A Conceptual Framework of Missing Links to Rural Poverty in Pakistan

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Microfinance institutions focus on the microcredit and forget about the other services such as microsavings, deemed necessary to eradicate the poverty. It is worthwhile to look at the economic problems of the people living in rural areas of Pakistan and to analyze if lack of funds is the only barrier to their economic well-being. The objective of the paper is to establish a need of the poor and develop a conceptual model of poverty alleviation where financial services including microsavings are linked to other non-financial interventions for successful and sustainable rural economic development.

INTRODUCTION

Poverty is more acute in rural than in urban areas since rural households rely mostly on agriculture as their main source of income (World Bank, 2004). Things are not much different in Pakistan. Based on a poverty line of $ 2 per day, more than 75% of Pakistan's population is living below the poverty line. The underprivileged rural communities in Pakistan face a lack of resources in the form of financial services, information and market access. Although in last few years the number of NGOs and banks which offer financial services in low income communities of Pakistan has increased manifold. But, their services have been limited to a small amount of loans and to some extent microsavings services. Microfinance is now widely used tool to combat poverty all over the world, but debate still remains as how economic efficiency of the low-income people can be improved in a more sustainable manner.

The aim of this paper is to develop a workable model of poverty alleviation on sustainable grounds. Thus, the paper attempts to find missing links and bridge the gaps which have not been addressed in earlier poverty alleviation strategies. In particular, this study will assess the need for (a) business development services (BDS) and (b) microsavings among rural households of Pakistan.

LITERATURE REVIEW

Thorough review of world literature on poverty alleviation strategies suggests that there are two types of services that have not been incorporated or remained missing in the poverty alleviation models. So, the first relates microsavings services that have been served half heartedly by the current financial systems. Traditionally, microfinance focuses on providing a very standardized credit product (Rutherford, 2000b). However, the poor, just like anyone else, need a diverse range of financial instruments to be able to build assets, stabilize consumption and protect themselves against risks (Matin et al., 1999). Thus, the broader concept of microfinance is needed to meet the current challenge of finding efficient and reliable ways of providing a richer menu of microfinance products.

The second set of missing services includes non-financial services. Nitin Bhatt 2001 emphasized on the need for understanding of the cause of poverty. Poverty is not only caused due to the lack of funds but also the lack of education and technical skills, poor knowledge and access to markets for making rational decisions contribute significantly to the menace of poverty (Lashley, 2004; Dunford, 2001). People living in abject poverty, especially in rural areas of developing countries, have a little or no education, poor access to markets, unreliable infrastructure, lack of access to information resources, inadequate technical skills, inability to perform simple mathematical calculations, poor sanitation and health facilities and no access to clean drinking water, they struggle on daily basis to earn their livelihood (Ruben and Clercx, 2003; Rutherford, 2003b). The poor in rural areas are small farmers, street hawkers, small shopkeepers, daily wage laborers and low paid contractual workers who are fighting to cope with hunger and poverty (Rutherford, 2003b).

Harper (2003) argues that “not all micro debt produces favorable results, especially for poor people working in low return activities in saturated markets that are poorly developed and where environmental and economic shocks are quite common." Even after years of microfinance efforts, there is a gap between supply and demand for microfinance services. Millions of families are still lacking saving accounts facilities and other financial services like transfer of payments. Microfinance institutions (MFIs) solely focus on disbursing loans and that industry has tried to force every saver to be a borrower (Helms, 2006). As a result, MFIs miss the segment of the poor population “who may wish to save but do not necessarily wish to borrow" Buckley (1997).

While the credit bias in development finance from the 1960s onwards has never given way to a savings bias, despite a widespread demand for savings services among the poor, savings are no longer `the forgotten half of rural finance'. [. . .] However not all donors have learned that lesson: that the poor need both savings and credit services; but more of the poor need savings deposit facilities than credit." (Harper and Arora, 2005).

