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Impact of Microfinance in Promoting Rural Economic Growth in Nigeria

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Abstract
The need to develop the rural areas in developing countries where there have been decades of neglect are on the increase. It is against this background that this paper examined the impact of micro finance contribution to Nigeria's gross domestic product. Time series data for 12-years period 1999-2010 were collated from Central Bank of Nigeria published annual reports. The least squares (LS) regression was used to analyze the data. The result revealed that microfinance activities have negative and non-significant contribution to gross domestic product in Nigeria. The paper recommends that rural poverty is often a product of poor infrastructural facilities; therefore government should make a conscious effort towards industrializing the rural areas thereby motivating the micro finance institutions to locate their offices and extend credit facilities to rural areas thereby improving rural economic growth.
Keywords: Development, Contribution, Motivation. Growth.

Introduction

The core objectives of National Integrated Rural Development Plan (2000) for Microfinance banks are; to ensure significant reduction of poverty and ultimately its eradication in the shortest possible time; mobilize and empower rural population to create wealth through increased agriculture, industrial and other productive activities; promote the expansion of the productive base of the rural economy through the creation of non-agricultural enterprises; provide rural support services

needed to bring about increased production of goods and services; provide access to extension services, input, credit and marketing services; and to raise rural productivity in general. The Integrated Rural Development Plan identifies poverty reduction, mobilisation of savings and financing agriculture as the three cardinal transmission channels through which micofinancing will enhance rural economic growth and development.

Evidence in Latin American, Asian and African countries show that saving mobilization is one of the key activities in building a sound financial system (Lamberte et al., 2006) however, in developing countries, savings are often under mobilized. Two commonly cited underlying causes are: (1) prevalence of inappropriate saving products and poor services by depository institutions; and (2) lack of confidence in the safety or liquidity of financial institutions by rural people (De Aghion and Morduch, 2005). Therefore, to effectively and efficiently mobilize savings, saving products appropriate for rural savers need to be developed and depository institutions need to improve their services to this category of the population. Also, the institutions need to win the confidence of the rural people by building easy and friendly saving and withdrawal procedures. In Nigeria, the government through its legislation seem to exacerbate the micro credit banking crisis. For example, in 1990, the government established the Community bank to promote banking habit among the rural people and accelerate rural development through financial intermediation. In 2005, the government through the Central Bank of Nigeria mandated the existing Community Banks to migrate to Microfinance Banks (CBN, 2005). The regulatory framework for Microfinance banks changed the ownership structure of the Community Banks by allowing a single individual to own a microfinance bank. The regulation also increased the minimum share capital for microfinance banks to N2 billion Naira for unit banks and 10 billion for state banks (CBN, 2005). Such policy has the ability of creating un-level playing ground between the poor and the rich. The reform targets economically active poor without effectively address the deluge of problems the defunct Community banks encountered.

Additionally, towards the last quarter of 2010, the Nigerian Deposit Insurance Corporate conducted a nationwide investigation on all the microfinance banks in country. The findings led to the complete closure of about 224 microfinance banks (Vanguard, 2011). However, the remote cause of such crisis could be trace to the lagging supervision and liberal licensing of microfinance banks. This is because Central Bank of Nigeria was giving microfinance bank licences without proper regulatory and supervisory requirements. This situation led to the proliferation of microfinance banks without complying to the regulatory issues like, regular rendition to Central Bank, keeping proper book of account, among others.

This development triggered wide spread criticisms on the microfinance model by depositors and customers of the affected microfinance banks. Though, the Nigeria Deposit Insurance Corporation promised full protection for depositors, and publishes regularly, depositors that are yet to collect their claims. The Nature of microfinance clients makes the NDIC promise mere window dressing as some of them cannot read nor write, let alone having access to national dailies.

With such policy vacillation, the ability of micro finance banks in achieving the National Integrated Rural Development Plan (2000) in the Nigeria economy is not certain and also constitutes a very good research area. The essence of this study is

to fill this research gap. From the foregoing therefore, this study in line with the National Integrated Rural Development Plan (2000) seeks to examine the impact of micro finance activities on rural economic growth using on agricultural contribution to gross domestic product in Nigeria as indicators.

Review of Related Literature

According to Anyanwu (2004), the unwillingness or inability of the formal financial institutions to provide financial services to the urban and rural poor, coupled with the unsustainability of government sponsored development financial schemes contributed to the growth of private sector-led microfinance in Nigeria. Before the emergence of formal microfinance institutions, informal microfinance activities flourished all over the country. Informal microfinance is provided by traditional groups that work together for the mutual benefits of their members. Micro-credit is the process of lending capital in small amounts to poor people who are traditionally considered unbankable to enable them to invest in self-employment (Kasim and Jayasooria, 2001). The World Bank (2006) describes micro-credit as "a process in which poor families borrow large amounts (or lump sums) of money at one time and repay the amount in a stream of small, manageable payments over a realistic time period using social collateral in the short run and institutional credit history in the long run".

