

Microfinance poised to play a vital role in achieving developmental objectives of the Government

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Executive Summary

The paper aims to explore the extents where the Microfinance sector can play a catalytic role in accomplishing the social & economic milestones set by the current government such as deepening financial inclusion; contribution to inclusive economic growth; improvement in socio economic indicators (reflected in SDG 2030) leading to poverty reduction.

Over the years, Microfinance has been the torch-bearer to provide a range of financial services to the low-income households such as credit, savings, insurance, and payments. Microfinance has been termed as one of the important tools to increase financial inclusion, leading to socio economic improvements and inclusive and equitable growth. Since most of the clientele of Microfinance largely falls in marginalized segments (including rural, semi-urban, women, disabled, transgenders and low-income economically productive population among others) where penetration of formal financial service providers is lacking, therefore it is one of the most important tools to alleviate poverty through expanding financial outreach.

As poverty alleviation is a multi-dimensional phenomenon, therefore policymakers require a diverse array of approaches and complimentary avenues to cater various aspects of poverty. Given that all the 'poor' are not the same, the tools will have to be different to target respective segments. For the poorest of the poor, approaches like the targeted cash transfer programs such as BISP may be needed with microfinance catering to the economically active poor and low-income households.

Segmentation of the poverty levels is one of the essential ways to devise targeted ways to attend to the needs of poor households to lift them out of poverty. One of the best approaches adopted has been the 'Graduation Model Approach' which segregates clients into different categories based on their poverty score and urge institutions to offer them befitting financial services. This also allows poor household to gradually elevate to another level once they are ready.

The role of financial inclusion to the objectives of SDGs has been critical as it is the means to end the most pressing development challenges such as: poverty alleviation; zero hunger; fostering quality education; gender equality; and shared economic growth.

Increase in Microfinance growth can lead to complementing most of the key government agendas which are as follows:

1. Funding for Microfinance can be used to increase access to finance in the low-penetration districts through its community-based approach
2. Since Life & Health insurance are important components of Microfinance services, therefore it is imperative to offer these services in conjunction with Government-led programs such as Sehat Insaf Cards.
3. Microfinance sector employs around 36000 people directly and helps in job creation especially for micro and small entrepreneurs. According to a recent study conducted by PMN in collaboration with Karandaaz and PMIC, every microfinance loan creates on average, 0.11 additional jobs every year ¹.
4. The government is focused on building 5 million houses for the low-income communities, therefore the outreach and in-depth assessment methodologies and distribution channels can be utilized for funding this housing schemes. Although the housing portfolio of the sector currently stands at 1% but it will get a boost if the government involves them through funding, this number can reach much higher.
5. Lastly, as per the NFIS strategy the government and SBP wants to bring 60% population in the formal financial fold, especially with niche segments like agriculture for marginalized & small farmers and SME finance for micro and very small enterprises; the Microfinance sector can greatly complement these efforts. As the Pakistan Microfinance Network is setting up a 'Digital Services Platform' which will help enable the Microfinance providers to connect with the larger financial services industry that will lead to ubiquity of financial access points, bringing convenience to the end clients and reduce the 'Turn Around Time' of loans as well as lower the cost of Microfinance Operations. The reduction in cost will result in catering to millions of new customers who are currently unserved in untapped markets.

In the last section of the paper, the sector has put forward some recommendations to achieve 75% of the total estimated outreach for Microfinance by 2023 (30 million active borrowers according to a new market estimation study conducted by Gallup and PMN). We expect that the government will recognize the efforts of Microfinance and make it the cornerstone of its financial inclusion and social impact strategies.

SECTION 1

1. Introduction

The purpose of this paper is to examine areas where the Microfinance sector can play a catalytic role in accomplishing the ambitious but achievable social & economic milestones set by the government such as deepening financial inclusion; contribution to inclusive economic growth; improvement in socio economic indicators (reflected in SDG 2030) leading to poverty reduction.

The paper is divided into three sections. The first section illustrates the current outreach of Microfinance and its estimated potential market size along with its central role in financial inclusion and social change. In the second section we will look at microfinance and financial inclusion as a key enabler to achieve United Nations' Sustainable Development Goals (SDGs) 2030 followed by comparison between the Government objectives (taken from government's manifesto and Honourable PM's address to the nation) and the recent policy objectives and programs initiated by the government. In section three, the paper has recommendations from the Microfinance industry that if agreed will provide continuous policy support to the industry in achieving its stated objectives.

