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MICRO-FINANCE AND SUSTAINABLE DEVELOPMENT: EVIDENCE FROM PAKISTAN

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ABSTRACT

This paper attempts to look into the microfinance sector of Pakistan, its effectiveness and outreach and will further explore if microfinance has been effective enough to ensure sustainable development in the country. The purpose of the study is to examine the extent and efficiency of the microfinance sector, identify the lags in the system and propose feasible recommendations. The study examines microfinance at micro, meso and macro levels. The study highlights the performance of microfinance sector, outreach and efficiency of micro-savers, micro-insurance and assets and liabilities of the sector. Financial infrastructure and challenges to the sector are also indicated. The microfinance market lacks competition and only a few institutes can be tagged as operationally sustainable and have achieved the economies of scale. The study concluded that microfinance in Pakistan is perceived more like a social service rather a financial service. This calls for new techniques and more sustainable models to enable microfinance sector to prevail.

Keywords: microfinance; microfinance in Pakistan; Sustainable Development; Micro insurance; Levels of Microfinance.

INTRODUCTION

Micro finance is small-scale financial services targeting the poor, and has been used as a tool to alleviate poverty since 1970s and has proved to be a powerful instrument for poverty reduction, enabling the poor to increase their income, build assets and build a shield against economic stress. Within the micro finance sector, the concept of sustainability refers to economic sustainability and has two dimensions. The first dimension is operational sustainability; which means that income (from interest rates, fees and other incomes from the clients) cover all operational current costs (administration, credit losses, salaries, capital cost

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et cetera), and the second is financial sustainability which means, the organization has reached a position where incomes not only cover current costs, but also build up their own capital.

There are good reasons to promote Commercialized Sustainable Microfinance, the details of which are discussed later. But not even this approach is without problems. It has been argued that this method has an insignificant or even worsening effect on poverty. One of the problems with sustainable, profitable MFIs is that the social context of the client is not considered to a sufficient degree. Social networks and social capital is usually exclusively seen as a positive resource for the individual as well as for society. It is not taken into consideration that social capital also has a functional side of exclusion. Social capital, or lack of it, affects the performance of microfinance users – for good or for bad. When clients default in repaying, the reasons are almost always to be found in illness or death in the family, or external factors like natural disasters. It is also common that female clients default in repaying, as her husband takes the money to spend on something else. Most of the poor countries have a culture, characterized by strong family ties and a great sense of responsibility towards family members, including the extended family (Liljefrost, 2005).

At least 36 million Pakistanis, one in five, live in poverty. Pakistan is off track on many of the Millennium Development Goals. Half of all adults, and two out of every three women, are illiterate. One in ten children die before their fifth birthday and 14,000 mothers die during pregnancy. This entrenched poverty leads to suffering, lost opportunity and a sense of grievance; all of which undermine Pakistan's long term stability and prosperity (DFID, 2011).

LITERATURE REVIEW

The solution to eliminating poverty has been fiercely debated, and as the world grows, some critiques argue that access of formal credit will facilitate more equal global development options (Morduch, 1998; Anderson, 2002).Microfinance is defined as "the provision of a set of financial products to all those excluded from the formal finance system" (Blondeau, 2006). Microfinance refers to providing financial services to people who are generally excluded from financial services, like microcredit, insurance and money transfers. (Akhter et al, 2009; Khan, 2008). Sasiciharan and Mathews (2008) commented that financial services are intangible products provided by financial markets, designed to meet people's financial needs, link investors and borrowers, and diversify risk. These programs are specially designed for the particular need of the people from lower class of the society (Khan, 2008). The definition goes beyond microcredit. Ahmad (2007) states that microfinance programs are broadly commended as new strategy to alleviate poverty, to bring about economic development and to improve the living conditions of the poor. More than 3000 specialist Micro Finance Institutions (MFIs) work around the globe catering around 92 million people. According to Grameen (2007) Foundation, there are 13 million microfinance consumers around the world with outstanding loans of USD 7 billion with 97 percent repayment rate, and the sector has annual growth rate of 30 percent. In spite of all the stats only 18 percent of the poorest households can access microfinance facilities.

