Impact of Microfinance on Emerging Economies' Economic Growth and Poverty Reduction

By

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Declaration

It is hereby declared that

1. The thesis submitted is my own original work while completing degree at BRAC University.
2. The thesis does not contain material previously published or written by a third party, except where this is appropriately cited through full and accurate referencing.
3. The thesis does not contain material which has been accepted, or submitted, for any other degree or diploma at a university or other institution.
4. I have acknowledged all main sources of help.

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Ethics Statement

Hereby, I **Mohasena** consciously assures that, the following conditions are met for this paper "**Impact of microfinance on emerging economies' economic growth and poverty reduction**"

1) This is original work that has not been previously published anywhere.
2) At this moment, the paper is not being considered for publication anyplace.
3) The writer's research and analysis are accurately and completely reflected in the article.
4) The publication adequately recognizes the contribution of co-authors and co-researchers.
5) The results are examined in relation to prior and continuing research.

If the Ethical Statement's rules are breached, it can have major consequences.

I agree with the above statements and confirm that this submission follows the norms of the Solid state.

Ionics as outlined in the Authors' Guide and the Ethical Statement.

Mohasena

Abstract

This essay will look at how microfinance affects both economic development and the reduction of poverty. The use of microfinance to provide the impoverished with new opportunities for business has gained favor as a means of decreasing poverty. Additionally, it works to promote empowerment, particularly among women, while building social capital in underprivileged communities. This study demonstrates how microfinance can play a significant role in a successful strategy for reducing poverty, particularly in rural areas. This study was produced using descriptive analysis and is based on secondary data. Microcredit can undoubtedly be regarded as a successful technique for reducing poverty in developing countries like Bangladesh after a thorough analysis of the data and information acquired. Future research and study are required in order to be more confident about the extent to which and the manner in which microcredit genuinely reduces poverty.

Keywords: Microfinance, Poverty, reduction, economic, Growth, Bangladesh

Acknowledgement

To begin with, I would like to convey my gratitude to Almighty Allah for his mercy in allowing me to complete my research by allowing me to remain calm, patient, and faithful during the course of my project. I am grateful to BRAC University's administration to make it possible for me to do the research under this heading.

Then I express my gratitude to all the institutions that took part in the research for letting me conduct the survey at such a crucial moment. My design and research approach were greatly aided by their recommendations. The committee members who allowed me to do research in this field are to be thanked.

To those respondents who answered the questionnaires honestly, I would like to extend my sincere gratitude.

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Chapter 1: Introduction

Background information on microfinance and emerging economies

Emerging economies, often characterized by a high degree of poverty, face many challenges in their efforts to achieve sustainable economic growth and advancement. The provision of financial services to people with modest incomes is known as microfinance or households, has gained widespread attention as a potential solution to these challenges. Microfinance has been defined as "the supply of loans, savings, and other basic financial services to the poor" (Robinson, 2001, p. 27). This financial service aims to empower low-income individuals by giving them access to capital to start or expand their own businesses, and to build assets for their future.

Organizations for microfinance (MFIs) have had success offering loans to a large number of people who are typically excluded from the traditional banking system. MFIs work with individuals or groups, often providing small loans without collateral, to help them start or expand businesses, and generate income. Microfinance has been implemented in many countries worldwide, including emerging economies such as India, Bangladesh, and Nigeria.

The potential impact of microfinance on economic growth and poverty reduction has been widely debated in academic literature. While some studies have shown that microfinance It's a powerful tool for fostering the economy and eradicating poverty, other studies have suggested that Microfinance's effect on these results is limited or even negative.

1.1 Purpose of the study

The purpose of this study is to examine the impact of microfinance on economic growth and poverty reduction in emerging economies. Specifically, the study aims to answer the following research questions:

1.2 Research questions

1. What is the impact of microfinance on economic growth in emerging economies?
2. What is the impact of microfinance on poverty reduction in emerging economies

Chapter 2: Literature Review

2.1 Definition of Microfinance

Microfinance has been defined in different ways, but it generally refers to the provision of financial services such as credit, savings, insurance, and remittances to low-income individuals or households who lack access to traditional financial institutions (Khandker, 2005). The goal of microfinance is to help alleviate poverty and promote economic development by providing small loans to individuals to start or expand their own businesses.

