DOES MICRO FINANCE ALLEVIATE POVERTY? EVIDENCE FROM RURAL AREA OF EASTERN PROVINCE IN SRI LANKA

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Abstract

Poverty is widespread and complex in both developing and undeveloped countries, encompassing both economic and non-economic dimensions. The study's findings provide a detailed comprehension of the influence of microfinance on reducing poverty in Sri Lanka. The data collection involved a comprehensive questionnaire completed surveys due to time and feasibility constraints. Furthermore, incorporating descriptive, correlation, and regression analyses into the study adds a layer of depth. According to the regression results, it was discovered that microcredit had a substantial impact on the entrepreneurial performance of women, resulting in a notable improvement of 24.1%. Education, training, and technological development are important factors that significantly influence the business environment for individuals who receive microfinance. Furthermore, the study emphasizes the significant effect of microcredit in reducing poverty in households, showing a remarkable 26.8% impact. Nevertheless, this impact is accompanied by a multitude of contributing elements, such as knowledge, health, and the current economic circumstances. Significantly, when contrasting experienced clients, with new and prospective clients, a noticeable disparity becomes apparent. Mature clients observe more significant enhancements in mitigating household poverty, highlighting the enduring beneficial outcomes of continuous involvement in microfinance initiatives. Although microcredit has a good relationship with the overall level of life for both categories, the study suggests that there is not a significant association with poverty reduction, particularly for recent and incoming clients. This highlights the significance of continuous and well-informed involvement with microfinance efforts in order to maximize their effectiveness in reducing poverty. These findings not only enhance the scholarly comprehension of microfinance but also provide practical guidance for policymakers and practitioners aiming to maximize the efficiency of such programs in various socio-economic settings.

Keywords : *Microfinance , Microcredit, poverty alleviation , Woman Empowerment*

1. Introduction

Poverty remains a pervasive challenge in both developing and underdeveloped nations, despite efforts to expand and bolster their economies. This multifaceted issue manifests in various forms, encompassing both financial and non-financial aspects. Poverty can manifest as a lack of income or property, an absence of basic survival capabilities, deficiencies in fundamental human abilities, institutional weaknesses, and, in extreme cases, a combination of economic, social, and political insufficiencies. This broad perspective includes factors such as limited education, inadequate livelihood opportunities, insufficient healthcare facilities, low income levels, and consumption disparities. The most severe form of poverty occurs when individuals lack access to life's basic necessities, impeding their ability to meet fundamental physical needs (Hussain and Hanjra, 2003).

The concept of poverty is dynamic and challenging to define precisely due to its multidimensional nature, evolving over time and varying across regions. Visconti (2012) posits that poverty emerges from unequal wealth distribution, restricted access to financial resources, the prevalence of intermediaries, monopolies, and a lack of democracy. Moreover, the absence of a universally accepted definition of poverty underscores its dependency on a country's political context (Chaudhry, 2003).

Microfinance is a key contributor to poverty alleviation, as it entails offering modest loans to persons who are situated below the poverty threshold. These loans provide financial assistance for self-employment initiatives, allowing borrowers to generate money and support themselves and their family. Microfinance has become increasingly recognized as a highly successful means of poverty alleviation over the past twenty years, tackling the underlying issue that remains worldwide. The significance of Microfinance Institutions (MFIs) in alleviating poverty in emerging economies has been acknowledged, as emphasized by the United Nations' designation of 2005 as the International Year of Microcredit. Microcredit, a component of microfinance, involves offering small loans to impoverished individuals, usually without requiring collateral. Microfinance is a range of financial services that target different groups of people, with a specific emphasis on those who are impoverished. The range of services provided encompasses not only small and micro loans, but also savings products, insurance, leasing, and other money transfer services (Addai, 2010).

Several research have examined the correlation between microfinance, financial inclusion, and the alleviation of poverty. Park and Mercado (2015) discovered an inverse relationship between poverty rates and financial inclusion in developing nations in Asia, highlighting the importance of financial inclusion in alleviating poverty. In their study, Sayekti and Dewanti (2018) emphasized the significant role of financial inclusion in promoting economic growth and reducing poverty in Indonesia. They said that financial inclusion contributes to the establishment of employment opportunities and helps to decrease vulnerability. Hussini (2018) discovered that microfinance plays a beneficial role in moderating the connection between financial inclusion and the alleviation of poverty.

Olokoyo and Babalola (2017) conducted a study in Nigeria, illustrating the direct correlation between financial inclusion initiatives and per capita income, thereby leading to a decrease in poverty. In their study, Wijewardana and Dedunu (2018) examined the influence of microfinance on reducing poverty in Sri Lanka. They specifically focused on variables such as the amount of loans, the ability to repay them, the level of accessibility, and the interest rate.

