance and demonstration of models that contribute effectively to poverty alleviation. The responsibility for provision of capital rests with governments, with support from bilateral donors and international financing institutions (Report of United Nations, 1995).

FEW SCHEME OF THE GOVERNMENT OF NIGERIA

Microfinance schemes for the upliftment of the poor falls majorly under the formal model. The informal microfinance scheme includes savings clubs/Pools, Esusu, Ajo and Money lenders. However, 'Esusu' is the most popular informal microfinance scheme in Nigeria.

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Esusu:

Esusu is a revolving loan scheme in Nigeria and entrenched in most West African countries operating as an informal micro-credit programme. The groups are voluntarily formed to operate the revolving schemes. Members make fixed contributions of money at regular intervals. At each interval, one member collects the entire contributions from all. Every member takes a turn until the cycle is completed, and then it starts again. For people who take their turn late, esusu functions as a savings mechanism. The esusus are very strong programme that have assisted the target group to alleviate poverty, particularly among market women in rural/urban markets. Each esusu's group has a recognized leader and Esusus are often used as a model by NGOs trying to establish microfinance programme in urban setting.

The Formal Model:

The formal microfinance model is built around formal financial institutions such as the commercial banks, rural banks etc. Most of the formal institutions that purvey credit to the poor had not been successful. The reasons adduced to their failure had been limited knowledge of the poor and no closer relationship between the formal institutions and the informal institution. The [6]Grammen experience is an example of that model that has been able to transform from informal to formal model of purveying micro-credit to the poor.

The World Bank Group and the International Monetary Fund's efforts at assisting countries to understand the poverty situation in their economy, assess the level and determine to reduce the level, knowing that most developing economies are held back with debt obligation, have proved quite successful in most developing countries. It has helped Nigeria to open up discussions with our creditors at the Paris Club Group of creditors. The cancellation of the Nigerian debt by the Paris Club of creditors on January 21, 2008, promises a great relief to the country. The World Bank and IMF determined in 1999 that nationally owned participatory poverty reduction strategies should provide the basis for all their concessional lending and debt relief under the enhanced Heavily Indebted Poor Countries (HIPC) initiative. This approach builds on the principles of the comprehensive development papers on Poverty Reduction Strategy by country authorities for submission to the Bank and fund boards.

Donors have also played a very strong role in the micro-credit program, particularly, international donors such as UNDP, through the NGOs. The alternative micro-credit delivery model proposed by Union Gabriel and Itoro O Ibanga (1997) called "The Ekpuk (family) model worked perfectly well within an extended family structure, particularly proven successful in some villages in Akwa Ibom State of Nigeria. However, this system of credit delivery need to be encouraged to work through formal credit institutions as much as possible, such as microfinance and NACRDB. It will help to support the development of strong non-bank financial institutions, with less risk of default.

In terms of direct intervention, the government established the National Poverty Eradication Programme (NAPEP) in 2002, to dispense government financial support for the poor and low income groups. In order to improve the employability of school leavers, the government also established the National Directorate of Employment (NDE), which provides vocational training and skills acquisition for this segment of the population. In the same vein, the Small and Medium Enterprises Development Agency of Nigeria (SMEDAN) was established to promote the development of Small and Medium Enterprises (SMEs). At the state and local government levels, credit enhancing and poverty alleviation programmes are also being promoted.

To complement the efforts of the Federal Government, the Central Bank of Nigeria initiated a number of schemes and programmes to improve the access of the poor and low income groups to finance. These include:

- Agricultural Credit Guarantee Scheme established in 1997 with a current capital base of N3.0 billion.
- Agricultural Credit Support Scheme established in 2006 with N50.0 billion.
- Commercial Agricultural Credit Scheme established in 2009 with capital of N200.0 billion.
- Small and Medium Enterprises Credit Guarantee Scheme established in 2010 with N200.0 billion.
- Refinancing and Restructuring Facilities for SMEs established in 2010 with N200.0 billion.

ASSESSING THE CONTRIBUTIONS OF MICROFINANCE INSTITUTIONS (MFI) IN NIGERIA

[6] The Grammen bank, which is generally considered the first modern microcredit institution, started with the group concept-informal lending to the poor. It was started to assist landless people in Bangladesh to obtain credit, which

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An assessment of the microfinance environment post-2005 reveals some marked improvements. For instance, there is a heightened awareness among stakeholders such as government, regulatory authorities, investors, development partners, financial institutions and technical assistance providers on the need for microfinance. As at December, 2010, a total of 866 microfinance banks and 3 credit bureaux have been established. Similarly, the microfinance certification programme for operators of microfinance banks has been put in place, while the regulatory and promotional machinery have been beefed up (The Nigerian Microfinance Newsletter, 2010).

From the perspective of donor partners, the United Nations Development Programmes (UNDP), provided support for the microfinance policy and funded the "Sustainable Development of the Microfinance sub-sector Programme for Nigeria" in the period 2004-2007. It is currently supporting the drafting of a comprehensive National Microfinance Development Strategy (NMDS) that will define the roles and responsibilities of stakeholders with a view to enhancing the success of the policy and the achievement of the set targets.