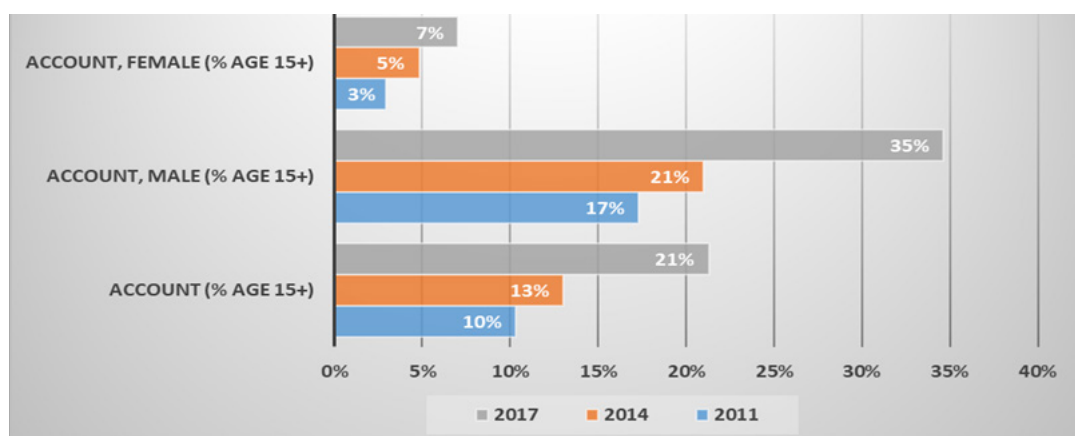
2. Microfinance Sector in Pakistan

Microfinance was pioneered in Pakistan in the 1960s through Comilla Pilot Project in former East Pakistan (present-day Bangladesh). This was followed by the launch of the Orangi Pilot Project's Orangi Charitable Trust (OCT) in Karachi and the Agha Khan Rural Support Program (AKRSP) in the Northern Areas of Pakistan.

The late 1990s was a watershed period for the sector as it received major impetus due to recognition of the important role of microfinance in the growing economy. Several microfinance initiatives were launched such as establishment of Kashf Foundation (KF), Urban Poverty Alleviation Program (UPAP) by National Rural Support Program (NRSP) and the launch of the then state-owned microfinance bank (MFB) Khushhali Bank Ltd. (KBL), with assistance of the Asian Development Bank (ADB). Microfinance received a further boost with the establishment of Pakistan Poverty Alleviation Fund (PPAF) in 1999 as an apex funding body for the sector. Promulgation of the Microfinance Ordinance 2001 further strengthening the micro finance eco system by providing a framework for creating privately owned specialized Microfinance Banks (MFBs) under the supervision of the State Bank of Pakistan (SBP).

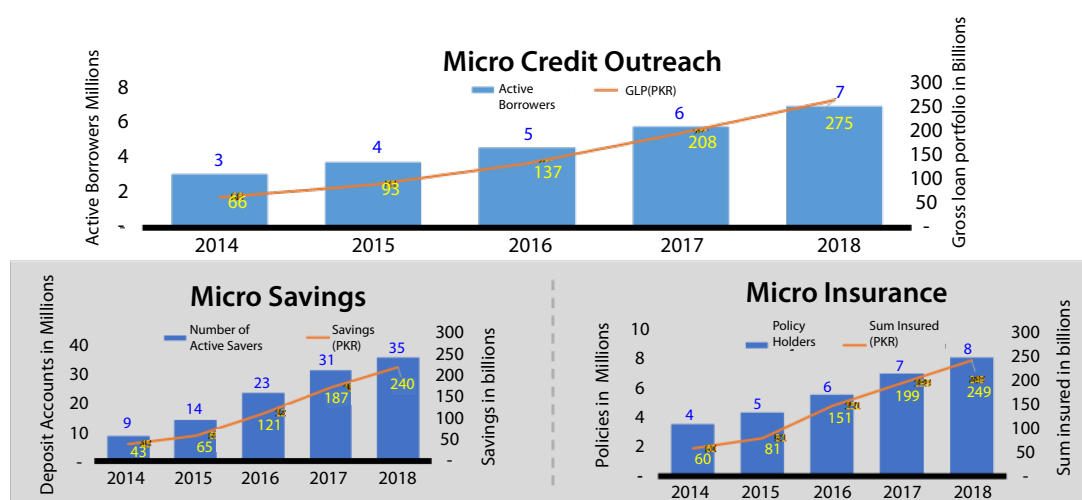
Microfinance has been seen by many through the lens of provision of micro-credit only, however it is the provision of a full range of financial services including credit, savings, insurance, and payments to the low-income households. Microfinance has been termed as one of the important tools to increase financial inclusion, leading to socio economic improvements and inclusive and equitable growth, as the providers work largely with the marginalized segments (including rural, semi-urban, women, disabled, transgenders and low-income economically productive population among others) where penetration of formal financial service providers is almost non-existent.

Exhibit A: Financial Inclusion trends



The microfinance sector has been growing at a double-digit rate for the last five years. At present, 6.9 million borrowers and a GLP of PKR 274 billion (see Exhibit B below). The number of depositors has increased to 35 million while value of deposits has risen to 239 billion. However, the current penetration level stands at 31.5 percent. Number of insurance policy holders stand at 8 million and the value of Insurance is 248 billion. Currently, MFPs are operational in over 100 districts in the country.

Exhibit B: Microfinance Outreach Trends²



The Microfinance industry is currently going through a high growth period with compounded annual growth rates in the last three years was around 40%. This has not only led to microfinance playing a leading role in the financial inclusion agenda, with a suite of financial services as indicated above, but also in achieving targets for agriculture lending and mainstreaming the marginalized segments (including women access to finance). It is because of this demonstration and the fact that microfinance has an inherent strength of working at the grassroots level that the State Bank of Pakistan (SBP) has felt the need to revise the lending limits of Microfinance Banks (MFBs) in the recently launched SME policy, to cater to the needs of Micro and Small Enterprises (MSEs). This is indicative of the important role the microfinance sector can play in going up-market and start lending to the MSEs where there is a huge gap in financing, thus leading to creating jobs in the economy. The industry players are moving towards innovative low-cost distribution models by using available technologies such as the use of mobile wallets (m-wallets).