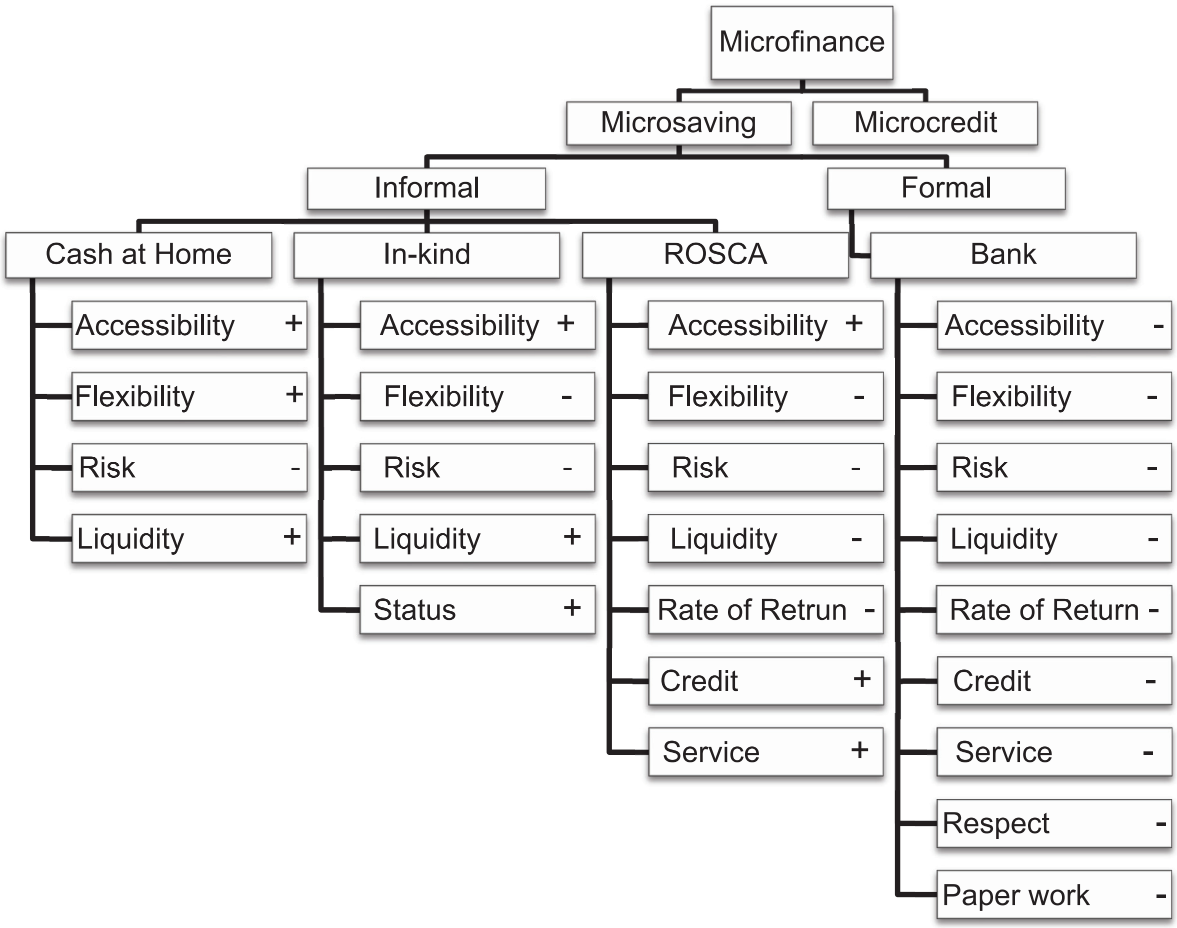
Poor households without access to safe saving accounts are forced to save in the informal saving systems where their savings can be stolen or lost (Rutherford et al., 1999b; Mary Kay, 2003). Poor households would also like to have safe, convenient saving accounts for different reasons, like sending their children to school, paying for health facilities or starting new business enterprises (Collins, 2005). For the poor, secure and accessible savings are at least as important as loans" (Harper and Arora, 2005).

For microloans, the MFIs need credit worthy clients but, for microsavings, clients ask for trustworthy institutions (Robinson, 2004). UNDP (2006) report suggests that people living in developing and low income countries have low access to much needed financial services than the developed world. A number of studies have highlighted the impact of microfinance as a package of microsavings and microcredit mitigate the risks which rural households face in the life cycle (Moll, 2005). Jaffrey Ashe (2002) termed the impact of savings led microfinance as substantial to gain higher respect in family, increase in income and assets. Gaiha (2001) has also termed the savings as insurance against the economic shocks for the rural poor.

