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FACTORS EFFECTING THE ELASTICITY OF MICRO CREDIT DEMAND IN SOUTHERN PUNJAB, PAKISTAN

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ABSTRACT

Purpose of the study: Microfinance institutions (MFIs) are delivering various services of microcredit, savings as well as insurance. The key objective of microcredit is to decrease the poverty level and for empowering the women as well as other poor people under various developing countries. There is the various factor which effects on the demand of microcredit. Therefore, the objective of the current study is to explore the factors which affect the demand for microcredit.

Methodology: In this conceptual study, the qualitative research technique was used. The data were collected from previous research studies and companies' websites.

Main Findings: It is concluded that numerous factors may influence the demand for microcredit by the various borrowers. These comprise the interest rate, the relationship between lenders as well as borrowers, different government policies, gender differences, prospective beneficiaries, the creditworthiness of borrower, transaction cost, limited access to credit, economic condition and the availability of information.

Applications: This helps analyze the barriers which the borrower and lender must face in operating the microcredit. In this way, microfinance institutions can take help from this study by considering these factors during the distribution of credit.

Novelty/Originality: The findings of this research study fulfilled the theoretical gaps in the literature by identifying the different fact which may help to revise the poverty level. Future research studies may focus on these factors, which may help to increase the economy and reduce poverty in southern Punjab, Pakistan.

Keywords: Government Policies, Gender Differences, Microfinance Institutions, Microcredit, Transaction Cost

1. INTRODUCTION

The role of microfinance institutions in poverty reduction and wellbeing of poor people has attracted the policymaker's attention in the developing countries across the globe as well as Malaysia (Al-Shami, Majid, Rashid & Hamid, 2013; Rashid, & Ejaz, 2019). The underlying logic is that by suing microfinance services, poor people take part in various income-generating activities, which enhances their well-being. It reduces the poverty level and increases the wellbeing of the participants. As it increases the economic activity of poor people (Hameed, Imran, Ślusarczyk, & Haque, 2019; Hameed, Mohammad, & Shahar, 2018; Ul-Hameed, Mohammad, & Shahar, 2018; UL Hameed, Nisar, Abbas, Waqas, & Meo, 2019).

Microfinance institutions (MFIs) are those institutes that provide various services to people without any access to the conventional banking system (Beisland, D'Espallier, & Mersland, 2019). These services include financial and non-financial services. Financial services include credit, saving and insurance. Non-financial services include training to facilitates micro-enterprise and social capital development activities.

Microfinance institutions (MFIs) are based on different organizations that play a major role in poverty alleviation. Microfinance refers to the various financial services provided to low-income people as well as disadvantaged households, who are not assisted by the conventional banking sector (Fenton, Tallontire, & Paavola, 2017). These institutions include microfinance banks and non-governmental organizations (NGOs).

2. LITERATURE REVIEW

A. Microfinance Institutions

After introducing the Grameen bank model by Muhammad Youns in 1974 in Bangladesh, microfinance emerged as a market, such as a feasible way to assess the needy and poor. In this program, small loans are given to the needy and poor people according to their demand or need. For lending loans, the borrower firstly arranged in a group and each member of the group act as a granter for the loan repayment of each other. Group liability

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and the regular repayments help in lending the loan without the requirement of collateral (Chaudhuri, nd). According to Conroy (2002), Microfinance is the wide range of financial services comprised services of payment credit, accepting deposits in accounts, lending loans transfer of money as well as insurance to the poor people.

According to Bastelaer (2000), microfinance institutions are providing financial services on a small scale, mainly the facility of savings and credit, to provide funds to those who have small businesses, who farm and fish, micro-enterprises where the things are produced, repaired, sold and recycle. The people who give their services, who only work for commission and wages, they earn the income by renting and providing the small piece of land, tools, vehicles machinery and also to those groups and individual belong from urban and rural areas (Robinson, 2001).