Microfinance is not a new phenomenon. Developed countries and some developing countries, particularly in Asia, have long history of microfinance. In India (recent Bangladesh, Pakistan and India) microfinance predates by two or conceivably three millenniums (Seibel, 2007). In early 1950s developing countries pursued rural finance policy, providing state controlled subsidized credit and directed institutes to cater rural population (Taneja, 2009). Later, microfinance phenomenon emerged in late 1970s to fulfill the short comings of the rural finance approach and to meet the global growth requirements. It is very important to state the fact, as many from microfinance circle believe that the phenomenon was invented in 1970s in Bangladesh. Originally there were three strands of indigenous finance in the history of finance in India. (a) Chit funds, (b) moneylenders, (c) merchant bankers. Chit funds are also called as rotating savings and credit associations (ROSCAs). All of the three have intricate and interlinked history of which very little is known (Seibel, 2007).

Sharma and Zeller (2001) and Ghosh (2006) found that traditionally formal financial institutes treated the poor as 'unbankable'. Sengupta and Aubuchon (2008) found in the early studies that the poor lacked resources required investing the borrowings in most efficient ways; hence they used to spend borrowings on consumption. Rogaly's (1996) findings are in contrast with the micro finance practice in institutions in numerous countries, according to which micro-credit is more advantageous to the people just below the poverty line rather than those who are way below, while the poorest of the people get worse-off the micro-credit (Hulme & Mosley, 1996).In order to benefit the lower ebb of the society the poor must be given access to credit. Micro-credit was very little practiced among formal financial institutes as they were unable to design requirements to avoid physical collateral until Grameen Bank introduced peer-group monitoring to minimize credit risk. Moreover, Yunus (2009) also state the poor have potential to be self-sufficient as their activities are basically meant to ensure survival.

METHODOLOGY

This paper is based on case study approach. Case study is a useful method when 'how' and 'why' is being raised about the current episodes, which are beyond researcher's control (Yin, 1994 as cited in Eisenhardt, 1989). Case studies usually include different data collection techniques like archives, interviews, questionnaires and observations (Eisenhardt, 1989). This approach also provides detailed and in-depth insight into the MFIs and the system which no other technique offers (Rowley, 2002).Therefore we use case study approach to analyze the micro finance sector of Pakistan, as it would be feasible to approach the topic using case study technique. Case study approach is very commonly practiced in micro finance research and also provides convenience of comparison. Initially we will discuss both Pakistan and Bangladesh separately and then will analyze them in context of impact, financial outreach and sustainability.

Data Unavailability

The major hindrance in coming up with the analysis was the lack of proper data and indicators.

Data Inconsistency

The available data was inconsistent and was unavailable over the year, even from the sources like World Bank. The other major problem was that the figures representing the same indicator did not match with different sources. Though, there are some loop holes which could not be fulfilled. However, the researcher has tried his utmost to present the latest figures and cut down the inconsistency as much as possible.

DISCUSSION AND RESULTS

Pakistan has a population of 177 million (September 2011 estimate) of which 67 percent lives in rural areas. It has a gross domestic product (GDP) per capita of $2871 and falls in the category of countries with low human development index (HDI) of 0.453 (2010 estimates). The 2009 statistics of HDI say that 60.3 percent of Pakistan's population lives under US$ 2 a day, compared to 75.6 percent and 81.3 percent in India and Bangladesh respectively and around 22.6 percent lives under $1 a day for Pakistan and 41.6 percent in India and 49.6 percent in Bangladesh. The country faces numerous internal and external perils like disrupt political environment, terrorism, high inflation, low foreign investment and continued costly confrontation with India.

In early 1970s, Government of Pakistan, with the urge to extend financial services to the poor established Agricultural Development Bank (now called ZaraiTaraqiati Bank Limited – ZBTL) in which civil society showed interest and later the private sector also joined. The aim was to deliver financial services to poor and low-income Pakistanis. The effort was mostly funded by international agencies and primarily focused on credit. Later, in early 1980s, Aga Khan Rural Support Program (AKRSP) and Orangi Pilot Project (OPP) were launched, the RSPs rendered general support, a variety of social services as well as financial services. Later in mid 1990s RSPs developed specialized micro finance units – one of those units, Kashf Foundation is one, which is a key MFP in Pakistan.

In spite of positive macroeconomic developments in Pakistan, poverty remains the core issue in the country. The poverty reduction strategy focused on boosting economic growth while maintaining macroeconomic stability. Authorities enhanced targeted interventions, enlarged social safety nets and improved governance. However, there is a big difference between the urban and rural population living below the poverty line, which is 15 percent and 28 percent respectively. According to Asian Development Bank report, the declining trend was observed in 1970s and 1980s but was reversed in 1990s due to poor governance and wide spread corruption. In 2008, 17.2 percent of the population lived below the poverty line, which is the lowest figure in the history of Pakistan.