Microfinance is all about the efforts to provide the financial services to the poor through mobilizing deposits locally and receiving them as a loan to low-income clients (Dieckmann, 2007). Poor people want to save but formal banks are not interested in small amount of savings. Consequently, they enter into a risky venture where they can lose their hard earned income - stolen, theft, ruined by flood or fire and animal may get sick and die (Helms, 2006).

The facts and figures available in UNDP (2006) report gave rise to some fundamental questions: Why are people in developing countries “unbanked"? Do they have saving capacity and do they want to have a safe place to save, and if yes, then why do they not save in formal financial institutions? A number of studies are available on the saving methods of poor people in different parts of the world. Literature suggests that cash at home, Rotating Savings and Credit Association (ROSCA), keeping livestock as money, purchasing raw material for construction, hoarding grain for food security and lending money to friends or relatives are some of the common saving practices (Robinson, 2004; Rutherford, 2000a; Hannig and Wisniwski, 1999; Isabel, 2004). These saving practices in the informal system raise a fundamental question of why people opt for informal saving mechanism over formal and what factors contribute to their decision for not saving with banks.

FIGURE 1
FACTORS THAT CONTRIBUTE TO THE DECISION, WHERE TO SAVE



Source: Author's own compilation

Since efforts are being made to include the poor in formal financial system, the figure (1) depicts well that what are the factors that contribute to the decision of using formal or informal financial system. In the informal saving mechanism people used to save at-home, in-kind and ROSCAs while formal financial systems are considered as commercial banks. Low-income people save in different methods for different reasons. In figure 1 (+) sign means positive reason or advantage to save and (-) sign mean negative association or disadvantage of saving in the particular saving method. Informal saving methods are more accessible, flexible, liquid and add to the respect of saver in the society. The poor people's perception about formal financial system is negative and they and they do not find any reason to save in banks. Even people feel risk of losing their money in banks.

EXISTING MODELS AND PRACTICES

Rutherford (2003a) has analyzed the microfinance models in detail and have illustrated that during the last 50 years, microfinance has gone through three approaches (see Table 1). In 1960s, governments started providing cash and kind loans to rural small farmers. Governments heavily subsidized these loans to modernize agriculture base. This approach is known as `Development finance approach'. This development approach acknowledges agriculture sector as the important element that can contribute to GDP growth of the country. The financial system that was started a decade ago took a different turn in 80s and started loaning to women for micro-enterprises. This development intervention acknowledges women as the forgotten half of the poor and known as `Microcredit approach'. The last decade (2000 - 2010) had to face many questions and development strategies as microcredit moved on to microfinance. By providing microcredit to the poor; it was recognized that the poor are the forgotten half of the population; landless women were better qualified for loans than male land owners, likewise informal business was recognized as the forgotten half of economy. Practitioners and academics started to question why the poor only need microcredit and do not need other financial services like microsavings. This critical questioning was an acknowledgment to microsavings as the `forgotten half of microfinance'. Why cannot the poor enjoy individual financial services? This style of intervention is called the `Financial services approach'.

Traditionally, microfinance focused on providing a very standardized credit product (Rutherford, 2000b). However, the poor, just like anyone else, need a diverse range of financial instruments to be able to build assets, stabilize consumption and protect themselves against risks (Matin et al., 1999). Thus, the broader concept of microfinance is to meet the current challenge of finding efficient and reliable ways of providing a richer menu of microfinance products.

TABLE 1
MICROFINANCE APPROACHES DURING THE LAST 50 YEARS

	The Development Finance Approach	**The Microcredit Approach**	**The Financial Service Approach**
Target	Men	Women	Poor Households
Uses	Farming	Micro-enterprise	Any
Key Products	Cash and kind loans	Micro-loan	Current accounts, savings, loans, insurance, pensions, remittance
Delivery	State DFIs and co-operatives	Solidarity groups	Individuals and groups
Financed from	Public subsidy	Grants and soft loans	Deposits, loans and retained earnings
Peaking	1960s-1970s	1980s-1990s	2000-2010

Source: Rutherford (2003a)

As we broaden the notion of the types of services microfinance encompasses, the potential market of microfinance clients also expands. For instance, microcredit might have a far more limited market scope (Rutherford et al., 1999a) than a more diversified range of financial services which would include various types of saving products, payment and remittance services, and various insurance products. For example, many poor farmers may not really wish to borrow but would rather have a safer place to save (Harper, 2003).