Mejeha and Nwachukwu (2008) say the dismal performance of the conventional finance sectors triggered the advocating of micro – financing by policy makers, practitioners, and international organizations as a tool for poverty reduction. Since its emergence, the number of microfinance institutions around the world has proliferated at a fast pace after the 1970s. Today there are more than 7000 micro – lending organizations providing loans to more than 25 million poor individuals around the globe (Mohammed and Hasan, 2008).
Iganiga and Asemotan (2008) say in Nigeria, like in many African countries, successive governments have implemented various agricultural and rural credit schemes as a means to address perceived shortage of rural credit, stimulate rural employment and productivity. Under these schemes, institutional resources, programme efforts and government energies were devoted, through parastatal based top-bottom interventions, to implement mostly supply led financial development strategies that is, the channelling of government supplied funds to rural entrepreneurs (Yaron, 1992).

Yi Luo (2006) say among the theories relating to finance boosting economic development, the important ones are the financial development thoughts of Goldsmith, Gurley and Shaw, the financial deepening theory of McKinnon and Shaw, and the financial development theories since the1990s.

Goldsmith (1969) first defined financial structure, specifying financial development as the change of financial structure, and conducted positive research using transnational data. Assuming positive correlation between financial system scale and financial service supply and service quality, he took the ratio of assets of financial intermediaries to GNP as financial development level, and demonstrated through positive research on the data of 35 countries over 103 years (1860 ~ 1963):

Rapid economic growth always went side by side with rapid financial development (faster than average). Gurley and Shaw (1955) held that financial development was a prerequisite for

economic growth. By analyzing the role of financial intermediaries, they examined financial systems with different structures, namely the impact of financial structure on economic growth. They theorized that finance served to convert savings into investments, thus enhancing the productive investment level of the entire society. Gurley and Shaw emphasized the significance of development of financial technologies, and pointed out that "the design and operation of a financial system may either accelerate the effective application of savings and investments or cause the ineffective use of fund". Gurley and Shaw directly pointed out that the cause of retarded economies of developing countries was inadequate financial development. The financial restraint hypothesis of finance restraint representatives McKinnon (1973) and Shaw (1973) advocated financial liberalization.

From the perspectives of Financial Restraint and Financial Deepening, they systematically expounded the relationship between monetary finance and economic development, for the first time systematically studied the characteristics of backward finance of developing countries, stated that governmental financial restraint policy hindered financial and economic development in developing countries, and proposed financial liberalization based chiefly on financial deepening. In addition, Patrick (1966) first brought up the cause and effect relationship between financial development and economic growth. He classified the viewpoints on the relation between financial development and economic growth into two kinds: supply-leading, which argues that financial development promotes economic growth; and demand-following, which alleges that financial development is only the passive reflection of the demand of economic growth for financial services.

According to Komicha (2007) it is important to make a conceptual distinction among some related terms: finance, rural finance, agricultural finance, rural credit and agricultural credit. Finance, in general, is the broadest concept encompassing all the other terms and representing the provision to meet operating and investment costs of an economic activity (Nelson and Murray, 1967). Rural finance is one of the broad divisions of finance, which comprises agricultural and non-agricultural finance, excluding financial services to urban households and firms. Agricultural finance specializes in the financing of the agricultural sector, which goes beyond provision of credit (Nelson and Murray, 1967). Rural credit is a narrower concept that specializes in provision of credit for rural households and firms, not only necessarily agricultural firms. Agricultural credit is the most specialized division, which provides credit service only to agricultural firms. Based on this distinction, "rural financial market" in this thesis refers to a market for rural financial services comprising agricultural finance, rural credit, and agricultural credit.

Methodology

According to Onwumere (2005), a research design is a kind of blueprint that guides the researcher in his or her investigation and analyses. The study adopts the *ex-post facto* research design. The secondary data were extracted from the Central Bank of Nigeria (CBN) Statistical Bulletin and National Bureau of Statistics (NBS). The relevant data include Microfinance loans and advances and agricultural contribution to gross domestic product.
The variables for the study are made-up of dependent and independent variables. Below is a breakdown of the respective variables and their justifications.