B. Microcredit

Microcredit can also be called micro-lending; it can be defined as "A very small loan given to poor people for helping them to be self-employed." It is given to poor ones for increasing the living standard of loan takers by investing it in income giving activities (Fernando, 2006). The microcredit is emerging globally as a more demand-driven, charging interest rates high, emphasizing and mobilizing the savings as a prerequisite for credit provision and also controlling the cost (Otero and Rhyne, 1994; Morduch, 1999). Microcredit is a very small loan for those people who want to start their own business and also help them to come out from a group of poverty. They have a lack of stable employment, collateral and certifiable credit history due to which they are unable to take formal credit (Nawai, 2010).

C. Purpose of Micro Financing and Credit

In developing countries, different NGOs and governments are using microfinance as an instrument to reduce poverty (Llanto, 2003). The primary purpose of microcredit is to deliver the money to very low-income people as well as the poor to use it in various activities of businesses and also for promoting their life standards. These loans are usually for a short period of time; loans are very small, mostly they are non-collateral bases and often required the weekly repayments. The obstacle which the financial institute faces for continuing the services of microcredit is the problem of repayment of loan. The reason is that mostly the micro-credit lending institutes are NGOs and non- governmental organizations. They are nonprofit leaning organizations. They get funds from donors and government (Nawai, 2010).

The poor are mostly disqualified for borrowing and availing the facilities of credit because they have to face the high cost of transaction and monitoring. To support the loan, they have insufficient collateral, low literacy low income. Usually they engage in informal and micro-business activities, including sale and processing of food, agriculture on a small scale, petty trading, craft and services. These activities contribute to gross domestic product and total employment to the country. In the third world, micro and small enterprises are considered as the major source of income and employment (Mead & Liedholm, 1998). According to World Bank that under three quarters and one-third of all employment in the under developing countries are mostly driven from informal sector (Webster & Fidler, 1996).

D. Micro Financing Institutions

With the passage of time, the number of banks and financial institutes entering in the market of micro-financing (Delfiner & Perón, 2007). There are many factors which are motivating the banks to deal with microloans. This is related to both the internal organization of the bank and the market in which it operates. However, one of the main incentives is related to the fact that is the high risk gives high profit. With the increase in competition the banks need to find the niche and do something change than the traditional operations. The countries in which there is no experience of microfinance, then there exists a market which is said to be the unattended market, this may become the source of positive return and growth for the bank (Delfiner & Perón, 2007).

The idea of microfinance institution suggested by then Muhammad Yunus, the purpose of this idea, is to eliminate the poverty from his country Bangladesh. In 1983 he initiated the Grameen bank; it is the first institution that used this concept and properly started micro-financing. Both Muhammad Yunus and Grameen Bank awarded noble prize for their efforts in micro-financing for increasing the social and economic development.

Microfinance lending institutions are mostly the NGOs and nongovernmental institute whose purpose is not to earn a profit. Mostly NGOs believe that Social procedures are the main cause of poverty among the poor which

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opposes the poor to their right to gain share of social resources such as availing the credit. So, these NGOs provide short-term loans to that poor people to investing in activities generating income and also in their small businesses. They act as financial intermediaries like formal banks. The main difference between the MFLs and the formal banking is that formal banking focus on rich client and the MFIs focus on poor client (Nawai, 2010).

Several Microfinance lending institutions provide the support in business such as advising on topics including sales, cash flow, accounting, pricing and costing, marketing and taxation they also help in making and developing the plan of the business. They provide support services after providing the loan (The Regulation of Microcredit in Europe, 2007).

A. Institutions provide the services of microfinance in Pakistan

- NRSP (National Rural Support Program) Microfinance Bank
- Kashaf Foundation
- First Microfinance bank
- Khushhali Bank
- Akhuwat Foundation.

B. Factors Effecting on Demand of Microcredit

A. Interest Rate

The interest rate on microfinance credit should be calculated on the base of these combinations of costs:

Credit price (interest rate) = Administration cost+ cost of capital+ cost of default (Johnson, 1997:51).