TABLE 2
EXISTING PRACTICES IN PAKISTAN

	The Development Finance Approach	The Microcredit Approach	The Financial Service Approach
Practices	Zari Taraqiati Bank Ltd. (ZTBL)	Rural Support Programs(RSPs)	Microfinance Institutions(MFIs)

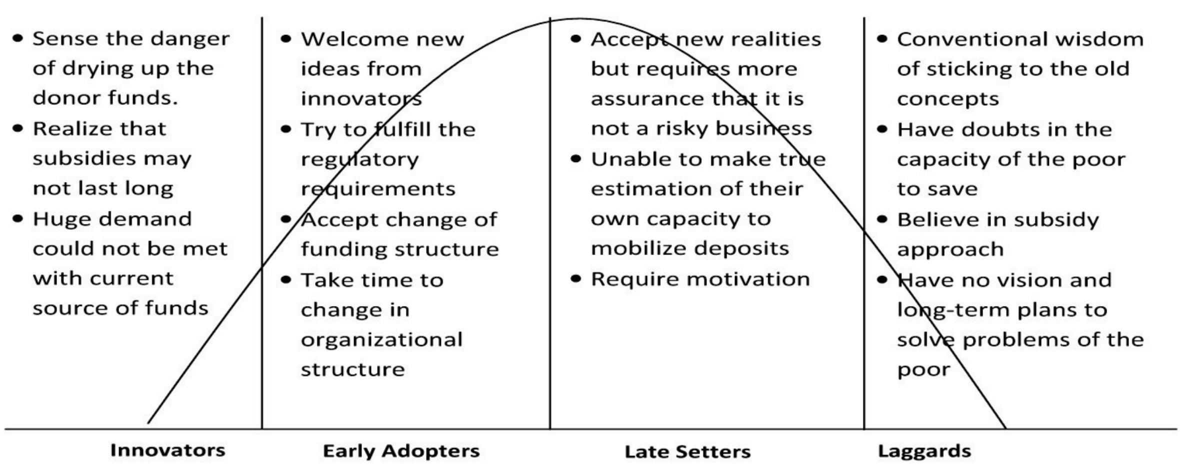
Source: Author's own compilation

Worldwide acceptance of microfinance as a poverty alleviation tool clearly began in Pakistan with an increasing number of NGOs and microfinance institutions (MFIs). Pakistan has an estimated target population of 25-30 million poor clients but PMN (Pakistan Microfinance Network) members have yet reached only 5% of this target population (Haq, 2008). Only 10% of savings accounts are maintained by `Intermediators' while 90% of them are maintained by Mobilizers, where savings are deposited with commercial banks only. When we look into the overall microsavings portfolio, the Pakistan Post emerges as a key player in deposit mobilization with a 78% share in small savings markets, followed by ZTBL with a 9% market share (Duos et al., 2007). This shows that Pakistan microfinance sector is still practicing "the microcredit approach" only and has not paid much attention to the other needed services. There is a long way to go and an urgent need to accelerate this growth, if one wishes to achieve the first millennium development goal of halving poverty by 2015.

Deposit mobilization services have not been extended to poor clients. It is a common practice by MFIs to ask client to deposit 10% of the credit amount in any commercial bank before they can use the credit facility. This compulsory savings is one of the reasons for the low average savings balance of Rs. 901 with mobilization. So, figure of 1.5 million savers would never mean that MFIs are offering savings products. There is a need for microfinance institutions to offer more diverse financial services ranging from credit to savings and insurance services for their clients.

The microfinance financial service era gave rise to the importance of saving services but a large number of MFIs still stay away from this new development. There could be many reasons of not offering the saving services but in general this attitude of MFIs can be grouped into four categories (see Figure 2). There were few innovators who stepped forward and started deposit mobilization on their own while others were relying on donor funding or government subsidies.

FIGURE 2
MFIs AND MICROSAVINGS DEVELOPMENT CYCLE



Source: Author's own compilation

Now we come to another crucial cross road; the question is raised if financial services are the only or major constraint in doing business for poor people. It should be kept in mind that poverty is not only the lack of funds but also the lack of education and technical skills, information and poor access to markets and lack of the knowledge needed to make rational decisions.