Independent Variable:

Micro-Finance Activity (MFA): The core function of banks is the channelling of fund between savers surplus and savers deficit. It is generally argued that the size of banks determines its ability to effectively carry out this operation. Financial intermediation is the ratio of aggregate deposit mobilised divided by total aggregate loans. Scholars have never disagreed on the appropriateness or robustness of this proxy in determining intermediation function. This study will adopt the measure as a proxy of financial intermediation (see, Eboh, 1996).

$$\text{Micro-finance activity} = \frac{\text{Aggregate loans and advances}}{\text{Aggregate Deposit}} \quad \ldots\ldots\ldots\ldots\ldots \text{(i)}$$

Dependent Variables Rural Economic Growth (REG)

Gross domestic product is often used as a measure of economic growth on economic-wide basis. This measure captures the rural and urban economic activities. However to capture rural economic growth, it is suggested that studies should adopt measures that are peculiar to the rural economy. This thinking has influence researchers to use the agricultural contribution to gross domestic product since the bulk of agricultural activities are in the rural areas (see Osinubi, 2003), The agricultural sector employs 90% of the rural population. This study adopts this as a measure of rural economic growth in Nigeria.

$$\text{ACGDP} = \frac{\text{Agricultural Sector GDP Output}}{\text{Aggregate Gross Domestic Product}} \quad \ldots\ldots\ldots\ldots\ldots\ldots \text{(ii)}$$

The objective of the study was modelled and tested using the Ordinary Least Square Regression model. The justification for adopting this analytical technique is based on the following premise; the ordinary least square is assumed to be the best linear unbiased estimator (Gujarati, 1995); it has minimum variance (Onwumere, 2005), and similar works in other jurisdiction adopted this technique in their paper. The variables are scaled to overcome the problem of heteroskedaticity associated with Ordinary Least Square. The simple regression equation is stated thus;

$$Y = B_1 + B_2X_2 + B_1 + u \quad \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots \text{(iii)}$$

Where, Y =dependent variable; X =explanatory variable; B_1 =intercept of Y; B_2 =slope coefficients; U =stochastic variables (Gujarati, 1995).

In order to specify the model for the study, equation (iii) is transformed to suit the objective as follow, thus, given that Microfinance activities do not have positive and significant impact on rural economic growth, it is represented as;

$$REG = a + bMFA + \mu \quad \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots \text{(iv)}$$

where:

REG = Rural Economic Growth
a = Constant of the Equation
b = Coefficient of the Independent Variable
MFA = Micro-Finance Activity
u = Error Term

Analysis of Data

Table 4.1 presents the nominal value of the respective data.

Table 4.1
Nominal Values of Model Data

Year	ALA (N,m)	AD (N,m)	AO (N,m)	GDP (N,m)
1999	2958.3	4140.32	114570.7	312183.5
2000	3666.6	7689.4	117945.1	329178.7
2001	1314	3294	122522.3	356994.3
2002	4310.9	9699.2	190133.4	433203.5
2003	9954.8	18075	203409.9	477533
2004	11353.8	21407.9	216208.5	527576
2005	28504.8	47523.7	231463.6	561931.4
2006	16450.2	34017.7	248599	595821.6
2007	22850.2	41217.7	266477.2	634251.1
2008	42753.06	61568.1	283175.4	672202.6
2009	58215.17	76662.04	299996.9	716949.7
2010	51986.15	74055.53	185660.13	773588.7

Source: CBN Statistical Bulletin 2010
Note:
ALA = Aggregate Loans and advances
Ad = Aggregate Deposit
AO = Agricultural Output
GDP = Gross Domestic Product

The nominal values of the model proxies was presented in table 4.1.In 1999, the aggregate loans and advances was N2, 958.3m and this rose to N3, 666.6m in 2000. In 2001, the aggregate loans and advances fell to N1, 314m but again picked up in 2002 when the aggregate loans and advances rose to N4, 310.9m. This again increased in 2003 when it was N9, 954.8m. The increased continued through to 2005, however, it fell in 2006 to N16, 450.2m but increased to N22, 850.2m in 2007 and continued the increase to 2009 when it rose to N58, 215.17m but fell to N51, 986.15m in 2010.

The aggregate deposit also showed fluctuation from 1999 to 2010. In 1999, the aggregate deposit for all microfinance banks in Nigeria was N4, 140.32m and this increased to N7, 689.4m in 2000. However in 2001, the aggregate deposit fell to N3, 294m but increased to N9, 699.2m in 2002. The increase continued in 2003 when the aggregate deposit rose to N18, 075m and through to 2005 when it was N47, 523.7m. In 2006, the aggregate deposit fell to N34, 017.7m however, it increased to N76, 662.04m but fell to N74, 055.53m in 2010.

The agricultural output in Nigeria was N114, 570.7m in 1999 and rose to N117, 945.1m in 2000. The increased in agricultural output continued in 2001 through to 2009 when it was

N122, 522.3m, N190, 133.4m, N203, 409.9m, N216, 208.5m, N231, 463.6m, N248, 599m, N266, 477.2m, N283, 175.4m and N299,996.9m. However in 2010, agricultural output fell to N185, 660.13m.