A lender can use the price of the loan in expanding the cheap access to borrower, if they decrease, he rates it reduces their profit but only by minute amount. They can use the cuts in interest rates in expanding their concerned customers. For example on average the poor people, as well as the females, are generally more sensitive to price as compared to the other people. Due to declining the interest rate increase the demand for loan by the poor and the females (Karlan & Zinman, 2008). With the decrease in interest rate the borrowing of loans by the poor females' increases (Chaudhuri, nd). The banks recognize that the increase in interest rate on marginal group would destroy the reputation of bank.

The main purpose of microfinance institution is to provide the loan to low-income household and poor people based on reasonable financial services. The main source of income of microfinance institutions is only the interest, so due to bearing high cost, the rates of interest on loan are comparatively high. Four major factors help in deciding the interest rate: the operating expense of microfinance institute, losses on loan, funding cost and the profit margin necessary for expanding the base of capital and for the funds which are expected for future growth (Fernando, 2006).

Though the high rate of interest helps in the growth of industry and provide the facility to millions of low-income houses, hold and poor to gain the credit, but there are still some needy people who cannot afford microcredit loan due to its high cost. Microcredit has not assessed by the poorest people and not widely utilized for financing agricultural activities. Only those people afford such high interest in microcredit that has the ability to generate an adequately high surplus (Fernando, 2006).

Karlan and Zinman (2008) argue that there is an assumption that is 'price inelastic demand' means that the borrower is indifferent to interest rate such that the lender can charge a bearable interest rate, so on this basis, the poor people demand microcredit is not affected. He made research on this assumption and found that a low rate increases the borrowing of females and the high rate decreases the repayment of loan.

B. Limited Access to Credit Services

A various factor with normal entrance to credit services has poor infrastructure, minute land holdings, and the nature of land term systems. According to Von Pischke and Adams (1980), lack of access to credit by those areas which have poor rural households has a negative impact on agricultural and nonagricultural output creation of input and for the benefit of family circle. (Diagne & Zeller, 2001). Lack of ability to obtain formal credit support has controlled poor farmers, facility to increase their output and get better their living conditions. The rural poor usually have little knowledge from where to get credit for their output actions. The poor people do not know how to invest and where to invest the loan. Additionally, formers have less approach to the banks. As the banks are generally located in city areas.

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C. Transaction cost

The transaction cost is one of the significant elements, which is the constraint to get a loan. The growth of microfinance institutions is trying to solve this issue. On the other hand once social capital is integrated, it should facilitate the poor's entrance and minor its costs, the transaction cost should be condensed and wellbeing should be improved by rising information flows (Bastelaer, 2000) terms of microcredit on sustainable basis to the poor and minimum income group consequently is important in order to attain the millennium development goal of halving shortage. In current time, a various factor has been recognized by authors as the input factor for demining the rural households on the whole demand for credit and the diverse credit sources.

D. Economic Condition

Microcredit provides the opportunity for poor people to invest capital in such activities help and generating profit. It provided the self-employment in the rural areas and helped the poor people to improve the economic conditions with the help of microcredit (TAJ, AKMAL, SHAH, AHMAD, & SADDOZAI, 2008).

The level of farmer's literacy, a domain of land under cultivation and their total income and revenue have a positive effect on microcredit demand (Bakhshoodeh & Karami, 2008). Support services such as Market information help in enhancing the productivity of microcredit loans. The economic factor includes various factors, which are inflation. Market condition, demand and supply factor, business environment, and consumer behaviour. These are those factors which create problem in getting loans. The microfinance, as a market-driven takes step to emerge in a practical way to arrive at the poor after Yonus initiate the Grameen Bank Model (GBM). This program introduces to provide minimum amount to the poor people according to their needs. Those people who give loans were set in groups form ad the group members stood as the guarantor for each other's loans. If the group members are responsible for paying back the loans, then no securities are requiring, and incomplete information should be solved related to this type of lending**.** Anggraeni (2009) is a current study on this subject where the author tries to find out the chances of being credit forced for SHG groups. This study found that group and individual characteristics incline the contribution in the lending programs. The similarity to groups, common profession and the income levels add to the achievement of the groups the economic conditions of the single members similar whether they the government employees, have they been the higher education and have a fixed income should influence the chances of contribution. Health, temporary usage requirements like weddings and debt/income ratio for the previous year considerably affect the chances of being credit controlled.