2.2 Historical Background of Microfinance

Microfinance has its roots in informal lending practices that have existed in many societies for centuries. The modern microfinance movement, however, began in the 1970s with the work of Muhammad Yunus, founder of the Grameen Bank in Bangladesh. Yunus pioneered the concept of microcredit, which involves the provision of small loans to poor people who lack collateral or a credit history. The Grameen Bank's success in providing microcredit to millions of people in Bangladesh inspired the creation of many other microfinance institutions around the world.

2.3 Theories on the Impact of Microfinance on Economic Growth and Poverty Reduction

Theories on the impact of microfinance on economic growth and poverty reduction are based on the assumption that access to credit can help poor individuals to invest in productive activities and generate income. Two of the most prominent theories are the "credit-led growth" hypothesis and the "poverty reduction" hypothesis.

The credit-led growth hypothesis suggests that microfinance can contribute to economic growth by increasing investment and entrepreneurship among low-income individuals

(Khandker, 2005). This hypothesis argues that microfinance can provide a catalyst for economic growth by enabling poor people to start small businesses, create jobs, and increase their income.

The poverty reduction hypothesis, on the other hand, posits that microfinance can help alleviate poverty by providing poor individuals with the means to improve their living standards. This hypothesis argues that microfinance can help poor people to meet their basic needs and build assets, which can contribute to long-term poverty reduction (Kabeer, 2005).

2.4 Empirical Studies on the Impact of Microfinance on Economic Growth and Poverty Reduction

Numerous empirical studies have been conducted to investigate the impact of microfinance on economic growth and poverty reduction. Some studies have found that microfinance has a positive impact on these outcomes, while others have found little or no impact. For example, Khandker (2005) found that microfinance has a positive impact on poverty reduction and economic growth, while Pitt and Khandker (1998) found that microfinance has a positive impact on the incomes of poor borrowers but no significant impact on their consumption levels.

2.5 Criticisms of Microfinance

Despite the widespread popularity of microfinance, some criticisms have been leveled against it. One criticism is that microfinance institutions charge high interest rates that can trap poor borrowers in a cycle of debt. Another criticism is that microfinance may not be effective in reaching the poorest of the poor, who lack the skills or resources to make productive use of credit (Morduch, 1999). Additionally, some studies have found that microfinance can have unintended negative consequences, such as increasing inequality or crowding out other forms of social welfare (Hulme & Mosley, 1996).

Overall, the literature on microfinance suggests that while it has the potential to be an effective tool for promoting economic growth and reducing poverty, its impact can be context-specific and may depend on a range of factors, including the design of the microfinance program, the characteristics of the target population, and the broader economic and political context in which it is implemented.

2.6 Overview of Microfinance in Emerging Economies

Microfinance has become an increasingly popular tool for promoting economic development and poverty reduction in emerging economies. According to the World Bank (2018), there are over 1,000 microfinance institutions operating in more than 100 countries, serving an estimated 200 million clients. In many emerging economies, microfinance institutions have filled a gap in the financial market by providing small loans to individuals and businesses that are unable to access traditional banking services.

2.7 Types of Microfinance Institutions

There are several types of microfinance institutions operating in emerging economies, including non-governmental organizations (NGOs), community-based organizations (CBOs), credit unions, and microfinance banks. NGOs and CBOs are often the pioneers of microfinance in emerging economies, as they typically have a grassroots presence and a deep understanding of local needs and conditions. Credit unions and microfinance banks are more formal institutions that offer a wider range of financial services and may be regulated by government authorities.

2.8 Characteristics of Microfinance Borrowers

The typical microfinance borrower in emerging economies is a low-income individual who lacks access to formal financial services. They may be self-employed or work in the informal sector, and may not have a regular income or collateral to offer as security for a loan. Microfinance borrowers may be women, who often have limited access to credit due to cultural or legal barriers.