Again the gross domestic product of Nigeria was also revealed in table 4.1. In 1999, the total goods and services produced in Nigeria was N312, 183.5m and this increased to N329, 178.7m in 2000. In 2001, it again rose to N356, 994.3m and in 2002, it was N433, 203.5m. In 2003, the total goods and services produced in the country as revealed from the table was N477, 533m while in 2004 it rose to N527, 576m, and in 2005 it was N561, 931.4m. In 2006, Nigeria GDP rose to N595, 821.6m and the increase continued through to 2007, 2008, 2009 and 2010. It was N634, 251.1m, N672, 202.6m, N716, 949.7m and N773, 588.7m respectively.

Table 4.2
E-VIEW Regression Results
Dependent Variable: ACGDP
Included observations: 12

Variable	Coefficient	Std. Error	t-Statistic	Prob.
MFA	-0.259897	0.292281	-0.889203	0.3948
C	0.520990	0.171505	3.037759	0.0125
R-squared	0.773274	Mean dependent var		0.371347
Adjusted R-squared	0.619398	S.D. dependent var		0.113417
S.E. of regression	0.114512	Akaike info criterion		-1.345262
Sum squared resid	0.131130	Schwarz criterion		-1.264444
Log likelihood	10.07157	F-statistic		0.790682
Durbin-Watson stat	1.442114	Prob(F-statistic)		0.394781

Source: Author's E-view Result

From the table above, it indicates that Micro finance activities in Nigeria for the period of this study had a negative and non-significant impact on agricultural sector contributions to Nigeria's gross domestic product (coefficient of MFA = -0.259, t-value = -0.889). The coefficient of determination represented by 77.3% indicated that the variation observed in the model was captured appropriately. While the Durbin Watson d test statistic was 1.44, the probability was 0.394 > 0.05 indicating that the impact of MFA on agricultural sector contribution was insignificant. Based on the results, the null hypothesis which states that Micro finance activities do not have a positive significant impact on agricultural sector contributions to Nigeria's gross domestic product is accepted while the alternate hypothesis is rejected.

Conclusion and Implications Discussion

Micro-credit is the process of lending capital in small amounts to poor people who are traditionally considered unbankable to enable them to invest in self-employment (Kasim and Jayasooria, 2001). The World Bank (2006) describes micro-credit as a process in which poor families borrow large amounts (or lump sums) of money at one time and repay the amount in a stream of small, manageable payments over a realistic time period using social collateral in the short run and institutional credit history in the long run. Microfinance is expected to

cater to the financing needs of rural dwellers thus enhancing the economic wellbeing. In addition, microfinance borrowers are typically self-employed, household-based entrepreneurs who have relatively unstable income sources and can be divided into two groups: rural and urban. In rural areas, the borrowers are usually small farmers and others who are engaged in small incomegenerating activities such as food processing and petty trade; while in urban areas, microfinance activities are more diverse and borrowers include shopkeepers, service providers, artisans, street vendors, and small-medium enterprises (Sapovadia, 2006).

According to Anyanwu (2004) who was of the view that the unwillingness or inability of the commercial financial institutions to provide financial services to the rural poor, coupled with the unsustainability of government sponsored development financial schemes contributed to the establishment of microfinance banks in Nigeria, therefore the core objectives of for the establishment micro finance banks are; to ensure significant reduction of poverty and ultimately its eradication in the shortest possible time; mobilize and empower rural population to create wealth through increased agriculture, industrial and other productive activities; promote the expansion of the productive base of the rural economy through the creation of non-agricultural enterprises; provide rural support services needed to bring about increased production of goods and services; provide access to extension services, input, credit and marketing services; and to raise rural productivity in general.
However, as shown by this study, Micro finance activities for the period of this study had a negative and non-significant impact on agricultural sector contributions to Nigeria's gross domestic product which indicates that the introduction of micro finance banking in Nigeria have not contributed to agricultural productivity in Nigeria.

It implies that rural poverty is often a product of poor infrastructure that hinders development and mobility as the rural areas tend to lack sufficient roads that would increase access to agricultural inputs and markets. Without roads, the rural poor are cut off from technological development and emerging markets in more urban areas. Poor infrastructure hinders communication, resulting in social isolation among the rural poor, many of whom have limited access to media and news outlets. It is therefore against these problems that most financial institutions would rather locate their offices in urban Centre where there are these basic social infrastructure than be located in rural areas. Therefore as a means to improving rural economic growth in Nigeria there should be a conscious effort by government to industrialize the rural areas as this will serve as a motivation for micro finance institutions to locate their offices in the rural areas. This will improve rural economic growth.

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