# Micro Finance and Poverty Alleviation in Sri Lanka

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**Abstract**

Microfinance services in Sri Lanka have a wide geographical outreach but the extent of outreach of private operators including NGOs and commercial banks in rural areas is rather limited although the poor and the poorest groups have been reached by these Institutions. Most of people prefer the MFI rather than the banks. Because, they can easily access the loans from MFI. The objective of this research is to provide further evidence on the contribution of micro finance for poverty alleviation in Sri Lanka. In this regards, a survey was conducted among the selected micro finance beneficiaries from Polonnaruwa District of North Central Province in Sri Lanka. The collected data were analyzed using statistical software and found that the micro finance programs significantly help to poor people to uplift their live which lead for the poverty alleviation in Sri Lanka. However, microfinance facilities are no 'magic bullet' for poverty reduction. Many other changes are also needed. Finally, it is noted that there is a significant relationship between the micro finance and poverty alleviation in a certain level of percentage.

**Key Words**: Micro Finance, Poverty Alleviation, Micro Finance Institutions (MFIs)

## Introduction

The microfinance movement began with the work of Dr. Muhammad Yunus in Bangladesh in the late 1970s, spreading rapidly to other developing countries. Most early microfinance institutions (MFIs), including Yunus's own iconic Grameen Bank, relied on funding from government and international donors, justified by MFI claims that they were reducing poverty, unemployment and deprivation.
Microfinance is a source of financial services for entrepreneurs and small businesses lacking access to banking and related services. The two main mechanisms for the delivery of financial services to such clients are:

(a) relationship-based banking for individual entrepreneurs and small businesses.

(b) group-based models, where several entrepreneurs come together to apply for loans and other services as a group.

In some regions, for example Southern Africa, microfinance is used to describe the supply of financial services to low-income employees, which is closer to the retail finance model prevalent in mainstream banking.

For some, microfinance is a movement whose object is "a world in which as many poor and near-poor households as possible have permanent access to an appropriate range of high quality financial services, including not just credit but also savings, insurance, and fund transfers. Many of those who promote microfinance generally believe that such access will help poor people out of poverty, including participants in the Microcredit Summit Campaign. For others, microfinance is a way to promote economic development, employment and growth through the support of micro-entrepreneurs and small businesses.

## Problem Statement

Microcredit is provision of credit services to poor clients. Microcredit is one of the aspects of microfinance and the two are often confused. Critics may attack microcredit while referring to it indiscriminately as either 'microcredit' or 'microfinance'. Due to the broad range of microfinance services, it is difficult to assess impact, and very few studies have tried to assess its full impact. Proponents often claim that microfinance lifts people out of poverty, but the evidence is mixed. Therefore, this research is an attempt to further emphasize the contribution of the micro finance for poverty alleviation in Sri Lanka. Hence, the rest of this paper will be discussed as below.

Objective of this study to investigate the relationship between Micro finance and poverty alleviation in Sri Lanka.

**Micro Finance in Sri Lanka and Literature**

Lanka Microfinance Practitioner' Association (LMPA) is a network formed by several Microfinance Practitioners in Sri Lanka. The main function of the LMPA is to enhance the ability of their members to provide quality financial services to grass-root communities. They achieve this goal by promoting Microfinance and by encouraging cooperation, sharing information and assistance between member practitioners and stake holders. LMPA is the pioneer in microfinance networking among microfinance practitioners in Sri Lanka, and was initiated on the 31st of March 2006. The Lanka Microfinance Practitioners' Association is incorporated as a non-profit Organization under the Companies Act No. 7 of 2007.

According to the Milford Bateman (2011) Sri Lanka has been ranked in sixth in terms of microfinance penetration. It can be observed with other most microfinance-friendly countries from Table 01.