Voica (2017) emphasized the significance of convenient availability of inexpensive financial services for the purpose of achieving sustainable growth and economic integration. Meanwhile, Sanya and Olumide (2017) recognized the factors that contribute to poverty and financial inclusion in Ekiti state, Nigeria. Aguera (2015) emphasized that financial inclusion serves as a stimulus for both economic progress and the eradication of poverty.Additional research conducted by Lavong (2015), Imoisi (2014), Abel, Grace, and Willie (2014), and Sayed (2015) has examined the effects of microfinance on household income, expenditure, and general well-being. In their study, Cyn-Young and Ragelio (2015) investigated the correlation between financial inclusion, poverty, and income inequality in Asia. They specifically focused on the influence of demographic characteristics and per capita income.

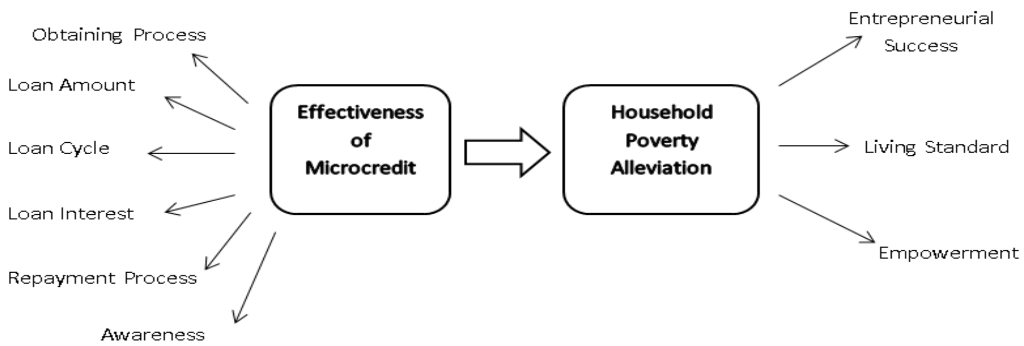
Several studies, like Migap et al (2015) and Nkwede (2015), focused on the Nigerian setting, while Joseph and Varghese (2014) examined the impact of financial inclusion on the development of the Indian economy. Chitokwindo, Mago, and Hofisi (2014) studied financial inclusion in Zimbabwe, highlighting its role in poverty and inequality in rural areas. Naime and Gaysset (2017) presented contrasting views, suggesting that financial inclusion does not uniformly impact poverty. They found that while financial inclusion decreases income inequality, it has no significant effects on poverty. This discrepancy in findings underscores the ongoing debate and inconsistency in results regarding the relationship between financial inclusion and poverty.

The main objective of this study is to examine the influence of microfinance loans on poverty in the specific setting of Sri Lanka. Addressing poverty involves tackling a complex problem that necessitates a sophisticated comprehension of the elements that contribute to it. The study aims to explore this intricacy by employing a thorough methodology, examining poverty from diverse viewpoints, and investigating the interaction of multiple elements. In order to attain a comprehensive comprehension of poverty, the research will examine a wide range of criteria including income levels, work prospects, education, and access to fundamental services. The study seeks to reveal the complex factors that contribute to ongoing economic issues experienced by specific sectors of the population by examining poverty from many perspectives.

Moreover, the research seeks to suggest policy interventions that can improve the efficacy of microfinance programs in alleviating poverty. The policy recommendations will be based on the empirical findings of the study, with the goal of addressing the identified deficiencies in service quality, sustainability, clients' understanding, and repayment capability in the Sri Lankan financial sector. Essentially, this research aims to thoroughly examine how microfinance loans affect poverty in Sri Lanka. The final objective is to offer significant insights that might contribute to ongoing efforts in promoting financial inclusion and reducing poverty. The recommended policy measures aim to educate stakeholders and policymakers, promoting a more efficient and enduring approach to microfinance as a means of reducing poverty in the country.

2. Research Methodology

The focal point of this framework is to examine the main effect of independent variable which is effectiveness of microcredit on alleviation of poverty as dependent variable. Number of different dimensions to measure the effectiveness of microcredit and also to measure the alleviation of poverty have been extracted from previous literatures. and the developed conceptual framework for this research as follows;



Source : Author constructed

The study aimed to assess the effectiveness of microcredit by examining dimensions such as the loan acquisition process, loan amount, loan cycle, loan interest, loan repayment process, and awareness of the entire credit program. Poverty was evaluated through three key dimensions: entrepreneurial success, living standards, and empowerment. The study aimed to survey 1,000 clients across 10 financial institutions in the Eastern Province of Sri Lanka, specifically in Ampara, Batticaloa, and Trincomalee districts. A random selection of 100 clients from each institution comprised the study population, exclusively focusing on women obtaining loans for productive purposes, such as business development.