The micro finance ordinance created by State Bank of Pakistan provided the land mark for new micro finance era in Pakistan and till 2007 six micro finance banks were established. In early 2000s, with the help of funding from the World Bank and the Asian Development Bank, Government of Pakistan boosted up the micro finance development. The Pakistan Poverty Alleviation Fund (PPAF), a whole sale facility and a primary player of refinancing market, made its first loans to MFPs in 2002. Later in 2003, Khushhali Bank was established which is now the largest specialized micro finance retail institution in Pakistan.

TABLE1

The Country at Glance

Indicator Name	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
GDP (current US$, billions)	73.95	72.30	72.30	83.24	97.97	109.60	127.50	143.17	163.89	161.98	174.79
GDP growth (annual %)	4.26	1.98	3.22	4.85	7.37	7.67	6.18	5.68	1.60	3.63	4.36
Unemployment, total (% of total labor force)	7.20		7.80		7.40		6.10	5.10	5.00		
Rural population (millions)	96.54	98.06	99.44	100.73	101.99	103.27	104.46	105.67	106.89	108.12	109.36
Rural population growth (annual %)	1.86	1.57	1.40	1.28	1.24	1.25	1.14	1.15	1.15	1.15	1.14
Rural population (% of total population)	66.80	66.46	66.12	65.78	65.44	65.10	64.68	64.26	63.84	63.42	63.00
Urban population growth (annual %)	3.13	3.10	2.92	2.80	2.75	2.75	2.99	2.98	2.97	2.96	2.94
Urban population	47.98	49.49	50.95	52.40	53.86	55.36	57.04	58.77	60.54	62.36	64.22
Urban population (% of total)	33.20	33.54	33.88	34.22	34.56	34.90	35.32	35.74	36.16	36.58	37.00

Indicator Name	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Population growth (annual %)	2.28	2.08	1.91	1.80	1.76	1.77	1.79	1.80	1.81	1.81	1.80
Inflation, GDP deflator (annual %)	24.8 9	7.89	2.46	4.44	7.75	7.03	10.4 6	7.65	16.2 4	20.0 1	10.33

Levels of Micro Finance Sector in Pakistan

In spite the fact that there is a regulatory framework and huge donor injections of approximately USD 400 million, the micro finance sector lacks a strong and sustainable institute which is able to reach the scale required to cause significant impact. It is mainly because of the reason micro finance is regarded as a social service rather than a financial service as the institutes extending micro finance loans do not separate themselves from social service. The MFIs also lack financial expertise and have staff from social back grounds. This reason also contributes to the fact that MFIs and the consumer fail to achieve sustainability as MFIs focus on providing the instant assistance rather than take bigger picture and provide long term access to financial services, even when huge funds are being injected in the sector. Government of Pakistan and the donors have fatally missed the opportunity to develop a strong financial framework due to their lack of fore sight towards sustainability and commitment towards covering lending costs.

The growth of micro finance sector is relatively modest (2.1 million Micro finance borrowers out of population of 170 million) and the sector relies on unsustainable institutes (out of 30 institutes only2 are sustainable, as per 2011 statistics). It is also concluded by various studies carried out that the most of the MFIs do not adhere to the regulatory framework set by SBP. Micro credit dominates at the consumer level however more work is needed to be done to

boost level of savings and other financial services. An over view of the strengths and challenges to microfinance sector in Pakistan at all three levels, micro, meso and macro are given in Table – 2 and Table – 3, respectively.

TABLE 2

Strengths of Micro, Meso and Macro Levels of Micro Finance

Micro	-	The services are showing steady growth and extending to more geographical areas.
	-	Leverage can be provided for telecommunication and physical infrastructure.
Meso	-	Pakistan Poverty Alleviation Fund helped numerous microfinance providers to flourish.
	-	There is an active network called Micro Finance Network.
Macro	-	Financial and macroeconomic environment is supportive.
	-	Microfinance legal and regulatory framework is supportive.
	-	New policies are developed after extensive consultation by State Bank of Pakistan.

TABLE 3

Challenges for micro, meso and macro levels of micro finance

Micro	-	There is lack of institutional sustainability and weak foundations for growth.
	-	Only a few MFPs have a successful sustainable business model.
	-	MFPs are irresponsive to clients' needs.
Meso	-	Structure of Pakistan Poverty Alleviation Fund hinders sustainability.
	-	The sector lacks top notch training facilities.
	-	There is limited commercial wholesale market.
Macro	-	The stakeholders in GoP do not understand microfinance.
	-	There is limited regulatory framework.
	-	Proper and sufficient information regarding microfinance sector, lacks.