Table 01: Micro finance Penetration by 2009

| Global Ranking | Country | Borrower accounts/ population |
|---|---|---|
| 1 | Bangladesh | 25% |
| | (Andhra Pradesh State, India) | 17% |
| 2 | Bosnia and Herzegovina | 15% |
| 3 | Mongolia | 15% |
| 4 | Cambodia | 13% |
| 5 | Nicaragua | 11% |
| **6** | **Sri Lanka** | **10%** |
| 7 | Montenegro | 10% |
| 8 | Viet Nam | 10% |
| 9 | Peru | 10% |
| 10 | Armenia | 9% |
| 11 | Bolivia | 9% |
| 12 | Thailand | 8% |
| 13 | India | 7% |
| 14 | Paraguay | 6% |
| 15 | El Salvador | 6% |

Source: Gonzalez (2010); *Rozas and Sinha (2010).

**Impacts on poverty reduction**

Hulme, *et al* (1996) the most-cited source of evidence on the impacts of microfinance is the early set of studies collected by David Hulme and Paul Mosley. The findings of these studies are provocative: poor households do not benefit from microfinance; it is only non-poor borrowers (with incomes above poverty lines) who can do well with microfinance and enjoy sizable positive impacts. More troubling is the finding that a vast majority of those with starting incomes below the poverty line actually ended up with less incremental income after getting micro-loans, as compared to a control group which did not get such loans.

Findings of the Hulme *et al* (1996) studies imply that credit is only one factor in the generation of income or output. There are other complementary factors, crucial for making credit more productive. Among them, the most important is recipient's entrepreneurial skills. Most poor people do not have the basic education or experience to understand and manage even low level business activities. They are mostly risk-averse, often fearful of losing whatever little they have, and struggling to survive. This does not mean that they do not want to better themselves (e.g., as suggested by the so-called backward bending labour supply curve).

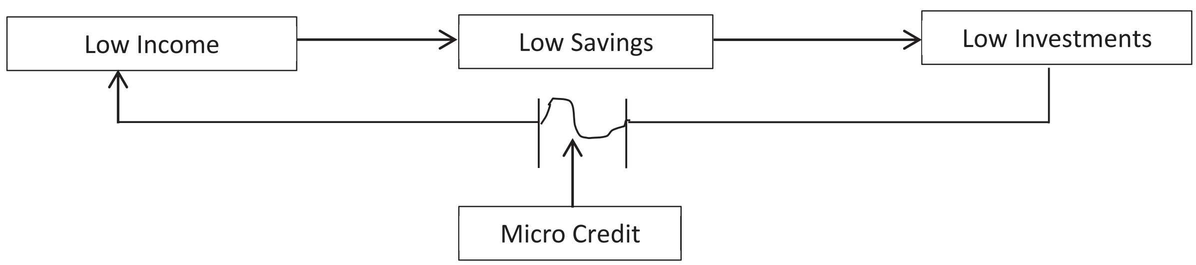
**Micro Finance, Poverty and Poverty Alleviation**

Microfinance supported these informal microenterprises through microcredit. The microcredit approach to poverty reduction is "the provision of small loans to individuals, usually within groups, as capital investment to enable income generation through self-employment"

Shahidur R. Khandker (2005) Income or consumption poverty can be reduced through interventions such as micro finance that poor become self-employed and generate income. But efforts to assess the impact of micro finance programe can be biased by nonrandom program placement and participation. Antipoverty program such as the Grameen Bank are often placed in areas where the poverty level is high. Shahidur R. Khandker (2005)

Using the Micro Finance Institutions (MFIs) we can reduce the poverty in society. The following figure describes how poverty will be breaking using the Micro Credit. Nikhil Chandra Shil (2009) explains the poverty alleviation in Grameen model as follows.

**Figure 1 Breaking the Vicious of Poverty: The Grameen Model**




**Methodology**

**Data collection method**
Data for the study collected through the questionnaire from Polonnaruwa District of Sri Lanka. For this purpose 300micro finance beneficiaries selected as a sample. Among those only 153 people responded. Therefore, only 153 questionnaires were used for analyses. Data were analyzed using the SPSS software.

In order to check the impact of Micro Finance on the poverty alleviation, the following hypothesis is derived.