While the introduction of digital credit (loans extended through mobile phones based on alternative credit scoring models) by some Telco owned MFBs and new Non-Bank Microfinance companies will pave the way to reach the unbanked in a convenient way to meet their financing needs. This will not only help in mainstreaming the marginalized segments but also in formalizing the informal sector. Hence adding to the country's GDP and help in documenting the economy.

The Pakistan's regulatory and business environment for microfinance and financial inclusion continues to remain among the best in the world due to the active role of the regulators – SBP and SECP, as per the Economist Intelligence Unit (EIU) multiple reports on Financial inclusion. A recent major development has been around bringing the unregulated Non-banking Financial sector (MFIs) under the regulatory ambit of SECP where the sector stakeholders including Pakistan Microfinance Network (PMN) and Pakistan Microfinance Investment Company (PMIC) have played a vital role.

Microfinance sector has also been to some extent critiqued for its interest rates as they are higher than the commercial lending institutions. The reasons for the relatively higher interest rates are manifold such as the labour and cost-intensive model of microfinance operations coupled with small ticket size (average loan of Rs.45k) and finally provision of unsecured loans.

Typically, as the industry reaches scale (the pivotal point is 15-20 M clients in Pakistan's case) and reaches maturity phase (usually an industry is considered to have matured when it reaches its penetration rate of 75%), then the operations costs start downwards which then leads to decline in lending rates. As a push factor, the microfinance providers are working towards brining operational efficiencies through leveraging technologies and digital model in which the SBP has played a major role. Also, the industry adheres to the international standards for transparency in pricing and client protection and reports to international data exchanges to ensure transparency.

The penetration rate for Microfinance is currently at 31.5%, whereas the potential estimated market size for microcredit is 20 Million ³ according to an earlier study conducted by Pakistan Microfinance Network. In collaboration with Gallup, PMN has finalized an estimation study of microfinance potential market segmented for credit, deposit, insurance and payment products. This was carried out using Access to Finance Study commissioned by SBP and shows a very high upside potential that microfinance can help in achieve going forward. The results have been deduced from the Access to Finance Survey (a2F) 2015 conducted by the State Bank of Pakistan in collaboration with Gallup. The new Microfinance market estimation exercise is also being carried by Gallup Pakistan in collaboration with PMN, the figures are shown in table below:

³ Micronote: Estimating potential market size for microcredit in Pakistan, December 2015
<https://bit.ly/2PhOjTW>

Summary Estimation of Microfinance Potential Estimation in Pakistan (based on A2F findings)	
CATEGORY	POPULATION ESTIMATES
Micro-deposit	60.9 million
Micro-insurance (Health)	96.8 million
Micro-insurance (Life)	96.8 million
Micro-payments	82.1 million
Micro-credit	40.9 million
Micro-enterprise credit	5.8 million

Globally, research has shown that Microfinance may not be silver bullet to reduced poverty with various studies support this claim. Since poverty is multi-dimensional, economic policies do not consider the multiple dimensions of poverty while designing policies which leads to neglecting the entrepreneurial potential of the country. Similarly, without segmenting the poor strata, policy makers come up with a single tool or consider only one tool as a panacea for social change and poverty reduction. Keeping this in view, there is new paradigm shift in the impact of microfinance as an important instrument for financial inclusion.

Box 1: Is Microfinance a tool for Poverty Alleviation or Financial Inclusion?

Some say that microfinance is going through an identity crisis. For a long time, it was the silver bullet to alleviate poverty globally - and pay for itself along the way. However, the debate about what microfinance can do and what it cannot has evolved around the globe and there is a better understanding of how it helps the poor.

For one, it has become clear that sustainable microfinance, or to be more specific – microcredit, is not meant for the poorest of the poor. It is more relevant for the economically active poor and the low income that live close to the poverty line (above and below). Treating microfinance as a social safety net is inappropriate and creates expectations that it cannot deliver. For another, microfinance does help alleviate poverty, but the transmission mechanisms are quite different from those that were initially hypothesized. It plays a critical role in creating access to finance, which is considered a key bottleneck when it comes to raising standards of living at the base of the pyramid. Microfinance is a key component of national strategies for expanding financial inclusion. By bringing more people into the financial sector, providing them products to smooth consumption, manage risks, and increase incomes, microfinance contributes to economic development at the BOP. Simply put, poverty alleviation is the end objective and financial inclusion is one of the means to achieve it. Thus, microfinance can by no means be the only approach, or even perhaps the main mechanism to fight poverty.

The challenge of poverty is huge in Pakistan: estimates of those living below the poverty line range from 23.9 percent to 37.5 percent of the population. The policymakers require a rich and diverse repertoire of tools and strategies if a significant reduction in poverty is to be made in the medium term. Given that all the 'poor' are not the same, the tools will have to be different to target respective segments. For the poorest of the poor, approaches like the targeted cash transfer programs such as BISP may be needed with microfinance catering to the economically active poor and low-income households.

Source: Pakistan Microfinance Review (PMR) 2012

Segmentation helps in providing targeted subsidies along with tools for intervention. Please see the Graduation Model, in **Exhibit C**, developed by the Pakistan Poverty Alleviation Fund (PPAF) based on the PPI (Poverty Probability Index referred to Poverty Scorecard). For information on PPI, please refer to **Annexure A**.