Performance of the Microfinance Sector

Microfinance in Pakistan performed a tremendous growth in the year 2007 in terms of outreach of the network and the extension of product lines. Approximately US$ 337 million (PKR 22.6 billion) was distributed among 1.8 million micro borrowers. Micro savings grew to a total of US$ 60 million (PKR 4 billion) and micro insurance coverage boosted to US$ 147 million (PKR 9.9 million).

The studies indicate a clear trend of urban over rural expansion of micro finance providers, as they tend to primarily focus on urban and semi-urban areas. The RSPs and Khushhali Bank hold the largest number of rural consumers. However, the MFPs understand the significance of rural outreach for future growth. In terms of gender coverage, number of women as micro-borrowers has grown significantly and it almost comprises of 50 percent of total micro finance consumers. MFBs like Tameer Bank and Khushhali Bank explicitly advertise their preference for feminine borrowers. The table below shows the figures number of women borrowers.

TABLE 4

Number of Women Borrowers

MFI	Number of Active Borrowers	Number of Active Women Borrowers	Number of Saving Accounts	Number of Women Savers
Orangi Charitable Trust	23896	4780	0	0
Asasah	23730	17540	23730	23730
National Rural Support Programme Pakistan	565863	232113	0	0
Orix Leasing Pakistan Limited	15177	10714	0	0
Punjab Rural Support Program	74172	40743	0	0
Safwco	18043	6605	0	0
Srsp	10847	5574	0	0
Thardeep Rural Support Program	30751	6003	0	0
Community Support Concern	17432	8075	0	0
Damen	36897	36897	0	0
First Microfinance Bank Limited	168191	61980	139517	35784
Kashf Foundation	319517	319219	98491	98491
Khushhali Bank	312851	0	3477	357
Network Microfinance Bank Limited	2336	537	8090	0
Pak Oman Microfinance Bank Limited	10853	2834	16859	2849
Rozgarmicrofinance Bank Limited	1601	228	4849	729
Sungi Development Foundation	1039	706	0	0
Tameer Microfinance Bank Limited	43791	8471	76050	4362
Kashf Microfinance Bank Limited	18434	3503	0	0

Source: Microfinance Network Pakistan, 2008

Based on the study, it must be significantly understood by the MFIs that in order to maintain growth and performance in future, sustainability, a crucial factor for continuing growth, is inevitable. To date, only two MFIs are considered sustainable i.e. First Microfinance Bank and Kashf Foundation. The time demands that the MFIs should keenly observe performance indicators like profitability, sustainability, asset and liability quality, management and efficiency. The table below shows the top five MFIs in the country with respect to geographical and active borrowers outreach. The given table details regarding top three districts in each province in terms of active borrowers.

TABLE 4

Top Three Districts in Each Province in Terms of Active Borrowers

District	Province	Active Borrowers	Potential Market	Growth
Quetta	Baloshistan	19812	171437	-54
Jafarabad		7044	121911	8
Nasirabad		4129	75783	-445
Mardan	Khyber-Pakhtunkhwa	45542	354988	-62
Peshawar		19856	451548	366
Nowshera		16772	201208	-1342
Lahore	Punjab	434764	872760	-10836
Faisalabad		229176	1096924	-2140
Multan		191494	689339	4452
Karachi	Sindh	251036	1329990	216
Hyderabad		89983	517652	597
Khairpur		65022	401853	5304
Muzafarabad	Azad-Kashmir	18548	0	-544
Kotli		11363	0	-17
Bagh		10481	0	-569
Gilgit	Gilgit-Baltistan	5461	0	545
Skardu		5028	0	-1498
Ghizer		4546	0	-2718
Islamabad	ICT	4209	74750	105

Source: Micro watch, 2011

TABLE 5

Top Five MFIs in Terms of Microcredit Consumer and Geographical Outreach

	MFPs	Microcredit Outreach	Geographical Outreach (No. of Districts)
1	NSRP	446,441	72
2	Kushhali Bank	407,155	49
3	Kashf	288,131	46
4	FMFBL	164,360	30
5	PRSP	135,213	27