Not all micro debt produces favorable results, especially for poor people working in low return activities in saturated markets that are poorly developed and where environmental and economic shocks are quite common" (Harper, 2003).

A poverty alleviation strategy has to incorporate non-financial services. This approach is named "the financial service plus approach" (see Table 3). At times, these non-financial services are also known as business development services" which includes technical skills, market access, input supply, technology information, price information and marketing of the produced products (ADB, 1997).

TABLE 3
THE FINANCIAL SERVICE PLUS APPROACH - MICROFINANCE OVER THE NEXT 10 YEARS

	The Development Finance Approach	**The Microcredit Approach**	**The Financial Service Approach**	**The Financial Services PLUS Approach**
Target	Men	Women	Poor Households	Rural Households
Uses	Farming	Micro-enterprise	Any	Value Chain Development
Key Products	Cash and kind loans	Micro-loan	Current accounts, savings, loans, insurance, pensions, remittance	Financial services, Business Development Services
Delivery	State DFIs and co-operatives	Solidarity groups	Individuals and groups	Household and Community Projects
Financed from	Public subsidy	Grants and soft loans	Deposits, loans and retained earnings	Community Savings Reinvestment
Peaking	1960s-1970s	1980s-1990s	2000-2010	2010-2020

Source: Adapted from Rutherford (2003a)

The institution can facilitate the shortcomings of small business developments. Financial deepening of MFIs would be more fruitful when grouped with non-financial services. Synergy of MFIs and BDS (Business Development Services) Providers has enough potential to trigger growth and lead the poor out of poverty (Downing et al., 2006).

A lot more research about BDS effects on micro enterprises and the life of rural people is needed. One such study by Mc Karman (2002) has found a strong impact of microcredit programs when offered with non-financial services. The firms which took vocational training and market link services by some BDS providers had been earning more profits than others. But much more scientific work is needed to study the impact of BDS on poverty (Marten and Paul, 2007).

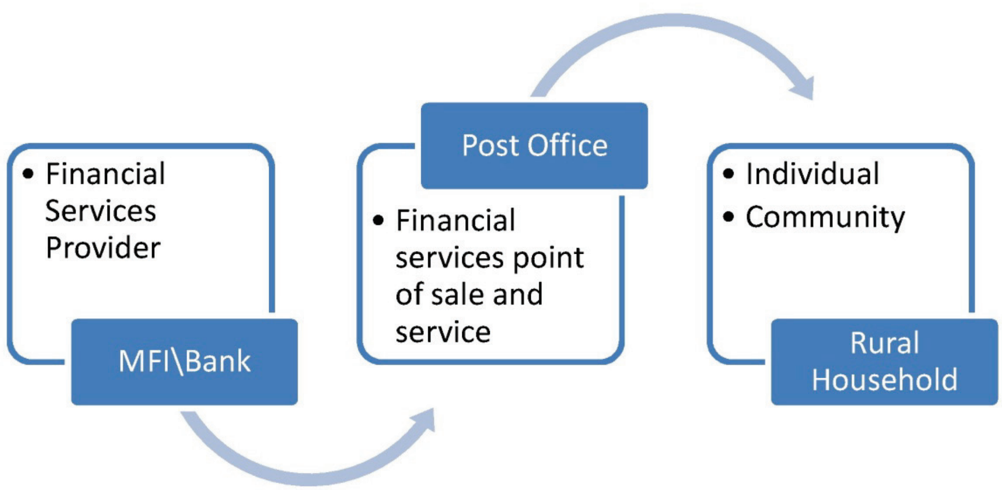
PROPOSED MODEL AND PRACTICAL IMPLICATIONS

The recent innovations in the financial sector, microfinance institutions possess some, but not all of the resources needed to address the constraints that are faced by the rural community. With the possible exception of providing a richer menu of financial products like microcredit, microsavings and transfer of payments, non-financial services like links to markets, access to information and infrastructure are beyond their domain. While there are different perspectives on the delivery of financial and non-financial services, the proposed model will address the following two questions:

> 1- *How existing financial institutions including MFIs, can offer the most demanded products and still remain financially viable?*

Microfinance services involve transactions of small amount in huge volume such as loans, savings, remittances and other services. Although the demand and potential for microfinance services has been established, the delivery of small scale financial services could be a costly business within the traditional delivery model.