Exhibit C: PPAF Graduation Model for Financial Services delivery

			Up to 100
		<40	Regular Microfinance & Microfinance Plus
	<23	Interest Free Loan Schemes & Concessional Loans	Transitory poor , transitory vulnerable Pro poor value chains Micro insurance products Creating entrepreneurs Access to savings and banking services Business expansion
0-16.17	Asset Transfers & Livelihood Interventions	Organization into Common Interest Groups (CIGs) Asset(s) strengthening Employment centres Development of Linkages	
Social Protection Safety Nets	Livelihood interventions (asset transfers + skill trainings) Provision of skill/vocational training Employment centres production centres Development of enabling ecosystem (small infrastructure, energy, education & health)		
Cash transfer GOP, Social Protection Programme	Conditional Cash Transfer Programs	Interest Free Programs	Sustainable Microfinance Programs

Source: This information has been taken from the PPAF document and adapted to the industry wide scenario

Based on the model, the policy makers have come up with targeted interventions and graduation schemes, for example:

i) **Benazir Income Support Programme:** Under this programme, subsidy is provided in the form of cash and conditional cash programs, leading to building of either assets or technical skills. This program is targeted towards beneficiaries whose Poverty score is up to 16.17 for which government is providing cash support.

ii) **Interest Free loan programs (Qarz-e-Hasna):** Under this programme, interest free loans are provided in the form of capital to help individuals in becoming entrepreneurs. This program is targeted towards clients whose Poverty score is from 16.17 to 40. In this programme, the government subsidises interest rates for clients.

iii) **Sustainable microfinance:** With a suite of financial services (including credit, deposit, insurance, payments and remittance) providing sustainable microfinance helps in creating micro enterprises that provides jobs and helps individuals in becoming future entrepreneurs of small enterprises (poverty score above 35) – Government support is required in terms of catering to the various market segments within the sector, market development and an enabling policy framework.

SECTION II

3. The role of Microfinance/Financial Inclusion in achieving governments objectives

3.1 Sustainable Development Goals (SDGs 2030)



Financial inclusion means that formal financial services—such as loans, deposit and savings accounts, payment services, and insurance—are readily available to clients and businesses and that they are actively and effectively using these services to meet their specific needs (CGAP definition, Achieving the Sustainable Development Goals - The Role of Financial Inclusion).

In May 2015, the State Bank of Pakistan rolled out the 'National Financial Inclusion Strategy', a comprehensive roadmap with the headline target to providing formal financial access to 50% of the adult population in Pakistan by 2020 (currently 21% of the adult population have access to formal financial services according to the Global Findex 2017). A set of cross-cutting key enablers have been laid out in the strategy to increase financial inclusion and support the targeted actions. A key part of the strategy is the coordination structure among various stakeholders including public and private sector entities, donors, policy makers, as well as regulators to make concerted efforts towards achieving the targets. To support this initiative PMN as an industry association developed a "microfinance growth strategy 2020" with a focus to i) diversify its menu of product and services (not just micro credit but deposit, insurance and impact-based credit products), ii) achieve scale (credit 10M active borrowers, deposit 50M active accounts-especially m-wallet and 13M insurance clients) and iii) adopt technology (linking microfinance with digital platforms, using both credit and non-credit based algorithms for acquisition and digital credit).

Similarly, in September 2015, The United Nations General Assembly adopted the Sustainable Development Goals (SDGs) – a set of 17 goals to be achieved till 2030. Though financial inclusion is not a direct target of the SDGs however it is widely considered to be a key enabler for **11 out of the 17 goals** to be accomplished. For example, the **Box II** contains the excerpt from a working paper published by CGAP on the role of financial inclusion to help achieve SDGs.

Box II: Role of Financial Inclusion in Achieving SDGs 2030

1. Eliminating extreme poverty (SDG 1)

This goal explicitly mentions the importance of access to financial services. When people are included in the financial system, they are better able to climb out of poverty by investing in business or education. Financial inclusion also prevents people from falling into poverty by softening the blow of unexpected expenses, hence increasing the role of insurance services. When hit with the death of a breadwinner, a savings account can be all that stands between a family's impoverishment and stability. Digital payment services also allow people to collect money from far-flung friends and relatives when faced with economic pressure. Increasing account ownership among the 79% unbanked in Pakistan—most of whom are poor women—would help the SDGs promote gender equality. Savings can have direct and indirect impacts on poverty. Savings allow families to increase their capacity to absorb financial shocks, smooth consumption, accumulate assets, and invest in human capital such as health and education. Such investments help people climb out of poverty and ultimately can lead to higher growth. Digital financial payments products allow people to collect money from far-flung relatives and friends during times of crisis, reducing the likelihood that they will fall into poverty to begin with.

2. Reducing hunger and promoting food security (SDG 2)

Farmers who have access to financial services often produce more bountiful harvests, leading to progress on the second SDG: reducing hunger and promoting food security. A lack of access to credit and insurance prevents farmers from making investments that could increase crop yields and strengthen food security (FAO 2015). Financial services can help farmers increase their production to meet the food needs of growing populations—in other words, greater food security. Research suggests that access to agricultural insurance can embolden farmers to make more and riskier investments, which can lead to increased earnings. In addition, savings products allow farmers to manage expenses during the down season. Rural households often must tap into savings to buy food, as they do not produce enough for their own consumption. Another financial product that supports food security is appropriate credit. Risk management and digital payments tools create opportunities for smallholder farmers to more tightly connect to agricultural value chains. Finally, digital financial services support agricultural extension services by improving information dissemination.