Anggraeni (2009) uses a big rural household review to analyze the demand side factors disturbing the outreach of Grameen style lending. Cheng finds that factors like household incomes, level education to female borrowers and entrance to the other sources of the formal lending influence outreach of such programmers. Demand for such loans determines from the opportunities of the off-farm investments. The results show that these programs have not just targeted the poor people automatically, quite the customers are improved off among the rural stacks. Further studying in Cheng is that the demand for credit is negatively correlated with the wage income of the poor households who have no speculation opportunity in the off-farm activities. This review paper shows the impact of microfinance on poverty falling as it relates to the first six out of seven-millennium goals Anggraeni (2009). Fernando, (2006) Grameen bank members have incomes round about 43% high than the objective group in the organize villages, and about 28% higher than the target group not contributed in the project villages. Bakhshoodeh & Karami (2008) documented that the Grameen bank should not only condensed poverty and enhanced benefits of participating but also superior the household capacity to continue their gains over time. Bastelaer (2000) note that the maximum rates of per capita income amongst microcredit programs, borrowers compare to those who did not borrow. Diagne & Zeller (2001) assert that men and women should contribute in BRAC that sponsor activities that have maximum income (that both in conditions of quantity and basis), possess maximum assets and are more frequently gainfully employed than as compared to non-contributing. Thus, demand-side factors are mostly linked to the income, education, health, profession and asset linked. The supply-side factors are associated with the cost of credit where the distance to the adjacent bank, the output of the crops (minimizes doubt of refund), future share of credit (policy-driven) and weather characteristics. A better width of inhabitants also helps decrease the cost of spend credit. NGOs engage in hobby a vital position in this procedure of connecting the possible borrowers to the lenders. On one give the NGOs help form the groups which make demand for credit services.

On the other hand, their turnout helps in examining the creditworthiness of borrowers and hence decrease the cost of borrow in what goes after we would first hypothetically inspire our study to identify the likely determinants of outreach. In responsibility so we would firmly uphold that the loans disbursed are a result of both demand and supply-side factors. We would represent both the supply relative as an optimization train by banks and the demand for loans as a result of executive by the borrowers.

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E. Gender Differences

The demand for Loans is higher in those districts where the literacy of females is high and more agricultural labour. The male receivers of loan mostly take the loan to expand their current running business such as poultry farm and retail shop whereas the female take the loan to start new business. However, the increase in income recorded in expanding the existing business as compare to starting the new one. Generally, access to microcredit proved the opportunity for the poor people specially the landless households and the female, to invest this in income-generating activities. It also provides the self-employment opportunity to improve the economic condition of country (Taj, Akmal, Shah, Ahmad, & Saddozai, 2008).

Microcredit is one of the most effective techniques used for reducing poverty between the poor people to become self-employed, especially for women because most of them are not allowed according to social customs for looking for wage employment (Fernando, 2006). One of the social barriers in the development of equitable enterprises and the economy is" gender discrimination." For involvement in the economic activity it is necessary to create gender equality. The barrier for the women in assesses to formal credit are the cultural, social are also associated with the procedural, economic, attitudinal and geographical barriers.
This credit was provided to the community organization members through a very easy and convenient procedure for the women, especially those who did not have access to any other formal credit institution before. However, it is very small. According to the credit beneficiaries, the amount of credit is small, and it should be increased. The credit is provided to the community organization members especially for women, though very convenient and easy procedures because they have no access to formal credit before. The men mostly take loan for expanding existing business whereas females take for starting new business, but the returns are high in case of expanding the business. It is because of difference in the experience of men and women. Overall the access to microcredit is increased by the landless household and females (Taj, Akmal, Shah, Ahmad, & Saddozai, 2008).