FIGURE 3
MICROFINANCE INSTITUTIONS AND PAKISTAN POST PARTNERSHIP MODEL



Source: Author's own compilation

In the proposed MFI-Pakistan Post partnership (See Figure 3), the Pakistan Post has a very important role to play while acting as an agent to the MFIs by selling products to the scattered rural population. The Pakistan Post is the most cost effective and efficient delivery channel. The following section will describe why the Pakistan Post has been considered central to the rural finance delivery model.

Pakistan Post and Rural Finance

A network of around 13,000 post offices (which is almost double the total number of bank branches in all of Pakistan) works in urban and rural areas to provide postal services and, among these, 10,650 post offices are working in rural areas all over Pakistan. The Pakistan Post, with its widespread network and traditional image of credit worthiness is poised to have the potential of playing an increased role in the rural finance market. The following three points show how the Pakistan Post can play an important role in rural finance:

> 1. The post could provide an agency function to commercial banks and microfinance institutions allowing them to open booths in post offices. Sharing expenses and common facilities will lower the overall cost of providing financial services to the rural population. Also, the banks can expand and provide products that the Pakistan Post is not normally allowed to provide because of existing regulatory regimes in rural areas.

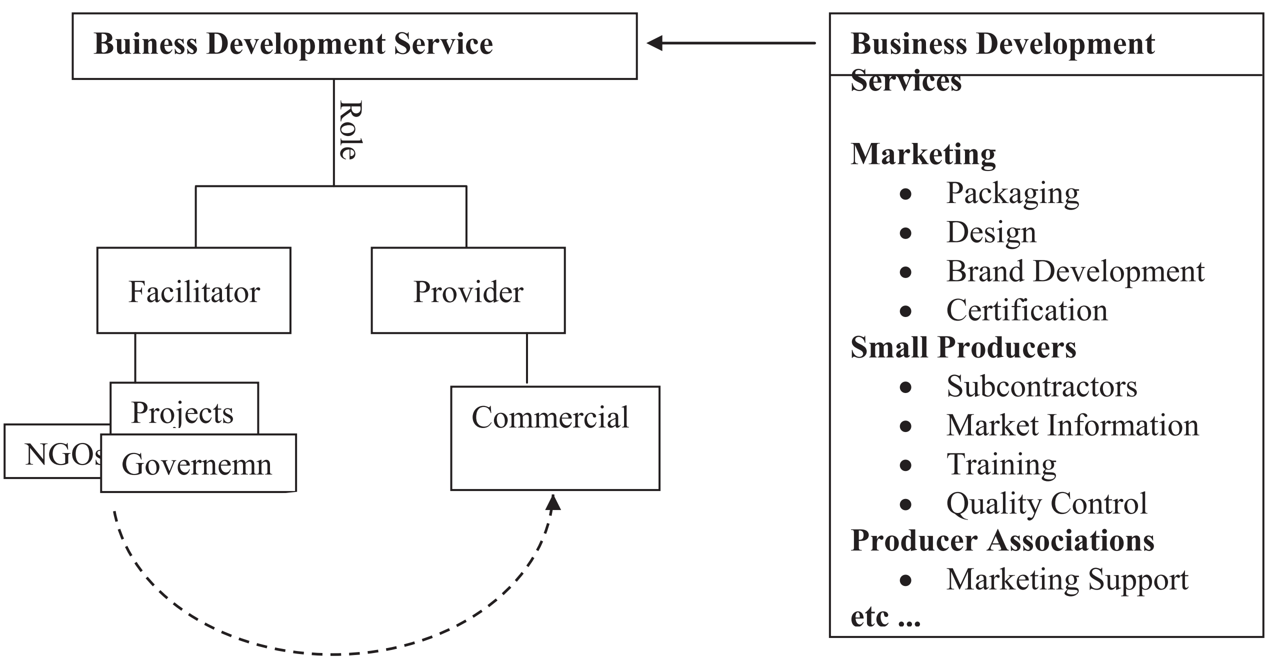
2. Capitalizing on the postal infrastructure and its credibility among the rural population, banks could increase access and outreach to quality, sustainable microfinance services for the poor and vulnerable population, especially in rural areas of Pakistan.
3. The Post office is already offering remittance services, payment services and is collecting utility bills from rural people and all of these services can be processed through saving accounts. Remittances and pensions can directly credit to personal saving accounts eliminating the need for people to wait in queues for long time. All these valued services will eventually have a positive effect on the savings of rural households.