3. Achieving good health and well-being (SDG 3)

Financial inclusion improves health by giving people the ability to manage medical expenses and rebound from a health crisis. Health shocks not only drain their resources for paying for medical treatment, but they also result in income loss because of the patient's inability to work or the depletion of their assets to confront health costs. Financial services like medical insurance can provide a formal channel for mitigating the risks of health emergencies. Women especially have a high demand for health insurance products to address the common health concerns associated with pregnancy and child birth, including greater susceptibility to infection. Furthermore, new products designed to leverage digital payments technology might help reduce medical expenses and increase transparency of health subsidies. Savings also is an important tool for managing medical expenses, whether planned or unplanned. Access to formal, interest-bearing accounts can further increase the value of these investments.

Published by CGAP on the role of financial inclusion to help achieve SDGs.

4. Fostering quality education (SDG 4)

Achieving quality education depends on people having the ability to invest in learning opportunities. Since economic growth is closely linked with human capital, academic underperformance slows development. Savings products help families plan for and manage education expenses. Nudges that encourage good savings habits also have been effective. When people send money to friends or relatives, digital payments products can provide influence over how the money is spent.

5. Promoting gender equality (SDG 5)

Financial services help women assert their economic power, which is key to promoting gender equality. Women also are less likely to report having borrowed from family and friends in the past years. In the absence of easy access to formal and informal loans, savings accounts can provide women with a safe and formal platform to build a credit history and store their earnings for future investments. The financial footprint created by digital payments also allows for alternative methods of assessing the creditworthiness of women who do not have traditional credit assets or a financial transaction history. Digital financial services also support women-owned businesses by reducing the risks of theft and lowering administrative and disbursement costs.

6. Access to Infrastructure: Water and Sanitation (SDG 6) and Energy (SDG 7)

Two of the SDGs focus on access to essential infrastructure and resources—water and sanitation, and energy. Both goals are likely to have significant impact on people's quality of life. There are many reasons to believe that innovations in digital financial services are likely to accelerate access to these resources, although the literature does not yet document this impact.

7. Promoting shared economic growth (SDG 8)

When poor people are excluded from the formal financial system, the foundations of shared economic growth are weak. Income inequality between rich and poor in advanced economies remains at its highest level in decades. And while the picture is more mixed in developing economies, sizable gaps persist in access to education, health care, and finance. Access to financial institutions and products allows people to gain higher returns on capital. This leads to increases in their income and consequently affects economic growth.

8. Promoting innovation and sustainable industrialization (SDG 9)

Promoting innovation and sustainable industrialization requires easy access to credit and other financial services that facilitate investment. According to the World Bank Enterprise Surveys, many of these firms cite limited access to financial services as one of their main constraints to growth. Access to financial services, particularly credit, is likely to allow more businesses to be started and allow existing firms to expand their services by enabling greater investment in inventory, labour, and other means of production. An increase in the number of MSMEs allows economies to create job opportunities for business owners and their employees.

9. Toward equitable and peaceful societies (SDG 10 and SDG 16)

People with access to financial services are better positioned to succeed economically and build a decent life, ultimately making it easier to reduce inequality (SDG 10) and promote peace (SDG 16). Wide swaths of the developing world are wracked by instability. Furthermore, inequality is rampant; in developed and developing countries alike, the poorest half of the population often controls less than 10 percent of the overall wealth. The danger of neglecting inequality is that people, especially young people, excluded from the mainstream end up feeling disenfranchised, which can lead to disengagement and conflict. In their comparative study of western Europe and Latin America, Acemoglu and Robinson (2001) argued that inequality breeds political instability by fostering social unrest in nondemocratic countries and encouraging the rich to contest power in democratic countries.

Given the increasingly clear link between financial inclusion and development, governments should continue to push the boundaries for access to and use of financial services. Prioritization of financial services does not take away resources from other key objectives set in the SDGs. The CGAP study build a strong case that financial inclusion complements other developmental efforts to create the means that ultimately will achieve the SDGs. As a matter of fact, by going cashless and using digital payments, governments can reduce costs and leakages, while increasing financial inclusion among individuals and businesses.

3.2 Role of Microfinance sector in complementing the Government Agenda

There are certain key elements in the Government agenda in which the Microfinance can play an incremental role in achieving its objectives. **Figure I** shows the summary of Microfinance recommendations and interventions, while **Table I** elaborates the specifics against each Government agenda item.