2.9 Challenges Faced by Microfinance Institutions in Emerging Economies

Microfinance institutions in emerging economies face several challenges, including the need for sustainable funding, the difficulty of managing risk and providing effective services to a diverse client base, and the challenge of achieving scale while maintaining quality (Dichter & Harper, 2007). In addition, microfinance institutions may face regulatory and legal barriers, such as restrictive licensing requirements, that make it difficult to operate and expand their services.

Chapter 3: Research Methodology

In general, the women in the poor communities of the Dhaka region work a variety of jobs to earn money, including sewing, working as cooks or maids in other people's homes, managing small businesses, and owning pets and selling their milk in remote union councils. Some also work in agriculture. These underprivileged people frequently lack knowledge of bank loan schemes and are wary of approaching important institutions. They frequently struggle to obtain loan paperwork, read it, and understand its requirements. Microfinance initiatives are therefore the only option left, as they visit the homes of the poor and make it easier for them to apply for loans. Additionally, due to the small quantity of these loans, low-income people.

3.1 The theoretical foundation of the study

Microfinance is the study's independent variable. The initial loan cycle and the higher loan cycle serve as its dependent variables. The control group refers to those who would benefit from the first loan cycle, whereas the treatment group refers to those who would benefit from the second loan cycle. Social, psychological, and economic empowerment are the three sub-determinants that make up women's empowerment.

3.2 The study is supported by the following theory.

The whole empowerment of women—including their social, economic, and psychological empowerment—benefits from microfinance loan cycles.

3.3 Data collection technique

Primary and secondary sources of data were used to collect the data for this investigation. An important source of data is questionnaires. The questionnaire is based, among other things, on observation and interviews. The secondary data for this study was acquired from secondary sources such as press releases, company reports, and financial statements. Processes and procedures used in this study include population, sample size, data collection method, and data analysis.

3.4 Population

Women who have benefited from three labor union councils in the Dhaka area are the source of the data. Between March 1 and March 31, 2021–2022, 900 active beneficiaries from the aforementioned union councils were recorded. 900 active beneficiaries make up the population for this study (SDF, 2021-22).

Profile	No. of Respondents	Mean	Standard Deviation
Married with children	75	2.67	0.97182
Unmarried	25	2.36	1.034209
Widows	30	1.78	0.43213
Married without children	20	1.35	0.47091

The accompanying table demonstrates that married women with children make up the majority of those who make use of microfinance programs. They need such little loans to launch their businesses and give their kids a better life.

3.5 sample size and sampling technique

The data would be acquired using a straightforward simple random sampling strategy. Women will actively participate in this study, the sample size is 150 females.

Formula Z 2 * (p) * (1-p)

for calculating sample size

ss = c 2

The Z number indicates the degree of confidence (for example, 1.96 indicates a level of confidence of 95%). In this example, p is expressed as a decimal (0.5), and it represents the probability of choosing a course of action. The confidence interval, abbreviated c, is also expressed as a decimal (for example, 0.05).

3.6 Data Gathering Device

A self-administered structured questionnaire with a 5-point Likert scale will be used to collect the data. From 1 (strongly disagree) to 5 (strongly agree), there is a scale.

How to create a questionnaire

A range of questions on the survey are intended to collect background information from respondents. Age, the number of family members, education, living conditions, income, and saving were among the topics covered in the questionnaires. There are multiple-choice questions (MCQs) on the survey. The one that best fits their reaction is to be chosen, the participants are told. Some inquiries only accept a yes or no answer.

3.7 Analysis of data

The SPSS application SPSS20 was used to examine the survey's data. To find the frequency distribution, graphical elements, and percentage, descriptive statistics were utilized. In order to determine the link between various variables, Pearson correlation was used. An ANOVA was performed to investigate how microloan cycles affected women's empowerment in one aspect. Economic, social, and psychological empowerment were all evaluated using an ANOVA.

3.8 The moral worth of society

Prior consent was obtained from respondents to participate in filling out the questionnaire, taking into account societal values and research ethics. They received thorough explanations of every element of the questionnaire and assurances that their identities would be kept confidential. They had ample time to read the questionnaire carefully and complete it in a leisurely manner.