Source: Micro watch, 2011

An Insight of the Sector

Micro savings. Micro savings are growing rapidly, both in terms of savers and volume. However, the interviews conducted by CGAP (2007) indicated that, MFBs perceive savings as a service rather a low-cost funding source. This view prevails due to lack of commercialization in the sector, as mentioned above, and extra focus on poverty alleviation and not on profitability and sustainability. Though this frame of mind is now shifting towards commercial microfinance, however more efforts are needed to be made to pull more investment. In order to develop more savings products and other innovative packages, more partnerships like Post Bank and FMFB should be developed. To date, Rural Support Programs have been the most successful projects in reaching out to savers by venturing with commercial banks but talking about volume, MFBs hold 69 percent of the micro savings as deposits. The top five microfinance providers in terms of outreach and growth of savings are given in table below and the top three districts in each province with highest micro savings outreach are:

TABLE 6

Top Five Microfinance Providers in Terms of Outreach and Growth of Savings, and the Top Three Districts in each Province with Highest Micro Savings Outreach

District	Province	Active Savers	Potential Market	Growth
Turbat	Baloshistan	65649	92271	714
Quetta		5103	174437	218
Gwadar		10513	55537	76
Swat	Khyber-Pakhtunkhwa	9823	286555	3335
Mardan		30256	354988	2360
Karak		931	102174	845
D.G. Khan	Punjab	135322	419252	14954
Lahore		87010	872760	13884
Rajanpur		90710	260436	13500
Karachi	Sindh	142053	1329990	31055
Tharparkar		205549	283491	23084
Badin		80567	294781	18505
Poonch	Azad-Kashmir	35659	0	1356
Kotli		34475	0	218
Sudhnati		10630	0	122
Astore	Gilgit-Baltistan	18675	0	16073
Skardu		4643	0	-3933
Gilgit		8648	0	-10018

Source: Micro watch, 2011

TABLE 7

Top five MFIs in terms of micro savings consumer outreach and growth in savings, 2011

	MFPs	Microsavings	MFPs	Increase in Value of Savings
1	NSRP	1832496	TRDP	4412521
2	PRSP	366187	POMFB	739575
3	TMFB	297577	NRDP	0
4	TRDP	292393	SAFWCO	0
5	Kushhali Bank	238495	DAMEN	0

Source: Micro watch, 2008

Micro insurance. The insurance sector in Pakistan represents only 3.1 percent of the financial market and only 4.4 percent companies listed in Karachi Stock Exchange (KSE) is related to insurance sector (Saeed, 2007). Three companies from the insurance sector hold 80 percent share of the insurance market. EFU General Insurance holds the largest share of 33 percent followed by Adamjee Insurance Company with 30 percent and New Jubilee Insurance with 10 percent share. They underwrite health, life and asset insurance policies. In 2000, the Government of Pakistan enforced a new law, Insurance Ordinance 2000, with the aim to promote the insurance market, ensure better governance and compliance. The capital adequacy requirement was raised and policy holder's rights protection was enhanced. The insurance market is supervised by an autonomous body, Securities & Exchange Commission of Pakistan which replaced the department of Ministry of Commerce, Department of Insurance.

In October 2007, three major insurance packages were introduced to cater the low-income borrowers; foreign business travel insurance, crop insurance and micro-insurance. The objective was to promote the micro-insurance in the country, establish a regulatory framework, and provide specialized training to the employees. State Bank of Pakistan believes micro-insurance will increase the market penetration of the insurance sector from 0.67 percent of GDP to more than 3 percent of GDP in the coming years. Micro- insurance is a new concept in Pakistan, however, introduced in 2007, it spread most rapidly. The MFBs and NGO-MFIs contributed to the growth of micro-insurance; however RSPs alone contributed 60 percent towards growth in insured clients in third quarter of 2007. RSPs developed in-house life insurance products while outsourced the health and the refined forms of life insurance through Adamjee Insurance Company and First Microfinance Agency. Till 2007, health insurance constituted the 55 percent of the total micro-insurance market and rest encompassed life insurance clients. Pakistan's first micro-insurance company, First Micro-insurance Agency (FMiA), launched in February 2007, offers tailored life and health insurance products meeting the needs of low-income clients.

First Microfinance Agency was established with the funding from Bill & Melinda Gates Foundation and Aga Khan Agency for Microfinance (AKAM). It works in collaboration with

New Jubilee Life (a subsidiary of Aga Khan Foundation for Economic Development (AKFED) and is one of the major insurance companies of the country. FMiA has widespread distribution channels, partnerships with microfinance banks, MFIs, and local organizations established by the initial Aga Khan Rural Support Program in the 1980s. FMiA offers customized products tailored according to the needs of the local rural residents, medical hotline is one such service, which decreases the costs for both the insurer and the client by accessing medical information through telephone. FMiA is also piloting life and health insurance products with Kashf in Lahore and with Tameer Bank in other regions. In the coming times, agency intends to launch life, health and asset insurance bundle policies.

