Chapter 8
Poverty Reduction Through Microfinance:
Panacea or Myth?

ABSTRACT

Microfinance is believed by many people in Africa to allow poor people to protect, diversify, and increase their sources of income, which is known to be the essential path out of poverty and hunger. This chapter examines whether microfinance can really help to reduce poverty. The enduring question is: Can microfinance be the game changer that will lift the many poor rural women and men in Africa out of the misery of extreme poverty? Is this strategy bliss or myth? First, the author provides a context and rationale for microfinance in African countries. Second, the chapter follows a brief overview of the literature on the impact of microfinance on women's empowerment and whether credit lending transactions benefit the intended recipients. Finally, the chapter reviews the arguments of both sides of the debate and draws out future research trends.

INTRODUCTION

Microfinance is currently known in Africa to be a valuable tool for providing financial services to the poor at the bottom of the pyramid as a form of micro-credit to expand businesses, as well as for savings, money transfers, and payment services (Wapakala, 2016; Schriber, 2001). The microfinance industry provides financial services to the world's poor in the hope of moving individuals and families out of poverty. In 2013 there were 4.7 million active microfinance borrowers in Africa (Riggins & Weber, 2016). This represented a smaller percentage of the population compared to other regions of the world, perhaps indicating the potential for rapid growth of microfinance in Africa.

However, microfinance is maturing in part due to the adoption of information and communication technologies (ICTs) given recent advancements in mobile banking, Internet usage, and connectivity. Adoption of technology is indispensable for money transfers, increased agricultural productivity and overall poverty reduction in Sub-Saharan Africa. Recently, microcredit has generated considerable en-

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thusiasm and hope for ensuring sustainable financial inclusion of the poor. (Riggins & Weber, 2016). Lack of access to credit is often identified as a major obstacle to the adoption of agricultural technology. Often, informal alternatives, including family loans, access to savings clubs are unavailable to the poor or loans are rigidly administered, or offered at exorbitant interest rates.

For long periods of time, poor people in most African countries had virtually no access to formal financial services. Lack of access to loans or unfavorable lending conditions are a hindrance to success for the poorest women groups. The challenge ahead is to ensure access to financial services for the poor majority. Savings services allow savers to store excess liquidity of future use and credit services enable the use of anticipated income for current investment or consumption. Overall, therefore, microfinance services can help low income people reduce risk, improve management, raise productivity, obtain higher returns on investment, increase their incomes, and improve the quality of their lives and those of their dependents.

According to the Microfinance Gateway, an online resource for the global community dedicated to advancing access to financial services for the poor, microcredit refers to small loans for unsalaried borrowers with little or no collateral, provided by legally registered institutions (Bogan, et al., 2007). In fact, the ability to borrow a small amount of money to take advantage of a business opportunity, or to pay for school fees, and bridge a cash-flow gap, can be a first step to break the cycle of poverty. In practice, microcredit represents quick small loans given to poor clients and a component of credit and savings, similar to what ordinary salaried individuals do when they borrow from their future earnings by using a credit card or obtaining a personal loan from a commercial or savings bank.

As we know it today, microfinance has its roots in Asia and in Latin America. In Asia, the 2006 Nobel Peace prize winner Mohammed Yunus established in the 1970s in Bangladesh the successful Grameen bank to provide financial services to poor individuals, particularly women. This revolutionary innovation resulted to what became known as the "Classical Grameen model." Initiated as microcredit groups, women groups borrowed money without demand for collateral from Grameen Bank to establish diversified activities such as collective farming, garment making, cottage industries, marketing, IT services, and many more. The profit generated was used for societal benefit and for sustaining the enterprise.

The microcredit practice led thousands of microfinance institutions to spring up around the globe, most of them, modeled closely on the classical Grameen Bank model. This method of microcredit was deemed radically unique as it allowed poor self-employed women to obtain a loan without collateral. As a financial strategy, microfinance supposedly focused on poverty alleviation by providing microcredit or other financial services to poor clients. This anti-poverty tool was supposed to mitigate one of the dimensions and experiences of being poor; specifically, not having access to credit to start or expand a business, or the emergency liquidity required to cope with risk.

In the past two decades, poverty predominated rural Africa, but currently, microfinance and self-employment are taking off, as observed by the author during field trips in Africa, because of the provision of relief to populations that would normally be excluded by conventional financial institutions (Kurmanalieva, Montgomery & Weiss, 2003).

As manifested in the history of the Grameen Bank model, the concept of microfinance has been replicated in many parts of Asia and is now extensively used in Sub-Saharan Africa. Though it is contested, to-date, evaluations of microfinance institutions (MFIs) have shown that microfinance services have a positive impact on women (Schuler, Hashemi, & Badal, 1998; Khandker, 2005; Lakwo, 2007). Over time, therefore, microfinance has exponentially grown across Africa to be a valuable tool for providing

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