Chapter 4: Results & Discussion

4.1 Introduction

SPSS 20 was employed to analyze the data gathered from the questionnaire. There are two sections to the chapter. Descriptive statistics, which are used to create graphs and tables as well as to ascertain frequency distributions, are discussed in the first section of the chapter. We are provided with the correlation between the dependent and independent variables in the second half of the chapter. ANOVA is one method that has been used to test the hypothesis.

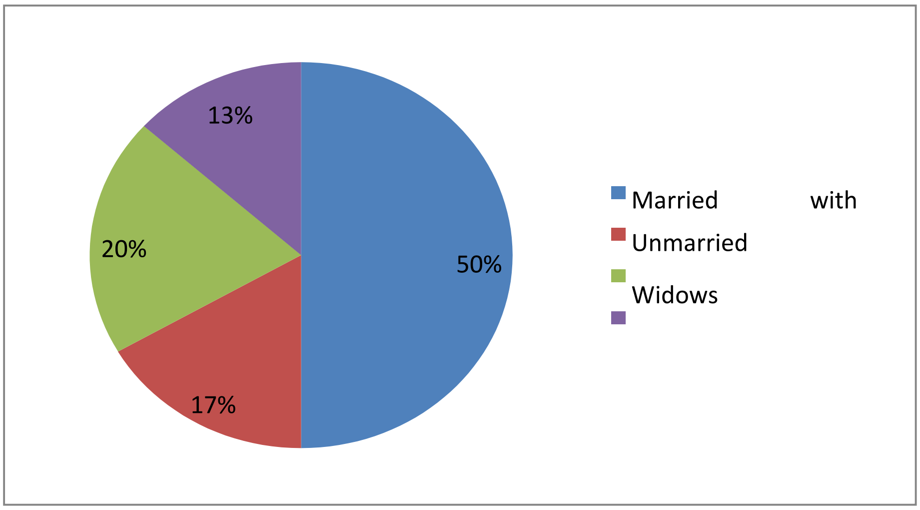
4.2 Demographics of the sample

To determine the demographic characteristics of the data, a descriptive analysis was performed. For this, percentages and pie charts were employed. The respondents' various age categories are shown in Table 4.2.1. A total of 150 females were chosen as responders; of them, 40 were between the ages of 36 and 50, 80 were between the ages of 28 and 36, and 30 were between the ages of 17 and 28. The pie chart that is shown represents the percentage of each group.

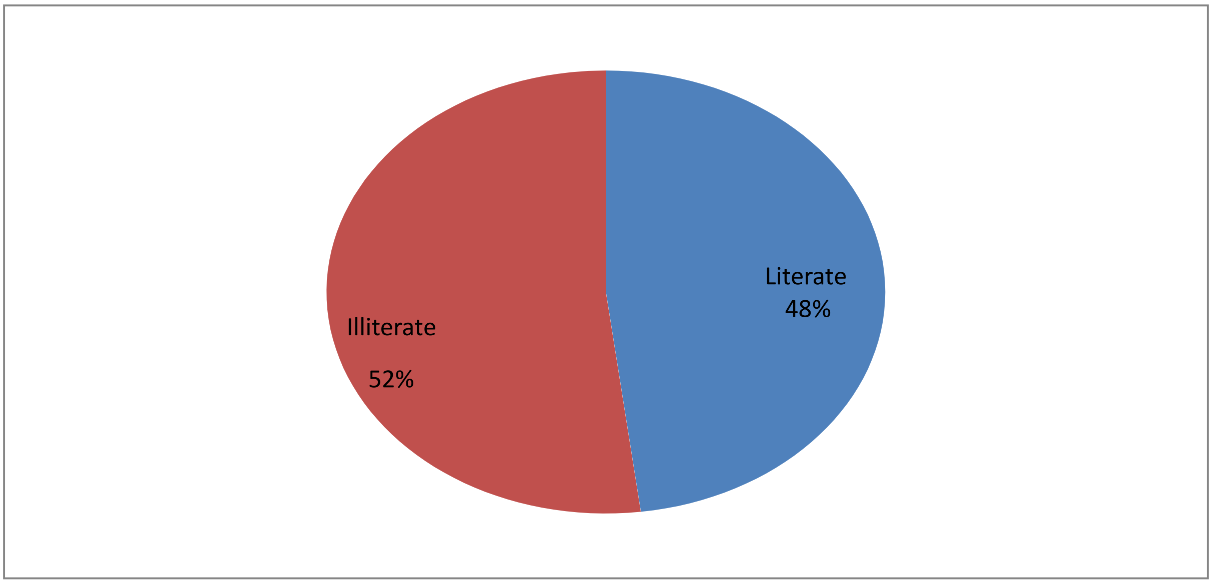
4.3 Based on marital status, distribution