***H0*****:** Micro Finance does not impact the poverty alleviation in Sri Lanka

***H1*****:** Micro Finance does impact the poverty alleviation in Sri Lanka

This paper investigates whether the micro finance contribute for the poverty alleviation in Sri Lanka. The independent variable is the proxies of Micro Finance such as loan amount, re-payment ability, accessibility for getting the loan, saving and etc. The dependent variable is the poverty alleviation which is measured using the income, savings, and property.

**Data analysis**

The information was gathered from micro finance beneficiaries who are engaged with Micro Finance Institution in the Polonnaruwa district. 300 questionnaires were issued among the micro finance beneficiaries, but only 153 people responded. Therefore, only 153 questionnaires were used for analyses. Data were analyzed using the SPSS software.

Table 4.1 presents the demographic information. According to Table 91% beneficiaries are female and 9% are male involved in micro finance activities. Nowadays, female contribution increase due to the economic conditions of the family.

When we look at the age of the beneficiaries mostly all age group people are engaged with Micro Finance. According to table 39.2% are between 46 and 55. It seems that middle age people are mostly involved in getting the loan from micro finance compared to other aged groups.

In the case of education, it describes that education of the most of beneficiaries is at low level. It can be observed that 33.3% are below the O/L qualification. Only 28.8% followed the O/L. So it is notable that most of uneducated people are trying to get the Micro Finance loan to build up their life and the career.

Table 4.1 Demographic Information

| Variables | Category | Frequency | Percentage |
|---|---|---|---|
| Gender | Male | 14 | 9.2% |
| | Female | 139 | 90.8% |
| Age | 25 – 35 Years | 25 | 16.3% |
| | 36 – 45 Years | 37 | 24.2% |
| | 46 – 55 Years | 60 | 39.2% |
| | Above 55 Years | 31 | 20.3% |
| Education qualification | Bellow O/L | 51 | 33.3% |
| | O/L | 44 | 28.8% |
| | A/L | 19 | 12.4% |
| | Graduate | 3 | 2.0% |
| | Other | 36 | 23.5% |

Source: Survey Data Collection

Table 4.2 describes the summary of responses by the beneficiaries of micro finance. Accordingly, 97.4% of beneficiaries agree that their life had increased after getting the micro finance loan and it helped 66.6% percentage of beneficiaries to increase their life style. 94% of beneficiaries were satisfying with their loan repayment and 81% of them agreed that they haven't difficulties with the payment. Beyond 90% percentage of beneficiaries had agreed that the microfinance helped to improve their business and the level of income, consumption level and saving. All the beneficiaries who had response to the questionnaire are improved the saving after getting the loan.  90% of them believe that micro finance is an effective tool for poor people to alleviate their poverty.

Table 4.2 Question asked, Frequencies and Percentages

| S/N | Questions | Frequencies | Percentages |
|---|---|---|---|
| 01 | Micro finance helped a lot to increase the life style | 149 | 97.4% |
| 02 | Property has increased by availing the facility of Micro Finance | 153 | 100% |
| 03 | Expectation of family members (education of children) have been reached through the Micro Finance | 102 | 66.6% |
| 04 | Satisfaction level of loan repayment | | |
| | Satisfied | 144 | 94.1% |
| | Not Satisfied | 9 | 5.9% |
| 05 | It has some finance difficulties to the lenders when they are going to settle the repayment | | |
| | Yes | 28 | 18.3% |
| | No | 125 | 81.7% |
| 06 | Micro finance investment helped to improve the business | 149 | 97.4% |
| 07 | Income level has increased after inception of Micro Finance | 142 | 92.8% |
| 08 | Consumption level has increased by getting Micro Finance | 135 | 88.2% |
| 09 | It helps to increase the saving | 153 | 100% |
| 10 | Micro finance give more facilities to get the loan | 148 | 96.7% |
| 11 | I believe that micro finance is an effective tool for poor people to alleviate their poverty | 138 | 90.1% |

Source: Survey Data Collection

Table 4.3 shows the correlations between difficulties of Repayment, Loan Amount, Interest Rate and repayment schedule. The results of the correlation matrix show that there is a positive relationship of with the Loan amount and Interest rate with Difficulties of Repayment and it is negatively related to the Repayment Schedule, because of some of peoples are getting the loans more than one institution and they cannot repayment schedules. That's why they have some difficulties with the repayments. And also Interest rate and the Loan amount show the positive relationship. The results of the correlation shows that there is no significant relationship loan amount and interest rate with difficulties of payment.