Figure I

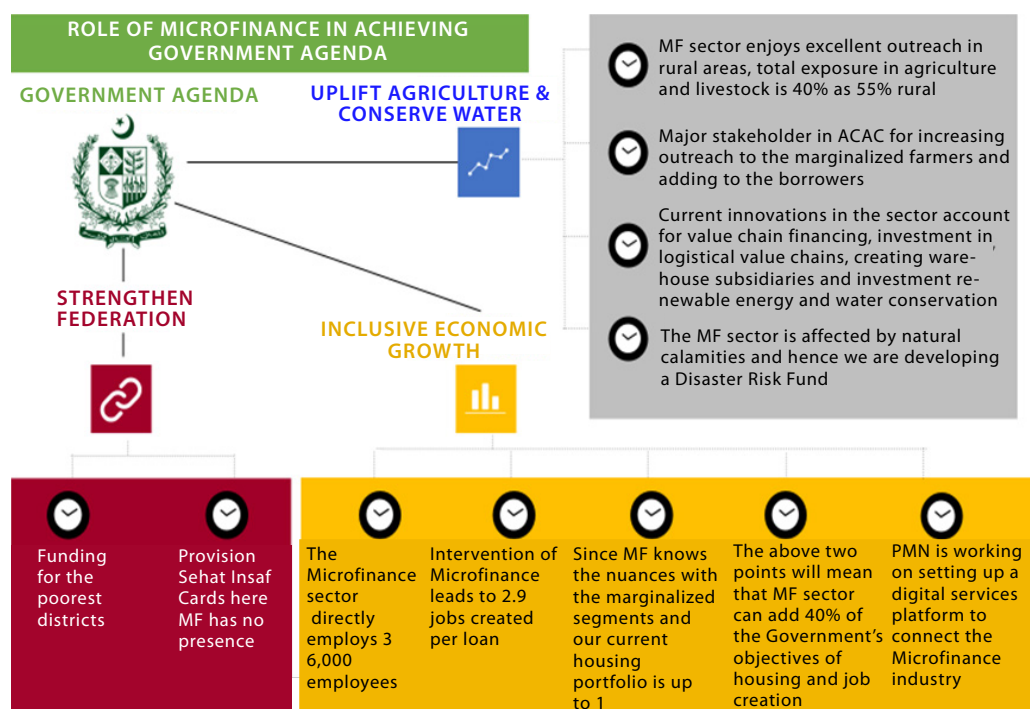


Table II

Government Agenda	Role of Microfinance sector
<p>1. Strengthen Federation</p> <p>1a) Alleviate poverty across Pakistan's poorest districts: Poverty is rampant in Pakistan with 29.5% of the population or close to 60 million people living below poverty line. There is a strong correlation between the incidence of high poverty and poor public delivery. Pakistan's Human Development Index (HDI) of 0.55 is currently the lowest in South Asia. There will be an increase funding for the poorest districts through existing poverty alleviation programmes. The government also plans to launch a special drive in the poorest districts to improve access to sanitation and clean drinking water.</p> <p>1b) Another focus area is the provision of Sehat Insaf cards and augment the existing BISP programme in these districts.</p>	<p>1a) Funding for the poorest districts: We strongly believe that this is excellent idea of the government to direct access of subsidy to the poorest geographical areas in Pakistan; sustainable microfinance is not the only tool of financial inclusion that addresses the issue of poverty. As already shown in Exhibit A (graduation model), BISP program of cash transfer and conditional cash transfer is an ideal tool for financial inclusion in these areas. Once BISP can build their assets or financial capacity of these clients having crossed score 16 on the PPI, they can be graduated to Qarz-e-Hassana (interest-free loan schemes). In this scheme government create linkage between financial sector and microfinance providers and cover operational costs and probable loan losses.</p> <p>1b) Sehat Insaf Cards: Another focus area is the provision of Sehat Insaf cards and augment the existing BISP programme in these districts. Government should direct its subsidy of Sehat Insaf cards to the areas where sustainable Microfinance services including micro-insurance are not available and for poverty scorecard at the BISP threshold. Anyone following above these two should be linked to the microfinance sustainable model</p>
<p>2. Inclusive Economic Growth</p> <p>2a) Create 10 Million jobs and strengthen the labour market: Government will strengthen the labour market and create 10 million jobs over 5 years in key sectors: SME, housing, ICT, health, education, green economy and tourism. These 10 million jobs will be created through cross-cutting initiatives led by the private sector</p> <p>o Ensure that each economic development initiative explicitly specifies and contributes towards the "10 Million jobs" agenda.</p>	<p>2a) The Microfinance sector directly employs 36,000 employees. Given that we want to achieve 75% of penetration by 2023 i.e. 15 million active borrowers (close to 30 million according to the new Microfinance Market estimation study). With the growth objectives, the number of employees can go up additional 64,000.</p> <p>2a) Intervention of Microfinance leads to 0.11 additional jobs per loan every year ⁴. This means that approximately 3.3 million additional jobs will be created by the industry once we reach 30 million active</p>