Table 4.2.2 based on their marital status. The frequency distribution of respondents is shown 75 of the female participants were married with kids; 25 were single; 20 were married but had no kids; and 30 were widowed.

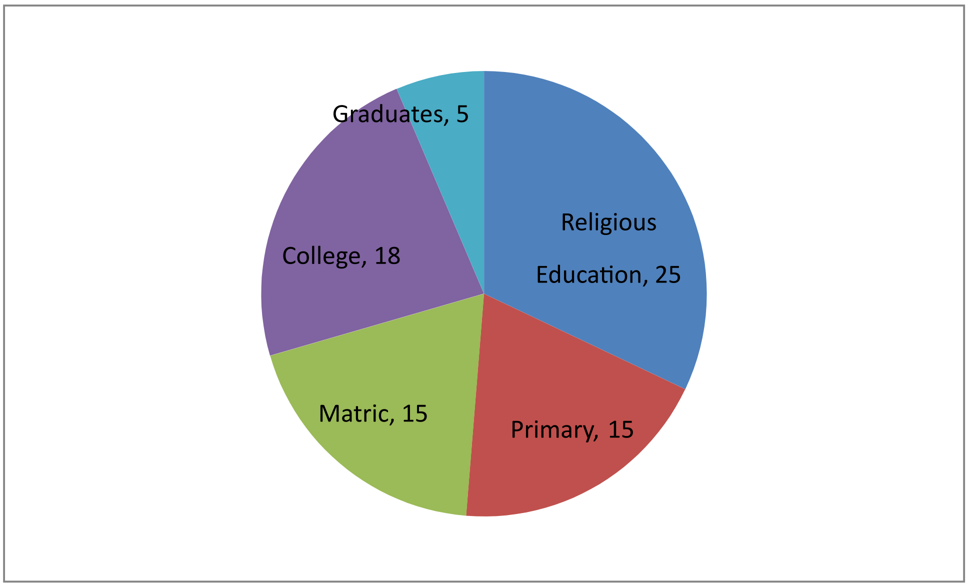
Profile	No of Respondents
Married with children	75
Unmarried	25
Widows	30
Married without children	20



The respondents were also divided according to their level of literacy. Nearly 48% of the 150 respondents were illiterate, while 52% were literate. The pie chart depicted in Figure 1 illustrates the percentages of education.