Table 4.3 Analysis of variables

**Correlations**

| | | Repayment Schedule | Difficulties of repayment | Loan Amount | Interest Rate |
|---|---|---|---|---|---|
| Repayment Schedule | Pearson Correlation | 1 | -.243** | -.313** | -.373** |
| | Sig. (2-tailed) | | .002 | .000 | .000 |
| | N | 153 | 153 | 153 | 153 |
| Difficulties of repayment | Pearson Correlation | | 1 | .009 | .030 |
| | Sig. (2-tailed) | | | .913 | .711 |
| | N | | 153 | 153 | 153 |
| Loan Amount | Pearson Correlation | | | 1 | .532** |
| | Sig. (2-tailed) | | | | .000 |
| | N | | | 153 | 153 |
| Interest Rate | Pearson Correlation | | | | 1 |
| | Sig. (2-tailed) | | | | |
| | N | | | | 153 |

**. Correlation is significant at the 0.01 level (2-tailed).
Source: Survey Data Collection

Table 4.4 Analysis of variables

According to the data analysis loan amount and monthly income has a positive significant relationship. There is also significant and positive relationship between monthly income and saving. But loan amount and monthly saving has no significant relationship. These correlation relationship proves that micro finance support the poverty alleviation in Sri Lanka.

Correlations

| | | Loan Amount | Monthly Income | Monthly Savings |
|---|---|---|---|---|
| Loan Amount | Pearson Correlation | 1 | .231** | -.109 |
| | Sig. (2-tailed) | | .004 | .179 |
| | N | 153 | 153 | 153 |
| Monthly Income | Pearson Correlation | | 1 | .437** |
| | Sig. (2-tailed) | | | .000 |
| | N | | 153 | 153 |
| Monthly Savings | Pearson Correlation | | | 1 |
| | Sig. (2-tailed) | | | |

| | | | | |
|---|---|---|---|---|
| N | | | | 153 |

**. Correlation is significant at the 0.01 level (2-tailed).
Source: Survey Data Collection

**Conclusions**

This research focuses on poverty alleviation through micro finance. According to data analysis, the variables that explain the poverty alleviation indicate that micro finance also strongly support for the poverty alleviation in Sri Lanka. 94.1% percent of beneficiaries are satisfied with their repayment schedule and 81.7% percentage of beneficiaries agreed that they have do not any difficulties with the repayment. In the case of saving, 100% percent of beneficiaries are savings in different ways. It means they can use their saving for investments and also it will become a growth of their business.

There are some issues arising when they are getting their Micro Finance loans as a group basis. Because, if one person avoid from the repayments of loan then other group members should take the responsibility of re-payment on behalf of the group. It will be a negative issue of the repayment for the group members; on the other hand, group lending is a good thing for Micro Finance Institutions.

Furthermore, there are some complains from the lenders that they have to give more interest when they are getting the loans from the private sector, but in the public sector they do not need to give much interest. But the issue is getting the loan from the public sector is very difficult. It takes long time and the people have to fill more documents and also the most of officers are trying to help for their friends and relations. In that time poor people are facing more difficulties to get the loan from public sector. So it should be remarkable to set up a good system for all in the country.

However, the micro finance programs significantly help to poor people to uplift their live which lead for the poverty alleviation in Sri Lanka. The following recommendations also should be considered to uplift the micro financing system in Sri Lanka which may lead for poverty alleviation.

**Recommendations**

1. As the interest rate is an additional burden over the clients. Hence, the interest rate must be reduced and re-payback period should be increased.
2. Most of the poor people don’t have enough knowledge to develop their business. Therefore, a special campaign should be developed after giving the loan.
3. Government Institutions should give the more attention to the poor people and conduct some program to develop their career.
4. MFI should develop a mechanism to avoid multiple loans received by the beneficiaries. Because, when the poor people receive micro loans from several places then it can become burden for settling it.

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