Key MFIs like Kashf, made it mandatory for their clients to purchase credit-life insurance. This is associated to the loan in case of an accident or death of the clients so the burden of debt does not fall on family. At Kashf, the products are in-house designed to minimize loan risks. These insurance products serve a dual purpose, firstly it reduces the credit risk associated with client's death, dramatically, as it pays of the outstanding loan amount and secondly it also protects the clients to some extent, but not too great.

The National Rural Support Program started offering health insurance on voluntary basis in October, 2005, however, today, NRSP offers a combined insurance package comprising of health, accidental death and disability insurance, in collaboration with Adamjee Insurance Company. The insurance covered up to $ 147, subject to severity of the incident. The table below depicts the largest micro-insurance providers, in terms of outreach and growth, in the country as of first quarter, 2011. The top three districts in each province with highest micro finance outreach are given in tables below, gives the category wise statistics of micro-insurance sector. The top five micro-insurance providers in terms of outreach and growth are also mentioned:

TABLE 8

Top Five Micro-insurance Providers in Terms of Outreach and Growth

District	Province	Active Borrowers	Potential Market	Growth
Lasbela	Baloshistan	1,900	84,637	221
Jafarabad		3,788	121,911	145
Turbat		0	92,271	0
Malakand	Khyber-Pakhtunkhwa	626	106,429	351
Haripur		5,040	103,830	294
Peshawar		6,581	451,548	273

District	Province	Active Borrowers	Potential Market	Growth
Sialkot	Punjab	48,571	501,997	12,404
Narowal		15,488	268,902	8,731
Leyyah		18,170	263,251	3,893
Ghotki	Sindh	28,831	248,442	17,894
Khairpur		29,340	401,853	14,554
Karachi		116,710	1,329,990	12,100
Sudhnati	Azad-Kashmir	469	0	-602
Poonch		3,534	0	-617.6
Muzaffarabad		10,090	0	-1,383.4
Astore	Gilgit-Baltistan	2,414	0	1,264
Skardu		3,003	0	545
Gilgit		1,765	0	-1,498

Source: Micro watch, 2011

	Assets	Deposits	Loans	Asset Share (%)
Public sector banks (state owned)	18,056	8,257	9,951	16.11
Commercial & Foreign Banks (non-state)	89,043	34,062	35,292	79.42
MFBs and MFIs	448	34	121	0.40
Non-bank intermediaries				
Leasing companies	767	n. a.	n. a.	0.68
Finance companies	622	n. a.	n. a.	0.56
Modarbas	261	n. a.	n. a.	0.23
Insurance	2,917	n. a.	n. a.	2.60
Social Security system	n. a.	n. a.	n. a.	n. a.
Total ($ million)	112,114			100

Source: State Bank of Pakistan, 2007, "Statistics of Scheduled Banks in Pakistan 2007," and 2006, "Financial Stability Review 2006;" Securities and Exchange Commission of Pakistan (SCEP), SECP, Islamabad, Pakistan.

TABLE 9

Top five MFIs in terms of micro insurance consumer outreach and consumer growth, 2011

	MFPs	Microinsurance outreach	MFPs	Increase in microinsurance
1	NSRP	1,267,908	PRSP	74,551
2	Kashf	576,262	FMFBL	12,703
3	Kushhali Bank	333,069	Akhuwat	5,904
4	FMFBL	184,502	BRAC	5,501

	MFPs	Microinsurance outreach	MFPs	Increase in microinsurance
5	TRDP	118,471	TRDP	5,084

Source: Micro watch, 2011

Assets and liabilities of microfinance sector

Assets of surplus funds of commercial and micro-finance banks in Pakistan usually consist of cash and investments rather than loans. Banks generate these surplus funds from returns on sums they invest in government securities (treasury notes and bonds), however microfinance banks generate these surpluses from short-term credit lines. The highlighted facts indicate poor asset and liability management. As the loan portfolios are growing, the increasing volume will not ensure sustainable development unless surpluses are not re-channeled prudently into portfolio growth. The data from PMN and NRSP show that only 50 percent of the assets of MFIs and MFPs are invested in loans. It is not only for the MFIs but commercial banks also need to re-think their asset management strategy to increase their returns and performance, but prudentially. However, it is worth noting here that new capital adequacy requirements by local regulators now obligate the financial institutions to have excess liquidity and investment in government securities. The char below gives revenues and assets of key MFIs as of 2008.