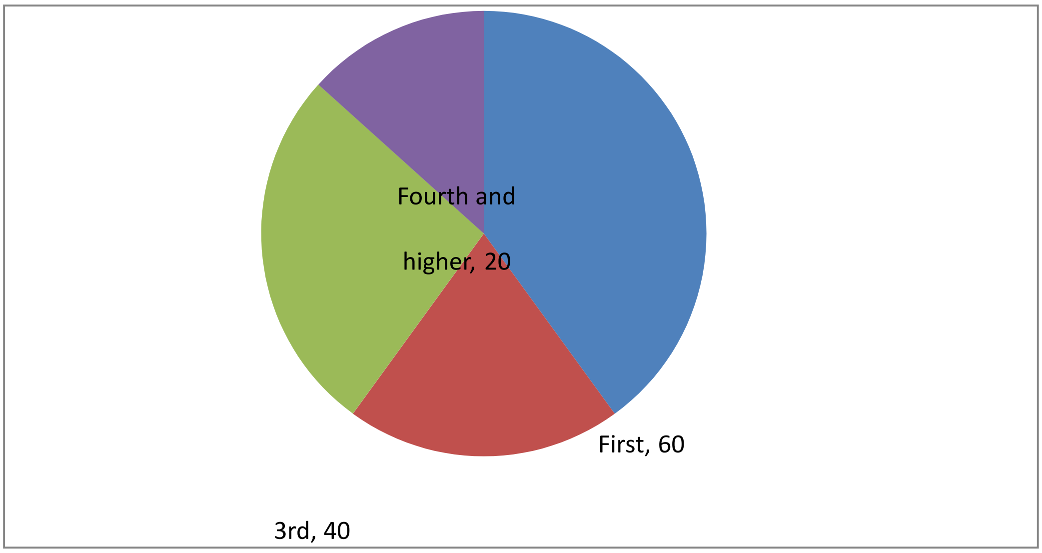


The following pie chart illustrates the respondents' overall educational attainment. A total of 72 women lacked any form of literacy. 25 had only received religious instruction; 15 had received instruction only through primary school; 15 had received instruction through middle school; 18 had received instruction through college; and 5 had received just graduate-level education.



The table below displays all of the loan cycle information that each respondent was able to gather. Out of all the responders, about 60 were part of the first loan cycle because they were the ones who had previously gotten loans. Twenty respondents were in loan cycles 4 and higher, while about 30 were in loan cycles 2 and 40 were in loan cycles 3. The chart displays the percentages of all of these responders in each loan cycle.

S.No.	Loan Cycle	No. of respondents
1	First	60
2	Second	30
3	3rd	40
4	Fourth and higher	20



Using Cronbach's alpha and SPSS 20, the reliability coefficient was determined. This was calculated to discover the strong association between the different questions asked. The statistics for Cronbach's alpha and reliability for each respondent are displayed in the table below. These analyses reveal a strong correlation between microfinance loans and women's economic, social, and psychological empowerment.

Dependent variables	Loan cycle (LC)	No. of respondents (N)	P-Value	Mean
Women social empowerment	1 2 3 4 and above	60 30 40 20	0.0005	3.5223 3.5921 4.2134 4.3455
Women economic empowerment	1 2 3 4 and above	60 30 40 20	0.0067	3.7132 4.1287 4.2623 4.4412

Women psychological Empowerment	1	60	0.0054	3.6919
	2	30		4.3128
	3	40		4.7734
	4 and above	20		5.2245

4.4 One-way analysis using ANOVA

The average levels of women's social, economic, and psychological empowerment and loan cycles were compared using the ANOVA method. The first, second, third, fourth, and subsequent loan cycles were regarded as independent variables, while the study took into account the social, economic, and psychological empowerment of women as dependent variables. The results are shown in the table below, which highlights the beneficial effects of loan cycles on women's empowerment by showing an increase in total female empowerment with each loan cycle.

The dependent variables—women's social, economic, and psychological empowerment—as well as the independent variable—loan cycles—are shown in the table. There were 60 responders for the first loan cycle, 30 for the second, 40 for the third, and 20 for each of the future credit cycles. Women's social empowerment had a mean value of 3.52 in the initial loan cycle, rising to 3.59, 4.21, and 4.34 in the subsequent loan cycles, respectively. These results imply that microfinance initiatives contribute to the social empowerment of women.

In the first loan cycle, the mean value for women's economic empowerment was 3.71; in the second, 4.12; in the third, 4.26; and in the fourth and succeeding loan cycles, 4.44. This proves.

This demonstrates the beneficial impact of microfinance programs by showing how women's economic empowerment improves as loan cycles move forward.

The mean level for women's psychological empowerment varied from 3.69 in the first loan cycle to 4.31 in the second, 4.31 in the third, 4.77 in the fourth, and 5.22 in the succeeding loan cycles. The mean value of women's psychological empowerment has a constant increasing trend as loan cycles progress, highlighting the highly positive impact of microfinance programs on women's psychological health.