The research included both mature clients (those using microcredit for over two years) and recent/incoming clients. The data collection involved a comprehensive questionnaire, resulting in 850 completed surveys due to time and feasibility constraints. The sample distribution included 320 clients from Ampara, 280 from Batticaloa, and 250 from Trincomalee districts. Approximately 60% of the sample represented mature clients (510 clients), while the remaining 40% represented recent and incoming clients (340 clients).The research assessed how these clients, categorized as mature or recent/incoming, improved their life standards, entrepreneurial skills, empowerment levels, and alleviated household poverty through the utilization of microcredit facilities.

3. Data Presentation and Analysis

The study adopted a comprehensive analytical strategy, utilizing descriptive, correlation, and multiple regression analyses to investigate the impact of microcredit on several aspects of women's economic and household well-being. The descriptive analysis yielded a first overview of crucial variables, providing vital summaries of the data. Correlation analysis subsequently identified connections between the effectiveness of microcredit and outcomes such as the success of women entrepreneurs, enhanced living standards, empowerment, and the reduction of household poverty. Ultimately, the utilization of multiple regression analysis facilitated a detailed investigation, specifically isolating the distinct influence of microcredit effectiveness while considering other influential elements. This methodology sought to provide significant insights into the complex impact of microcredit programs on women's economic empowerment and total household prosperity. It serves as a vital resource for policymakers, practitioners, and scholars in this subject.

Approximately 28% of the surveyed households, headed by women credit holders, were led by those making major decisions. The majority of clients (87%) were above 30 years old. Educational levels varied, with only 1.3% having a university education, 16.4% completing advanced levels, 28.9% finishing ordinary levels, 30% studying till ordinary levels without completion, and 23% having no satisfactory education.

Around 98% of loans were taken for business initiation or development, with 71% of clients taking loans more than three times. Most households (53%) had two income sources, and all clients were engaged in business activities, with self-employment being the most common (50%). Business types varied by location, impacting household poverty alleviation.

Income distribution showed that 53% had a monthly household income exceeding Rs. 30,000. Regarding accommodation, 96.7% owned their homes, and 46.7% had made recent improvements, indicating positive steps out of poverty. Despite challenges, the majority of clients maintained a positive attitude toward the microcredit program.

The correlation provides a thorough summary of the connections between the effectiveness of microcredit and important factors associated with entrepreneurial achievement, quality of life, empowerment of women, and reduction of household poverty. The correlation coefficients in each case, which range from 0.400 to 0.772, show moderate to strong positive connections. These data indicate that when the efficacy of microcredit improves, there is a corresponding enhancement in entrepreneurial achievement, living conditions, empowerment of women, and reduction of household poverty. All correlations in the investigated sample of 152 persons are statistically significant, as indicated by p-values of 0.000. This highlights the reliability of these associations. This evidence supports the idea that microcredit programs have a crucial role in positively influencing several aspects of socio-economic well-being, hence strengthening the potential influence of these financial interventions on larger aspects of individual and household prosperity.

The regression study reveals that the effectiveness of microcredit has a significant impact of 24.1% (R square value) on the entrepreneurial performance of women. The remaining 75.9% is determined by several other factors, including education level, training and development, and current technology development.

The results have definitively addressed the main research question: "Has microcredit proven to be an effective strategy in reducing household poverty levels?" Regression research reveals that the success of microcredit has a 26.8% influence on household poverty alleviation, as indicated by the R square value. The remaining 73.2% is driven by several other factors, including knowledge, health, and the situation of the economy.

The research found two distinct client categories: mature clients, who have been utilizing microcredit for a period exceeding two years, and recent & incoming consumers, who have been utilizing microcredit for a period shorter than two years. The sample consisted of 30 new and prospective clients and 122 established clients. For each client category, distinct Pearson correlation and regression tests were performed to investigate the association between independent and dependent variables.

The regression analysis reveals that the household living standard is influenced by the effectiveness of microcredit by 24% (as indicated by the R square value), while the remaining 76% is determined by other factors. No substantial correlation has been found between the efficacy of microcredit and the success of entrepreneurs, the empowerment of women, and the reduction of poverty within households for both recent and prospective clients.