TABLE 10

Revenues and Assets of Key MFIs as of 2008

MFI	Financial Revenue from Loan Portfolio	Financial Revenue	Average Total Assets
	All figures in PKR, 000		
Orangi Charitable Trust	30,221	59,678	234,817
ASASAH	94,536	96,508	316,372
NATIONAL RURAL SUPPORT PROGRAMME PAKISTAN	1,272,297	1,401,781	6,163,048
Orix Leasing Pakistan Limited	41,526	41,526	163,792
Punjab Rural Support Program	100,030	183,481	1,982,024
SAFWCO	33,579	33,713	160,235
SRSP	15,630	19,278	89,362
Thardeep Rural Support Program	67,213	73,108	0

MFI	Financial Revenue from Loan Portfolio	Financial Revenue	Average Total Assets
Community Support Concern	26,335	27,940	276,249
DAMEN	88,444	96,874	402,172
First Microfinance Bank Limited	505,932	593,540	3,450,708
KASHF Foundation	1,075,368	1,236,777	4,511,784
Khushhali Bank	541,060	805,859	6,694,511
Network Microfinance Bank Limited	20,238	31,965	197,726
Pak Oman Microfinance Bank Limited	29,958	63,884	477,480
RozgarMicroFinance Bank Limited	12,501	16,742	93,451
SUNGI Development Foundation	526	5,758	29,957
Tameer Microfinance Bank Liminted	213,194	270,723	1,775,466
KASHF Microfinance Bank Limited	33,918	55,525	599,222

Source: Micro watch, 2008

In the year 2006 and 2007, private banks and non-bank financial institutes like Orix leasing raised debt by issuing term-finance certificates (TFCs) in the financial markets. Banks also injected additional equity to meet the terms of new capital adequacy requirements. Huge grants and funding have been provided to micro finance providers in the past few years (through domestic and international donors), most of which was unleveraged. These institutes hold liabilities in the form of small credit lines or subsidized debt from domestic banks, this too like poor asset management, indicates a poor financial position. Such liabilities hinge upon the institute’s ability to diversify the investments to better resources through commercial banks or by investing internationally. The table briefly outlines the liabilities structure of major MFIs in Pakistan as of 2008.

TABLE 11

Liabilities Structure of Major MFIs in Pakistan as of 2008

MFI	MFI	Total Equity	Total Debt	Commercial Liabilities
Orangi Charitable Trust	OCT	165,514	121,596	18,752
ASASAH	ASASAH	-22,317	331,644	65,963
NATIONAL RURAL SUPPORT PROGRAMME PAKISTAN	NRSP	684,548	7,967,881	3,174,569
Orix Leasing Pakistan Limited	ORIX	19,115	181,685	87,426
Punjab Rural Support Program	PRSP	1,076,661	1,166,847	635,024

MFI	MFI	Total Equity	Total Debt	Commercial Liabilities
SAFWCO	SAFWCO	39,407	142,241	0
SRSP	SRSP	3,575	107,203	0
Thardeep Rural Support Program	TRDP	25,885	422,482	0
Community Support Concern	CSC	52,177	257,723	0
DAMEN	DAMEN	56,905	397,446	0
First Microfinance Bank Limited	FMFBL	557,520	3,536,732	100,000
KASHF Foundation	KASHF	994,336	3,965,224	1,566,052
Khushhali Bank	KB	1,871,223	4,814,520	263,709
Network Microfinance Bank Limited	NMFB	88,350	104,769	0
Pak Oman Microfinance Bank Limited	POMFBL	419,910	39,464	0
RozgarMicroFinance Bank Limited	RMFB	49,845	29,565	0
SUNGI Development Foundation	SUNGI	29,302	655	0
Tameer Microfinance Bank Liminted	TMFBL	1,194,635	1,101,074	340,581
KASHF Microfinance Bank Limited	KASHF Bank	711,753	486,691	0

Source: Micro watch, 2008

Financial Infrastructure

Pakistan has mature capital markets but they are relatively narrow and shallow compared to other capital infrastructures in the region. As of Karachi Stock Exchange (KSE), September 30, 2009 figures, 650 companies were listed in the stock exchange with market capitalization of US$ 32.68 billion (PKR 2.715 trillion) and listed capital of US$ 9.62 billion (PKR 800 billion). However, the stock exchange is has negative performance since 2007 due loss in investors' confidence (Bokhar, 2008). Given the country's recent profile, foreign investors are reluctant and wary to invest in such unstable hostile environments.