Government Agenda	Role of Microfinance sector
<p>o Ensure that economic development initiatives will offer Employment Guarantee Schemes for the Bottom-of-the-Pyramid with focus on women and rural areas.</p> <p>2b) Implement policy framework to build five million houses: Government will play the role of an enabler and facilitator, but not developer, to build 5 million low cost housing units. We will ensure the development of 1.5 to 2 million urban and 3 to 3.5 million rural housing units.</p>	<p>borrowers and majority of these jobs will be created at the base of the pyramid (low-income segments)</p> <p>2b) Since microfinance knows the nuances with the marginalized segments and our current housing portfolio is up to 1% hence, we are ideally positioned to provide access to low cost housing. Microfinance sector aims to reach 10 million active borrowers and 50 million depositors by 2020 coinciding with the targets laid out by NFIS. Even if we allocate 25% of our incremental portfolio i.e. 8.5 million, then 2 million housing clients will be tapped through financing by the Microfinance sector.</p> <p>2b) The above two points will mean that microfinance sector can add 40% of the Government's objectives of housing and job creation (specially for the marginalized – low-income, women, PwD)</p>
<p>2c) Enhance Access to Finance for citizens and industry: The government's plan to improve and implement State Bank of Pakistan's National Financial Inclusion Strategy, drastically increase access to finance, increase deposit base of banks and establish an infrastructure lending bank for large projects. Key objectives set out by NFIS include that 50 percent of adult population needs to have formal accounts, 25 percent of adult women needs to have accounts with formal financial institutions, increase percentage of adult population to be living within 5 km of access points and 15 percent of total private sector credit to be lent to SMEs. There will also be a focus on championing digital financial services efforts to encourage shift towards a cashless economy. Development and delivery of innovative financial instruments and services will be incentivised.</p>	<p>2c) PMN is working on setting up a digital services platform to connect the Microfinance industry with larger financial services industry to leverage their financial service distribution channels for the use case of financial services. This will not only provide easy to access financial solutions and instruments for the Microfinance clients but also for the unbanked population. The platform will also connect with payments schemes, ATM networks and payment gateways in the future.</p>

⁴ <https://www.opportunityfund.org/assets/docs/US%20Microfinance%20-%20Small%20Loans,%20Big%20Results.pdf>

Government Agenda	Role of Microfinance sector
<p>3. Uplift Agriculture, Build Dams and Conserve Water</p> <p>3a) Unleash Pakistan's potential in agriculture & Revamp the Livestock sector:</p> <p>Government will increase farmers' profitability and boost growth rate; there will be optimisation of existing subsidy programmes, reduction of input costs, transforming agriculture produce markets, <u>improve access to finance</u>, champion mechanisation and incentivise value-addition for exports.</p> <p>Agriculture is undoubtedly the backbone of Pakistan's economy as 45% of the labour force depends on this sector for livelihood. However, growth rates have been poor owing to bad policy decisions and poor implementation. Farm input costs are rising, our agriculture produce markets are monopolised, access to finance is dismal, bad practices are depleting our natural endowment, <u>climate change is adversely affecting our ecosystem</u>, value-addition of crops is weak, and agriculture related exports are far below potential. This gross neglect of the agriculture sector, <u>especially small farmers</u>, will hamper Pakistan's GDP growth rate if left unattended and an aggressive turnaround is now pertinent.</p> <p>The government aims to make <u>inputs cheaper for farming</u> to be profitable; <u>we cannot encourage a commodity price increase to achieve profitability as it will add to inflation</u>, but a one-time price adjustment may be required. However, we will decrease costs by:</p> <p>We will expand existing and create new <u>warehouses along with crop grading system in key locations across Pakistan under public-private partnerships</u>.</p> <p>We will expand existing and create new markets for <u>value addition</u>, e.g. organic farming, SME level processing to provide cheaper inputs for local manufacturers (reduce import burden), encourage high-value exports, etc.</p> <p><u>We will encourage private banks to roll-out digital loans for quick access with easier terms of repayment and launch warehouse receipt financing.</u></p>	<p>3a) Microfinance sector enjoys excellent outreach in rural areas. Out of the total exposure of microfinance in rural areas is 55%. The total exposure in agriculture and livestock is 40%.</p> <p>3a) We are now a major stakeholder in ACAC for increasing outreach to the marginalized farmers and adding to the borrowers instead of just increasing the amount of portfolio in value terms.</p> <p>3a) Current innovations in the sector account for value chain financing, investment in logistical value chains, creating warehouse subsidiaries and investment renewable energy and water conservation. To help achieve the current initiative, we want to be part of the 10 billion tree Tsunami campaign. As an industry we commit to contributing 500 million trees in 5 years. This will be done through provision saplings to all Microfinance clients every year especially those in rural and agriculture lending. We'll put up a Tree-counter at our website to measure the targets.</p> <p>3a) The microfinance sector is affected by natural calamities and hence we are developing a Disaster Risk Fund to hedge the risks to the industry and farmers. We also strongly believe in the fact that climate risk is leading to exclusion and hence this fund is very important in going to areas which are affected by climate.</p> <p>3a) Microfinance sector is being digitized under the NFIS, and we look forward to continuous support from the Government on this initiative.</p>