4. Conclusion and Recommendations

Overall, the analysis concludes that mature clients in the sample are seeing a greater improvement in household poverty reduction as a result of the effective implementation of microcredit, compared to the incoming and recent clients. The examination of responses from incoming and current clients reveals a positive association between the effectiveness of microcredit and all other indicators, including household poverty alleviation. However, the only notable correlation that can be shown is the link between the efficacy of microcredit and the standard of living inside households. There is no substantial correlation between the efficacy of microcredit and the reduction of poverty in the households of new and recent clients. However, it is evident that microcredit mostly affects the consumption and expenditure patterns of new and recent clients. This validates the observation that the majority of new and existing clients mostly utilize credit for personal consumption, whereas more affluent households utilize credit for activities that generate revenue or enhance their asset portfolios. While their standard of living has really risen, there has been no notable improvement in their household poverty condition.

The study affirms that a substantial percentage of the impoverished rural population resides in isolated regions with limited access to public development. The majority of individuals living in rural areas who are economically disadvantaged often rely on microfinance institutions for access to credit. Fortunately, many establishments are specifically designed to cater to the impoverished population residing in rural areas. Typically, they employ a group-based lending approach that reduces stress for both the lender and the borrower and yields a high percentage of payback. Additionally, attributing credit to a small organization characterized by strong cohesion among its members promotes higher rates of repayment. The provision of microcredit to impoverished rural communities, whether through direct loans or inventory credit, has a positive impact on agricultural productivity in rural regions and contributes to the improvement of food security. It enables easier access to healthcare facilities, fosters the growth of community leaders, and enhances the beneficiaries' social status within their communities.

Regardless of the many approaches employed by microfinance institutions to offer credit, the study has demonstrated that their primary objective is to alleviate poverty. Having direct access to credit is a crucial asset for individuals to effectively organize and develop themselves. Furthermore, it promotes the expedited utilization of local resources such as land, labor, and assets.

Access to financing directly contributes to the development of local institutions by enhancing their ability to efficiently strategize and execute initiatives. It fosters increased self-sufficiency and empowers communities to have more control over resources and growth, while also strengthening the feeling of personal ownership. The study has debunked the prevailing misconception that the impoverished are not creditworthy and that women pose higher risks compared to men. -Ultimately, those who are impoverished possess a deeper comprehension of poverty, and as a result, they are the ones who have the potential to break free from it. The motivation for the impoverished to improve their own position depends on their appreciation of the opportunities available to them, such as access to microcredits.

The effectiveness of assisting the poor is contingent upon the perception of its impact, particularly when considering credit. Consequently, regardless of the amount of funding allocated to a school or health post, if individuals in poverty lack financial resources, their ability to utilize these facilities will be hindered, rendering the investment futile. Therefore, in order for poverty reduction measures to be successful and enduring, they must encompass a systematic transformation in the quality of life for those who are impoverished.

Ensuring the continuation of poverty reduction necessitates implementing measures and strategies that enhance the economic productivity and human resources of individuals living in poverty. In order for policy interventions to effectively benefit the impoverished, they must be carefully directed and focused. In order to accomplish this, both official and informal lending institutions must employ group-based lending, which effectively mitigates payback issues.

Furthermore, in order to cater to the need of the impoverished, it is imperative to establish official institutions that provide unsecured microcredit. Furthermore, it is imperative to establish a robust partnership between the Sri Lankan government and microfinance institutions in order to alleviate poverty in rural regions. The provision of microcredits to rural individuals facilitates rural development, necessitating government support for microfinance organizations by providing funding for lending to the impoverished.

Attempting to target a significant number of individuals living in extreme poverty just through the use of microfinance may not be a feasible goal. Specialized initiatives may be required to offer a comprehensive array of services to the extremely impoverished, encompassing education, healthcare, and broader societal advancement for the underprivileged, in addition to providing assets or loans.

In addition, microfinance institutions must enhance the technical and skill ability of their workers in microfinance by implementing systematic training programs. A training program could be created to improve the staff's ability to plan, implement, monitor, and evaluate microfinance projects. This will allow MFIs to customize microcredit to align with the requirements and consumption habits of applicants and guarantee the contentment of recipients. In order to facilitate timely access to credit for manufacturing, microfinance institutions might consider reducing the collateral requirement for applicants. This can still be accomplished by providing loans to collectives. It is imperative to incentivize numerous microfinance institutions to extend loans to the impoverished rural population, as the researcher contends that this will facilitate connections within rural industries and stimulate economic growth in rural areas.

The study has determined that the supply of microfinance services has a substantial effect on poverty alleviation. According to the report, many microfinance institutions provide loans to impoverished individuals under government supervision with the goal of reducing household poverty. Hence, this discovery would aid the decision-makers of microfinance institutions in allocating funds to the microfinance market, thereby facilitating the decision-making process. Microfinance institutions should develop a more appropriate and strategic model before entering the microfinance industry. When these organizations provide advise on entering the microfinance market efficiently, it instantly reduces the poverty level. This is because microcredit recipients gain expertise on how to handle their finances.

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