Debt financing is consented inevitable for the growth of microfinance in the coming years. Therefore, the MFIs must overcome the prevailing obstacles in order to grow forward. Empirical estimates indicate that the top five microfinance organizations need approximately US$ 515 – US$ 565 (PKR 44-48 billion based on September, 2011 exchange rate) by the year 2012 to meet the growth of number of borrowers and loan balances. As Pakistan Poverty Alleviation Fund (PPAF) is the sole whole seller of microfinance funds, serving only non-regulated MFIs, huge funds are required to meet the growing demand of the borrowings.

It is harder for MFBs to obtain secured funding as they cannot provide guarantee against their assets or loan portfolios, therefore left with only expensive and unsecure financing alternatives. Moreover, the banks are required to charge low spread in microfinance deals, make financing sources even narrower.

In short, microfinance institutes in Pakistan have only four available instruments which facilitate whole sale market transactions. Instruments are term finance certificates (TFCs), foreign currency loans, bank debt and secured lines of credit.

- Term Finance Certificates (TFCs) are the most flexible form of financing, and is available to all MFPs.
- There is a price cap on foreign currency loans (1 - 1.5 percent approx.), which State Bank of Pakistan waives off sometimes. However, foreign exchange terms and policies make it hard for the micro finance institutes to access the secure foreign loans.
- LIBOR plus one to four percent is used to price the bank financing for the period of short maturity (2 – 3 years).
- The secured credit lines are only available to NGO-MFIs and non-shareholding companies.

TFCs are the supplest option due to their structure. They are the debt instruments issued to generate funds in form of redeemable capital. Regulated by the Stock Exchange Commission of Pakistan, TFCs can be issued at either flexible or fixed interest rates. In the past, Tameer Bank and Kashf Foundation have floated TFCs to raise funds. However, such TFCs are traded in the unlisted market.

Challenges in Microfinance

The principal challenges faced by all MFPs in Pakistan are inadequate human resources, reaching funding and ensuring constant funding. To date, microfinance is perceived as a social movement against poverty, which has proved to be the primary factor of hinging growth in the sector and the major cause of the afore mentioned challenges. Since, microfinance is perceived as a socially driven cause, university graduates and professionals are reluctant to choose it as a career line, mainly because of the un-sustainability of the sector which hinders career development and growth opportunities and salary structures are very low. The factors along with long working hours and physical fatigue result in high employees turn over and low management capacity throughout the microfinance sector.

Microfinance providers face a deficiency of funds and funding sources, and the available sources are not constant. Only limited amount of medium-to-long run funding is available that too is subject to State Bank of Pakistan's regulations. Commercial banks lend to microfinance providers reluctantly as MFPs are not profitable, lack adequate expertise to manage finances and do not hold long track records. Finally, the MFPs failed to generate ample funds to build their financial statements, invest in return-full projects or service debt. The basic reason was the loan pricing. As loans were regarded as more of a social product, providers did not price them according to their costs rather subsidize the loans for the clients.

Since 2000, the Government of Pakistan and State Bank of Pakistan (SBP) have taken some significant steps for the sector's prosperity. However, the central bank has yet lot more to do when it comes to the role of SBP. SBP should not only regulate and supervise but finance the sector, which it did, when SBP started "SBP Funding Window". The SBP's prudential regulations (Prudential Regulations for Microfinance Banks) must be revised and pruned periodically, keeping in pace with the market dynamics. One most important amendment needed to be made is to allow commercial banks lend the MFBs, as it prohibits the latter from issuing securities. SBP's policy regarding the foreign funding is reluctant. Moreover, other requirements like loan exposure limits per borrower and rigorous requirements regarding equity should be reviewed to enable MFBs reach scale and achieve sustainability.

New Trends in the Sector

First Micro Finance Bank Ltd. (FMFB) and Pakistan Postal Service syndicated in late 2007. FMFB, an MFI which is sponsored by Aga Khan Development Network joined hands with Pakistan Post in Oct, 2007 to render microfinance services across Pakistan through post offices. FMFB provided funds to forward credit. As per the agreement, the postal service supply office space and validates clients, in order to appraise, disburse and collect the loan amount. The plan was to expand the partnership to 42 strategic locations and disbursing