In this way banks would be closer to their clients and Pakistan Post by utilizing its available resources including human capital will also benefit. Summing up, the Pakistan Post because of its firmly established in the fabric of the rural sector, can mobilize savings and provide financial services to those who have the least access to the banking sector.

2 - What other interventions are required to address the non-financial constraints of the rural community and strengthen the livelihood of the poor?

Non-financial constraints, such as lack of access to markets, market information; improved technologies etc., of the rural community present a challenging and complex environment. The objective to improve the living standard of the rural poor requires more and better understanding of their constraints. This better and more nuanced understanding leads to improving the system around the poor through innovative intervention that build upon and mirror local and home grown solutions.

FIGURE 4
BUSINESS DEVELOPMENT SERVICES, ACTORS AND THEIR ROLES



Source: Author's own compilation

The proposed intervention stresses the access to opportunities in the marketplace by providing market information, links to markets and by helping the uneducated rural poor meet quality standards at each level from input supplier to retailer. The listed services in the figure 4 are not intended to cover all the needed non-financial services, but a few services have been named that are required to the people living in distant areas. The proposed intervention of BDS involves number of actors playing two major roles namely `facilitator' and `provider'. The role of facilitator is vital in business development intervention. A number of bodies like NGOs, Projects and Government institutions intervene and provide the services in the beginning. The ultimate role of these bodies is of catalyst that brings the positive change in the market. Once these interventions enjoyed a significant success in building the markets links will open the avenue for commercial players.

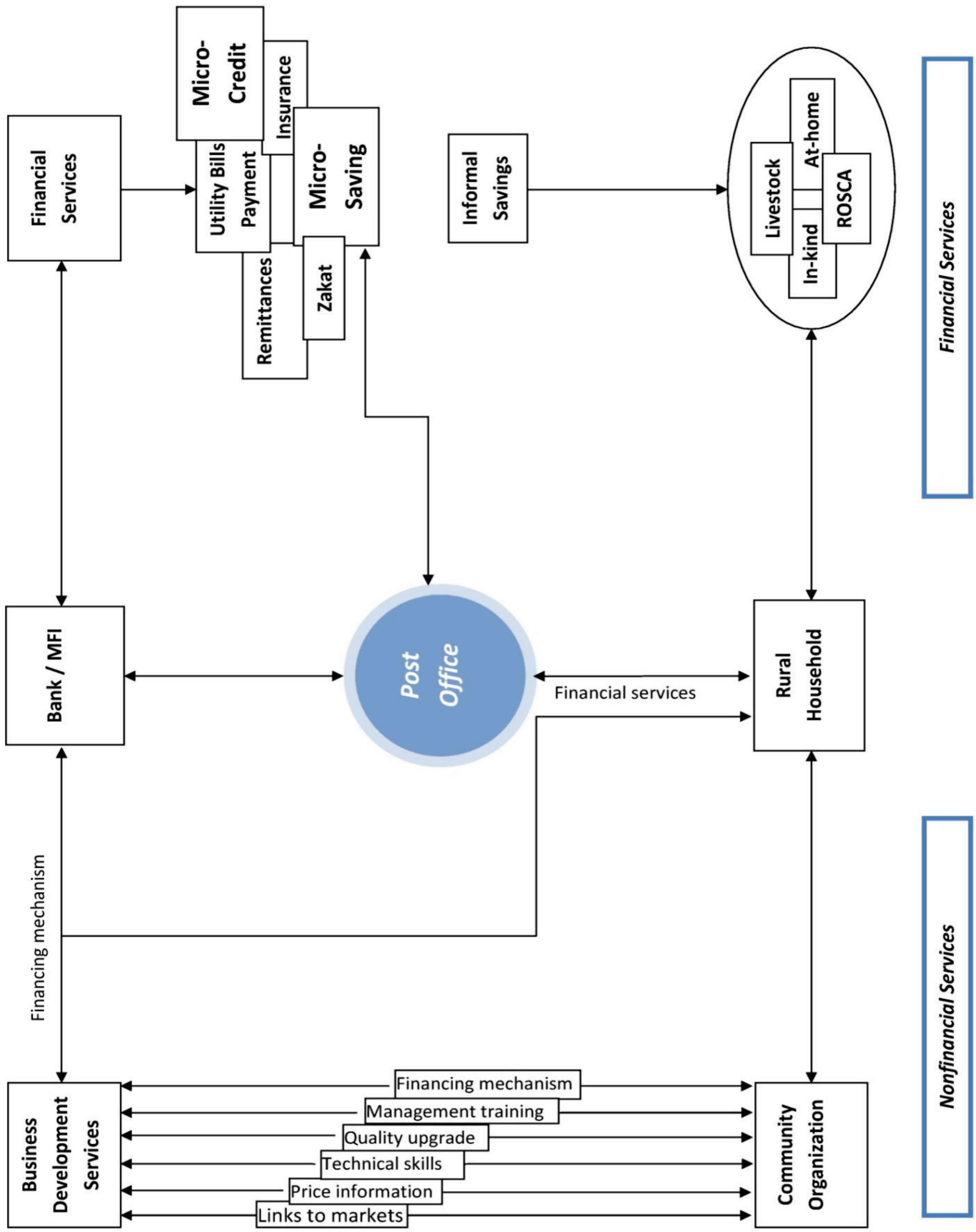
This success will facilitate the 'business development service providers' (NGOs, Industry associations, national government agencies etc) to come in and provide the different type of services under different delivery and payment mechanisms. This gradual transformation from business development service `facilitator' to `provider' is visible through the dotted line in the figure 4. It is vital to ensure that the services offered by the BDS providers meet the needs of poor rural communities. BDS providers that address the constraints of the rural community and contribute to their social and economic development could make a positive return on their investments and sustain their operations. This will shed the conventional thinking of the poor as in need of subsidies or as parasites to the economic growth. The ultimate objective of this intervention is of well functioning market with diverse range of high quality services.