4.5 Limitation and scope for the future study

The purpose of the study was to determine how microfinance affected both economic expansion and poverty alleviation. Due to time, distance, and cost constraints, the study would have planned to cover Dhaka. The Dhaka region not included here will also benefit from this study's findings in the similar way. Using tiny loans, self-help organizations mostly made up of rural women are formed using the microfinance technique to engage in modest economic activity. The goal is to equally distribute the advantages to the group's participants, promoting both social and financial independence. Small and medium-sized enterprises (SMEs), on the other hand, are business-focused organizations with larger investments that strive to support people's entrepreneurial potential. SME operations, in terms of scope and funding, take place at a macroeconomic level. Microfinance operations in Dhaka, Bangladesh, have virtually stopped due to accumulating past-due bank borrowings. As per typical, the sanctity under which SHG-based microfinance programs were initially established in the late 1980s has been compromised by the presence of politicians. Only powerful NGOs could keep up microfinance operations with strict oversight and rewards. But there are only a few of them. NBFCs may not have a positive experience in some locations where they operate.

Institutions that provide microfinance are crucial to a nation's development. They offer low-income individuals who depend on moneylenders charging excessive interest rates an alternative source of funding. Although I can't argue that they aid in lifting individuals out of poverty, they do save them from sinking any further. Microfinance organizations might be extremely important to the growth of small-scale industries. But this approach still has a lot of flaws. If these institutions are to function well, the BRAC must create some sound regulations.

Chapter 5: Conclusion & Recommendation

5.1 Conclusion

According to the study's results, the majority of respondents are in favor of starting and growing microfinance initiatives nationwide, especially in the Dhaka region. According to calculated data, microfinance is a successful tool in the fight against poverty. In addition to assisting economically disadvantaged people in generating income, microfinance also helps them raise their social standing. According to 55 out of 68 respondents (80.88%), microfinance is a very effective strategy for achievement. The adoption of microfinance also enhanced purchasing power. The majority of the research's conclusions, which are consistent with past studies, indicate that microfinance can aid people's efforts to escape poverty. Islamic microfinance is also helpful in the fight against poverty, especially in Muslim countries like Pakistan.

5.2 Recommendations

- If microfinance institutions set up their own business and have the freedom to decide how to divide profits, they may be able to earn bigger profits from interest payments.
- A determined effort is required to inform the impoverished, especially illiterate villages, about microfinance programs.

The need for lower interest rates arises from the fact that consumers are being burdened with higher interest costs. Because microfinance programs are currently mainly centered in metropolitan areas, access is restricted. Expanding the number of microfinance institutions in rural areas is essential to ensuring greater accessibility.

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Appendix

Impact of Microfinance on Emerging Economies' Economic Growth and Poverty Reduction

Section 1: Background of Respondents

1. Date of Interview_________________________________

2. District_________________________________

3. Group Name_________________________________

Section 2: Microcredit Information

4. How long have you been in the AIM scheme?

a) Less than one year

b) 1-2 years

c) 2-3 years

d) 3-4 years e) 4-5 years

5. **How many cycles of the AIM microcredit have you completed**? ____________

Section 3: Demographic Information 6.

How old are you? ___________________

a) Between 17 and 28
b) Between 28-36
c) Between 36-50

7. How many years you spent in education? ....

a) Not educated at all

b) Less than 5

c) 5-10 years

d) 12 years

e) Above 12

8. How many children have you had before joining AIM scheme? ------------------ a)

Unmarried

b) Married but no children

c) 1

d) 2

e) More than 2

9. How many children do you have now? ---------------------

a) Unmarried

b) Married but no children

c) 1

d) 2

e) More than 2

10. How many children do you have in school?

a) Unmarried

b) Married but no children

c) 1

d) 2

e) More than 2

11. How many members who live with you in your house? ---------------- a)

0

b) 1

c) 2

d) 3

e) More than 3 Section

4: Socioeconomic Information

4-1. Saving Information 12.

Do you make any saving?

a) Yes

b) No

c) Sometimes

d) Most of the time

e) Never

13. If yes, where do you always put your savings?

a) Bank account

b) In house

c) Community saving service

d) Others/ please specify…………………….

4.2. Business Training

14. Have you received any training before joining group lending? a) Yes b) No

15. If yes, please indicate to the type of the training………………..

Section 5: Livelihood

5.1. Household Income

18. How much do you estimate the average monthly income of your household? -----------

5.2. Household Assets

19. How much did you spend on household assets, in the last year? ………………….

20. Please indicate to the type, quantity and the price of the following assets that household purchased past one year.