F. Creditworthiness

In order to check and determining whether the borrower can repay the loan or not, the lenders should look at the economic prospects and the borrower's record (Chakravarty & Shahriar, 2010). The level of farmer's literacy, domain of land under cultivation and their total income and revenue have a positive effect on microcredit demand (Bakhshoodeh & Karami, 2008). Borrower how have the collateral can easily get the loan because it will reduce the risk of loss of funds of lending institutes. These characteristics are character, education, collateral and the borrower's creditworthiness (Fred, 2009). Clients having negative factors regarding borrowing loans such as irregular income, illiteracy and bad history of credit have to face serious difficulties in borrowing the loan. Usually they need support to start the new business.

In addition to borrower's characteristics, ability and capacity to repay, the requirement of collateral and the condition of the market should be taken into consideration while giving loans to borrowers (Shariff & Nawai, 2010). There are three main elements may affect the individual lending are the nonconventional collateral's demand, a new screening procedure with dynamic incentives and the traditional elements are used in terminating the threat if the individual default which may ensure the 100% interest rate (Chakravarty & Shahriar, 2010). According to Saleh & Ndubisi (2006), he characterizes the repayment problem of loan in four basic factors these are: 1) lender's own related cause, 2) extraneous causes 3) causes related to business operation, and the last is 4) causes related to borrower.

G. Informal Relationship

The informal and close relationship between the microfinance institution and the borrowers helps in the early detection of many problems such as the non-repayment of the loan. Besides it the corporation and coordination of different agencies provide help in providing support necessary for the success of borrower's business (Roslan Abdul Hakim et al., 2007). The procedure which involves the interaction of lenders and borrowers is defined as the relationship. It helps to identify the lending problems easily and also help in improving the efficiency of loan (Chakravarty & Shahriar, 2010).

Borrower-bank relationship have a major impact of on the probability applying for loan and for being approved for microcredit.the potential borrower how have longterm membership with microfinance institution having previous loan records and the non-mandatory savings accounts, they have a more probability of applying for the loan and also approved for the group-based loan. If the borrower associated with multiple lenders increases the probability fro demanding the loan, but reduces the probability of a borrower for being approved for the loan (Chakravarty & Shahriar, 2010).

H. Government Polices

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The barrier in the development of micro-enterprises includes lack of particular procedures of law and administrative, limited access to micro-credit institutions, lack of skill development opportunity and market information is imperfect (Census of Establishment and Enterprise 2005). The challenges which are mostly faced by the small-medium enterprises are: human capital have limited skill, technological penetration and capability level is low, skill development opportunities are less, minimal research and development, high international competition, greater focus on domestic markets, difficulties in access to loan from financial institutions and the high bureaucracy level in government agencies (Saleh & Ndubisi, 2006).

The policies of government such as they aim for generating employment, skill and training and for the development purpose, they become the major tool for helping the poor people to become beneficiaries of microcredit (Delfiner & Perón, 2007). According to Helms and Reille (2004), the government should have to expand the scope of the financial sector by promoting innovation, transparency and competition through the suitable regulatory and legal framework and policies of consumer protection. In actual they argue that competition is only the most effective and single way to reduce the interest rate and the microcredit cost. So, with the decrease in interest rate the borrowing of loans by the poor female increases (Mcloughlin, 2013).