On the whole, when the answers to the above two questions are assembled in one piece, they take the final shape in the poverty alleviation model (see Figure 5). The Poverty alleviation model focuses on pro-poor measures and outlines a community based and bottom-up approach to help the poor. This model envisages giving access to key services to the poor segment of the society with an effective delivery system at a grassroots level.

CONCLUSION

The expectation that word `poverty' would become history, if availability of funds is assured, amounts to an assumption that lack of capital is the only barrier to the economic development of the rural poor and that other operational constraints are either absent or can be addressed by increasing the availability of funds. The available literature indicates that apart from financial constraints, there are some other operational constraints as well that hinder the poor from enjoying the fruits of growth and from being integrated into the formal economy. Microcredit has a strong role as a poverty alleviation tool; however, it is underlined that poverty alleviation policy initiatives must not only broaden the concept of microfinance to include a richer menu of products, but also should help the people to overcome their non-financial constraints, links to markets, lack of information etc. The missing links to poverty alleviation strategy can be categorized into two broad categories (a) Financial services (b) Non-financial services. The rural poor people are just like anyone else, they need access to a diverse range of financial services. Although the existence of financial constraints cannot be denied, there are some non-financial constraints as well that usually have not given way to development interventions. Lack of infrastructure, poor information sources and underdeveloped, inefficient markets all hold back rural communities from reaching their full potential. Such problems cannot be solved by giving access to financial services through microfinance initiatives and need to be addressed directly. Small entrepreneurs and farmers deserve business development services such as developing supply chains, developing a strong process to maintain quality, in time supply, quality raw material, providing better design and networking them with microfinance windows to facilitate the initial investment they would require for small settings. Bundling financial with non-financial services and intervention with the existing infrastructure of the Pakistan Post as well as the newly established tier of private actors (business development service providers) will increase the income of rural households and, hence, enable them to improve their living standard and of the rural poor and come out of the vicious circle of poverty. On the whole, it is very simple and logical to conclude that, while access to microcredit is important to rural people, there is little doubt that rural people face many risks, and in these cases, well designed microsavings products and business development services could have an important development impact.

FIGURE 5
POVERTY ALLEVIATION MODEL



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