Despite the interest created, interventions initiated and patronage engendered, a large percentage of Nigerians are still excluded from financial services. The 2010 Enhancing Financial Innovation and Access Financial Sector Development Organization (EFInA) study revealed a marginal increase of those served by formal financial market from 35.0 percent in 2005 to 36.3 percent in 2010, five (5) years after the launching of the microfinance policy. When those that had financial services from the informal sector such as savings club/pools, Esusu, Ajo, money lenders are included, the total access percentage for 2010 was 53.7 percent, which means that 46.3 percent or 39.2 million adult populations were financially excluded in Nigeria (The Nigerian Microfinance Newsletter, 2010).

The table below further gives a breakdown of the access statistics:

	Percentage (%)	Total number (millions)
Adult population	100	84.7
Financially served	53.7	45.5
Financially excluded	46.3	39.2
Formally served (included)	36.3	30.7
Informally served (included)	17.4	14.7
Banked	30.0	25.4
Other formal institutions	6.3	5.3

Source: EFInA Survey Report, 2010

A further analysis of the EFInA survey results showed that within some selected countries in Africa, Nigeria was lagging behind in terms of people that are financially excluded. For instance, South Africa, Kenya, Botswana had 26 percent, 32.7 percent and 33 percent, respectively, of their population excluded from financial services compared with the 46.3 percent for Nigeria.

The access gap is further revealed by the savings pattern of Nigerians. Several factors have accounted for the sub-optimal performance of the microfinance sub-sector, among which are:

- Uneven Distribution of Microfinance Banks and Institutions
- Carry-over of Inept culture in converted Community Banks
- Lack of knowledge and Skills in Practical Microfinance Banking
- Poor Corporate Governance
- Lack of Funds for Intermediation
- Harsh and Costly Business Environment
- Weak Internal Control System.

The experience of microfinance lending in Nigeria had not been quite successful from the formal model approach. Inadequate information will preclude making a categorical statement of the success of informal model. However, most poor groups seem to appreciate informal lending, despite the financial cost involved. If MFIs extend lending to the very poor, then, they can help break the power and hold of such creditors, who operate in the inter-locking credit and factor markets. Although high, the interest rates charged by the MFIs are lower than the rates charged by informal creditors (money lenders/employers/landlords (Olomola, 2008). Unfortunately, however, most MFIs have been found lacking when it comes to lending to the very poor.

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Nonetheless, it seems that microfinance has significantly dented the informal credit markets by undermining debt-bondage and usury in the rural areas of Nigeria. Thus microfinance is having a modernizing impact, even if inadvertent, unacknowledged and unsung. However, the validity of some of the usual arguments against informal finance has been questioned and the co-existence of both the traditional institutions and modern financial intermediaries has been advocated (Bouman, 2008). The private sector seems to be bracing up for the challenge through the formation of informal financial groups (IFGs) and the participation of NGOs, including donor agencies. Available literature indicates that lenders resort to the disbursement of credit to groups rather than individuals as a way of overcoming the problems of high transaction costs and loan default and as a way of extending their coverage of beneficiaries of small loans. However, results have been mixed, with failures outnumbering successes (Olomola, 2008, Huppi and Feder, 2009). Unfortunately, the persistent skepticism of most development theorists about the contribution of informal finance to development derives partly from the fact that much of the available information about traditional savings and credit associations has been sketchy and inaccurate, with little detailed analysis.

ADDRESSING THE CHALLENGES IN THE NIGERIAN MICROFINANCE INSTITUTIONS

The impact of microfinance in Nigeria gives room for cheers. If appropriate strategies are employed, the challenges could be considerably addressed. For this purpose the following steps are suggested:

- Effective Regulatory Oversight
- Proper staffing
- Proper and Appropriate Business Models
- Capacity Building Programme
- Continuous Awareness Creation
- On-lending Facilities
- [7]Financial Inclusion Strategies

In addition, linking the informal finance to formal financial institutions should be emphasized. Judging from the proved advantages of informal finance, policy attention has to shift in the direction of integrating the formal and informal systems rather than eliminating the latter. Further inquiry into the operations of informal finance is warranted to correct existing misapprehensions and misperceptions and to tap fully the savings and credit potential of the informal sector. Indeed, rather than disappearing, informal finance continues to expand in Nigeria (Olomola, 2008). In the opinion of Propiel (2006), informal finance is much more extensive and diverse than formal finance and accounts for most of the financial services, other than term finance, provided to the rural sector. In most sub-Saharan African (SSA) countries, formal rural credit accounts for less than 10% of total credit disbursed. Moreover, the survival of informal finance over the years and its persistence both in rural and urban economies in spite of policy emphasis on modern financial intermediaries indicate the advisability to seek a better understanding of its operations with a view to drawing useful lessons for the improvement of the rural financial system.