I. Prospective Beneficiaries

Loan demand is high in those areas where the female is higher, and there is more agricultural labour. Microloans' purpose is to finance the activities which help in generating income, and microfinance includes wide range of facilities of services to poor such as savings microcredit and the insurance (Chakravarty & Shahriar, 2010). The male receivers of loan mostly take the loan to expand their current running business such as poultry farm and retail shop whereas the female take the loan to start new business. Nevertheless, the increase in income recorded in expanding the existing business as compare to starting the new one. Generally, access to microcredit proved the opportunity for the poor people specially the landless households and the female, to invest this in income-generating activities. It also provides the self-employment opportunity to improve the economic condition of country (Taj, Akmal, Shah, Ahmad, & Saddozai, 2008).

Large and medium farmers mainly have the availability of rural credit for agriculture, whereas the non-farmer and small farmers did not possess collateral, and due to their low economic condition, they were un-bankable (Waheed, 2009). The consumption of credit for the agricultural inputs is high in rural areas of Pakistan, which is met by the informal sources of loans and tries to keep the households at the better off the household. If there is no credit, the farmer would probably go below the poverty line (Saleh & Ndubisi, 2006). With the credit the income of household increases, and which helps in providing more resources for the investment in assets, savings and expenditure. Study shows that the microcredit has a positive influence on the borrower's well-being, so it helps in coping the difficulties of economy (Hoque, 2008).

J. Availability of Information

The lender can extend the more loan and more favourable interest rate if he has all the information about the borrower's repayment history, total current loans he has and his previous bankruptcies. If the microfinance institution utilizes soft information, it reduces the risk of lending loans. This in return increases the profitability of firm and also reduce the reliance of microfinance institution on government and private sector for subsidies. In other words we can say that this soft relationship helps the microfinance institutes to achieve sustainability (Chakravarty & Shahriar, 2010).

Saleh & Ndubisi (2006) argues that the Grameen Bank makes the close ties with the borrower during the stages of application for the loan, approval of it and its utilization stage. This helps in reducing the asymmetry of information by the production of soft information on the borrower's creditworthiness. Borrower-bank relationship have a major impact of on the probability applying for loan and for being approved for microcredit.the potential borrower how have longterm membership with microfinance institution having previous loan records and the non-mandatory saving accounts, they have a more probability of applying for the loan and also approved for the group-based loan. If the borrower associated with multiple lenders increases the probability fro demanding the loan, but reduces the probability of a borrower for being approved for the loan (Chakravarty & Shahriar, 2010).

3. CONCLUSION

The objective of this study was to explore the factors which affect the demand for microcredit. By using the data from previous studies, it is concluded that numerous factors may influence the demand of microcredit by the various borrowers. These factors include; interest rate, relationship between lenders as well as borrowers, different government policies, gender differences, prospective beneficiaries, creditworthiness of borrower, transaction cost, limited access to credit, economic condition and the availability of information. It is quite supportive in analyzing the obstacles which the borrower and lender face in operating the microcredit.

Therefore, microfinance institutions can take help from this study by considering these factors during distribution of credit.

4. RECOMMENDATION FOR FURTHER STUDY

By reviewing the findings of the study, the following recommendations are proposed to the microfinance institutions working in Pakistan;

- The loan amount is too small; it could be increased to fulfill the requirements of the farmers and other people.
- The interest is too high; that is the main reason the farmers and other people discourage getting loans so, and it could be reduced.
- The government should have to establish specialized microfinance institutes to reduced operating costs.
- Organizations should expand their branches for regular information.
- Specialize banks should be open to reducing the transaction cost.
- Loan borrowing procedure should be easy because, in many research papers, the loan lending procedure is too lengthy that many farmers and other people do not fill it so, it could be easy.
- Factors which decrease the demand for microcredit borrower should be given attention to reducing their negative effects.
- Meeting with loan recipients to help them with using inappropriate loan business, MFI should develop/ provide access to their branches and services in rural areas.
- Microfinance programs also reach to the poorer persons.
- This review paper can be further used for the research study to determine the actual effect or intensity of the effect of this factor, which affects the demand of microcredit in Pakistan. Moreover, to analyze the ways and services to improve MFIs services for the betterment of poor women and gender equality.

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