SECTION III

Recommendations from the Microfinance Sector

1. The current penetration of Microfinance needs more improvement especially with the current market size of 41 Million Micro-credit. Therefore, the sector needs to ramp-up growth projected 50% (20 Million) or 75% (30 Million). To achieve this scale of Microfinance operations, following challenges need to be addressed.
2. As indicated in microfinance Growth Strategy 2007 (EMFOP-Expanding Microfinance Outreach in Pakistan) and NFIS 2015 & 2018, Microfinance is a sustainable business model with triple bottom-line approach. We recommend that the present government should continue this stance and provide the level playing field through market-based approach.
3. A Microfinance committee should be setup that should develop a growth strategy to reach 75% Microfinance penetration till 2023.
4. As per the Government's own agenda, subsidy should be targeted, and graduation model should be followed, hence we strongly suggest that the govt should segment the poverty band and continue providing subsidy to BISP beneficiaries up to 16 on PPI scorecard, on the bracket of 16-40 provision of interest-free loan schemes to be continued. Government can either 1) provide funding from its budgetary support and cover operational costs of institutions or 2) fund through commercial banks and cover cost of capital (for commercial banks) and operational cost of Microfinance providers.
5. Conventional Microfinance will continue to work on a sustainable triple bottom-line model where govt will provide support through policy intervention and supervise through its regulators. In addition, any subsidy should help in enhancing growth and risk infrastructure for the sector.
 - a. **Enhancing Growth:** especially for low-penetration areas (markets are there such as Khyber Pukhtunkhwa & Azad Jammu Kashmir, but MFPs may not operate due to security situation in these areas) and marginalized segments (specific products for women, transgenders, Persons with Disability (PwD), and youth or innovation (alternate financial delivery channels, low-cost housing, renewable energy, low-cost education, drip irrigations and other innovative agriculture financing models. PMN is currently doing a research on an innovative approach on Warehouse Receipt Financing (WRF) and what ecosystem needs to be put in place by the government to benefit farmers and increase their income).
 - b. **Managing Risks:** this includes provision of guarantee schemes; setting up of Disaster Risk Fund (DRF) to mitigate risks of climate change; capacity building of the regulators.
6. Putting in place a '**Pakistan Stack**' along the lines of **India Stack**, which is a collection of open APIs (Application Program Interface) that belongs to multiple entities such as governments, businesses, startups and developers for utilising a unique digital Infrastructure to solve India's hard problems towards presence-less, paperless, and cashless service delivery.

INDIA STACK PROVIDES 4 DISTINCT TECHNOLOGY LAYERS

Presenceless layer

Where a universal biometric digital identity allows people to participate in any service from anywhere in the country

Paperless layer

Where digital records move with an individual's digital identity, eliminating the need for massive amount of paper collection and storage

Cashless layer

Where a single interface to all the country's bank accounts and wallets to democratize payments

Consent layer

Which allows data to move freely and securely to democratize the market for data

Increasingly, policymakers and key industry players are recognizing the potential of building technology stacks by layering platforms to tackle the issue of financial exclusion through large-scale biometric identity program known (in Pakistan's case it can be the CNIC and Biometric Verification System (BVS), which allows for fast and cheap identity authentication.

In Pakistan this can either government-driven technology stack, as in India, or a public-private partnership to provide a combination of public utilities and software standards that would increase both bank and non-banks entities' ability to offer consumers a broader range of financial services at lower costs. PMN plans to conduct a research to investigate the benefits and downsides of **India Stack** and come up with a set of recommendations to set up a '**Pakistan Stack**' where government involvement will be necessary to bring onboard all key stakeholders especially NADRA.

7. As indicated in point 1 & 2, government subsidy for insurance in the form of Sehat Insaf cards should be extended to low-penetrated geographical areas (Balochistan & FATA) and for beneficiaries who lie below 40 on the poverty scorecard. Microfinance sector should cover the remaining minimum 75% market by 2023.

8. For low-cost housing sector to grow, following are the recommendations:

- a. Long-term funding
- b. Enhanced limit
- c. Foreclosure law
- d. Land titles

9. For growth in agriculture finance, SBP is already pushing both commercial banks and MFPs. We recommend that the push should help in making availability guarantees and funding lines for small and marginalized farmers. We also recommend that given Agri sector subject to climate risk, supporting the sector in setting up the Disaster Risk Fund will play a critical role.

Annexure A: Poverty Measurement

About the PPI: A Poverty Measurement Tool

The Poverty Probability Index (PPI®) is a poverty measurement tool for organizations and businesses with a mission to serve the poor. The PPI is statistically-sound, yet simple to use: the answers to 10 questions about a household's characteristics and asset ownership are scored to compute the likelihood that the household is living below the poverty line. With the PPI, organizations can identify the clients, customers, or employees who are most likely to be poor, integrating objective poverty data into their assessments and strategic decision-making.

Why Measure Poverty?

Your organization may operate in a highly-impooverished area, but without objective poverty data on the households you reach, social performance management will rely on assumptions. Organizations that collect poverty data from all or a statistically significant sample of households they reach can: measure poverty outreach (i.e. the portion of customers, clients, or employees who live below the poverty line or are vulnerable to becoming poor), improve the performance of the intervention among the poor and poorest, and track poverty levels over time.

With these data, management staff can make informed strategic decisions and can provide stakeholders with objective evidence that the organization is reaching the poor and those vulnerable to poverty.

How Does the PPI Work?

Unlike other poverty measurement methods, the PPI was designed with the budgets and operations of real organizations in mind; its simplicity means that it requires fewer resources to use. The PPI is a set of 10 easy-to-answer questions that a household member can answer in 5 to 10 minutes. The questions are simple – “What material is your roof made of? How many of your children are in school?” The scored answers provide the likelihood that the survey respondent's household is living below the national poverty line and other internationally-recognized poverty lines. The PPI is country-specific and there are currently scorecards for 60 countries.

Today, the PPI has proven its reliability and feasibility to many organizations around the world. Armed with client-level poverty data, these organizations are now making more informed decisions and assessments. The PPI is now used by a wide range of organizations—international NGOs, social enterprises, donors, investors, multi-national corporations, governments and more—across a variety of sectors including agriculture, healthcare, education, energy, and financial inclusion.

Source: <https://www.povertyindex.org/about-us>



MicroNOTE: Microfinance Poised to play a vital role in achieving developmental objectives of the Government

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