

Chapter 8

Role of Microfinance Banks in Provision of Credit for Poverty Reduction in Pakistan

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ABSTRACT

Microfinance banks started their operations in Pakistan in 2000 and have been working over the years. This chapter mainly considers microfinance bank growth in the provision of credit for poverty reduction. Six hypotheses are developed to address the main issues under investigation in this study. Secondary data is used to calculate compound annual growth rate for the period 2011–2015. Results showed growth in microfinance banks (total assets and branch network) and provision of loans/credit (customers, gross advances, net advances and advance per customer). For better returns on investment and economic development, further investment is suggested in the same sector.

INTRODUCTION

Banks have always been playing a major role in the economic development of any country because these are considered to be life blood of any economy. Origin of banks goes beyond centuries but according to Richard Hildreth (2001) the first regulated institution which resembles with the present bank was established nearly seven centuries ago but, in its origin, it had nothing to do with the present banking business because its main purpose was to collect loans during the war. He also described that in the seventeenth century the Bank of Amsterdam and the Bank of England (prototype of all the modern banks) were established. Now there are banks all over the world and contributing towards the economic and social development.

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Major commercial banks have been giving loans to the rich for the sake of earning profit and do not care much about the poor but there have been many similar institutions which have been working for the welfare of the poor and the Irish Loan Fund system in 18th century cannot be ignored because it is considered to be the first proper microfinance institution and after that the concept of microfinance institutions have spread around the world. In 1992 Banco Sol was the first commercial bank dedicated solely for the microfinance (CGAP).

Banking in Pakistan

According to Raiysat (2016) banking business started in Pakistan at the time of its independence with five commercial banks. A State Bank of Pakistan was also established to control the operations of the banks in Pakistan. The State Bank of Pakistan with help of Security and Exchange Commission of Pakistan is putting its efforts in betterment of banking sector in Pakistan. There has been a slump in the performance and growth of the banking sector in Pakistan when the Government of Pakistan in 1974 took a decision to nationalize all the institutions but in 1992 with the privatization decision and introduction of foreign private banks the banking sector again started growing and performing well. Standard Chartered Bank of Pakistan and Citi Bank Limited have played an effective role in this regard and banking sector is divided into five sub sectors which are private commercial banks, public commercial banks, foreign banks, Islamic banks, specialized banks and microfinance banks. The importance of microfinance was realized at its peak in the late 1990s. Khushhali Microfinance Bank was the first microfinance bank which started its operations in Pakistan under the State Bank of Pakistan in 2000. Within a period of next four years, four new microfinance banks i.e., The First Microfinance Bank Limited (2001), Apna Microfinance Bank limited (2003), Rozgar Microfinance Bank limited (2003) and Tameer Microfinance Bank limited (2005) started the operations in Pakistan. At present there are 11 microfinance banks. Sindh microfinance bank is the latest bank which has started its operations in May 2016.

Role of Microfinance Banks

Microfinance banks have been actively involved in the economic activities and keeping in view their role in the financial system of Pakistan, microfinance banks are classified separately and therefore ranked accordingly. There are major two credit rating companies working in Pakistan which rank the banks according to their credit quality (SBP 2016) and these are Pakistan Credit Rating Agency limited and JCR-VIS Credit Rating Company Limited. According to PACRA (2016) latest rating Tameer Microfinance Bank is at the top in long term credit followed by Mobilink Microfinance Bank Limited and Apna Microfinance Bank limited, and in short run Mobilink Microfinance Bank Limited and Tameer Microfinance Bank limited are at 1st position followed by Apna Microfinance Bank limited but with good credit quality. On the other hand, JCR-VIS (2016) updated list classifies Tameer Microfinance Bank limited, The First Microfinance Bank Limited and Khushhali Bank as top rating banks in short and long-term credit quality.

The literature has indicated that most of the work is done on the role of microfinance institutions in poverty reduction and rising the living standard of the people not only in Pakistan but all over the world but there isn't much work done on the growth of the microfinance banks specifically in Pakistan. This study will not only find the actual growth rate of the overall microfinance banks but also reveal the actual growth in terms of borrowers and advances to reduce the poverty in Pakistan.

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