While it has been demonstrated in a number of studies that the poorest can improve their socio-economic conditions, researchers have pointed to several general issues that make microfinance work for the poorest:

- Even a well-designed microfinance programme is unlikely to have a positive impact on the poorest unless it specifically seeks to reach them through appropriate product design and targeting (Wright, 2000). Experience shows that unless there is a targeting tool, the poorest will either be missed or they will tend to exclude themselves because they do not see the programmes as being for them, do not have the ‘correct’ clothes, etc. (Navajas et al. 2000; Simanowitz, 2000).
- Mission creep: There is a strong tendency to move to the top of the clientele group, and give little attention to the needs of the poorest, with the end result that their proportion diminishes over time (Navajas et al. 2000). Only MFIs that design programme around the needs of the poorest are likely to retain them as clients.
- Savings and Credit: there is a general consensus that facilitating savings is important, because there is a high demand for it among the poorest and because savings play a role in protecting

[7] Financial Inclusion Strategies is to allow poor and low-income people to access credit, insurance, remittances and savings products. In many countries, the financial sectors do not provide these services to the lower income people. An inclusive financial sector will support the full participation of the lower income levels of the population.

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against the seasonality of cash-flows and fulfilling a [8]micro-insurance function. In addition, building up deposits reinforces discipline for [9]micro-entrepreneurs and can eventually yield collateral and serve as a source of funding.

- Savings alone, however, have only a minor developmental impact (Morduch and Harley, 2007). For instance, the protection against shocks might allow children to remain in school or income-earners to get medical treatment and minimize time away from work, but it is slow to create any significant wealth in itself unless credit is also available. MFIs that focus on savings more than credit tend to reach a smaller proportion of the poorest, have a lower and slower impact on poverty reduction, and are therefore less conducive to reaching the Millennium Goals by the target dates. While the savings-first institutions are easier to finance by donor agencies (far less-start-up capital required), the few comparative studies available show that borrowers fare better than non-borrowers (Chen and Snodgrass, 1999; Fruman and Paxton, 1998).

Again, synergies between microfinance and other programs should be encouraged in Nigeria. It is clear from available evidence that there are strong potential synergies between microfinance and the provision of basic social services for clients. The benefits derived from microfinance, basic education, and primary health is interconnected, and programs have found that the impact of each can increase when they are delivered together.

- The marginal cost of providing education or basic health information can be substantially reduced when the infrastructure for microfinance is already in place.
- Services provided need to be relevant to the needs of the target group and not just an add-on that is of poor quality (UNICEF, 1997 MkNelly and Dunford, 1998, 1999; Marcus, 1999).

The inefficiencies of many state-run specialized financial institutions have provided a strong rationale for market-based financial sector reforms. It is now realized that these reforms had their own limitations, while SMEs and the agricultural sector, especially food production, need state support. Therefore, instead of focusing solely on microfinance, designing efficient state-run financial institutions as part of developing an inclusive financial sector should also be integral to the poverty reduction efforts. Management and operational lessons learnt from successful MFIs can provide valuable inputs into the design of specialized financial institutions for SMEs and the agricultural sector.

Access to financial services is but, one aspect of the support needed by entrepreneurs running SMEs and micro-enterprises. They also need training in business skills and access to marketing information so that they can expand to take advantage of both domestic and international markets and thereby create decent jobs. Here too, the government has important role to play, as the majority of SMEs and micro-entrepreneurs will not be able to afford the market-determined fees for such training or marketing information.

In sum, while NGOs are making valuable contributions to safety-net by providing micr-credit to the poor and vulnerable, the government cannot abrogate its role in the area of social provision. The government also has to be a major player in the design and operation of an inclusive financial sector to cater for the needs of the “missing” middle in the informal and agricultural sectors. This is crucial to ensure that growth is employment-intensive to maximize its impact on poverty reduction.

CONCLUSION

This paper has established that microfinance is indeed a strategy of poverty reduction. The scheme of microfinance has been found to be an effective instrument for lifting the poor above the level of poverty by providing them with increased self employment opportunities and making them credit worthy.

It is a progressive strategy for Nigeria to have developed strong linked information by merging the formal, semi-formal and informal institutions that have in the past purveyed credit to the poor under one umbrella, NACRDB. With some effort, substantial progress can be made in taking MFIs to the next orbit of significance and sustainability. There is a need for designing financial sustainable models that increase outreach and scale up

[8] Micro-insurance is a system by which people, businesses and other organizations make payments, to share risk. Access to insurance enables micro-entrepreneurs to concentrate on growing their business while mitigating other risks affecting poverty, health or the ability to work.

[9] Micro-entrepreneurs are people who own small-scale businesses that are known as microenterprises. These businesses usually employ less than 5 people and can be based out of the home. They can provide the sole source of family income or supplement other forms of income. Typical micro-entrepreneur activities include retail kiosks, sewing workshops, carpentry shops and market stalls.

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operations for the poor in Nigeria. People residing in the villages are still unaware of banking policies and credit system, so NGO should communicate to them and share their view with villagers. Banks should convert and build up professional system into social banking system for the poor. The Federal Government and State Governments should also provide support for capacity building initiatives and ensure transparency and enhanced credibility through disclosures.

As financial inclusion agenda is becoming a global pursuit, Nigeria would need to explore strategies that are working in other countries and adopt them in a concerted manner.

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