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## **Micro-financing as Poverty Reduction Strategy: a Case Study of Oredo and Egor Local Government Areas of Edo State, Nigeria**

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### **Abstract**

*Micro-finance is another source of credit facility being encouraged in Nigeria as anti-poverty strategy tool to assist the poor and low income group to enable them access credit (finance) so as to engage in meaningful commercial activities to pull them out of poverty. The paper attempts to find out if the strategy is helping the poor and low income group to access credit. The survey method was adopted for the study and the primary and secondary sources of data collection were used to elicit data for the study. In the two local governments used as case study, it was discovered that many people in the low income group and the poor have been able to access credit;*

*and it is helping them to move out of poverty. However, it was discovered that there are many flaws that are militating against the strategy, among which are stringent collaterals, high cost of operations and high interest rate. The corrections of these flaws will help many poor and low income groups access credit and reduce poverty in the country. The paper recommends among others, that the interest rate of financial institutions be reduced and collateral requirements should be reduced to enable more low income earners benefit.*

### **Introduction**

Many people out there remain where they are – economically and socially stagnated. This is because they cannot afford to access credit (money) which can enable them make meaningful living to survive. They remain at the lowest rung of the economic and social ladder due to poverty, partly occasioned by their inability to access credit. Poverty is not what anybody craves for. The society or leadership of society can cause poverty. Poverty pertains to people's inability to access economic resources for consumption of economic goods and services; hence poverty is sometimes defined as economic deprivation.

In Nigeria, many strategies have been applied to fight poverty. These different strategies are the products or programmes of different administrations in the country, whether military or civilian. But none seems to have provided the much-needed impetus to tackle poverty. Many of the strategies cum programmes experience failures due to one reason or another.

But the country's leadership did not rest on its oars hence emphasis was placed on microfinance, a subsector of the financial sector of the economy. This is another strategy the government is applying to fight poverty, especially since 2005. Though micro-financing has been in practice in Nigeria and other developing countries for over a century, the government has seen reasons to dovetail it into the main stream of the financial sector of the economy so as to officially mainstream the people, especially the poor and low income group into it. It is necessary to know if micro-financing is helping to fight poverty in the country, hence two local government areas of Edo State is used as a case study.

### **Theoretical framework**

There are four theories of poverty. According to Johnson (1968), these are the power theory of poverty, the capitalist entrepreneurial theory of poverty; the individual theory of poverty, and the corruption theory of poverty. In this paper, the corruption theory would be applied because it suits the Nigerian situation.

The corruption theory looks at the root causes of poverty in the third world cities and attributes them to the following factors:

- Inadequate access to employment opportunities
- Inadequate physical assets such as land, capital, and minimal access by the poor to credit facilities, even on small scale
- Inadequate access to the means of supporting rural development in poor regions.
- Inadequate access to market where the poor can sell goods and services.
- Low endowment of human capital.
- Lack of participation, failure to draw the people into the design of development programmes, and so forth.

This means, the interaction of these factors places a large portion of the population or society in the vicious circle of poverty, which is characterized by low productivity which leads to low per capital income. Where there is low per capital income, there will also be low level of savings per head which will in turn results to low level of capital formation or accumulation, which eventually will results to low level of productivity.

In Nigeria, wealth imbalance is one of the factors that fuels insecurity. This is because economic growth is not impacting positively on the welfare of the citizens. According to Lamido Sanusi (2012), “the increasing rates of insecurity and civil unrest in the country originated from the prevailing high level of wealth imbalance”. Corruption and mismanagement of the commonwealth have made few people super rich while majority of the populace still live in abject poverty. In Nigeria, ninety per cent of the people still live on less than \$2 per day, while seventy per cent still live on less than \$1 per day, and so many women dying in child birth, so many children are out of school, life expectancy is as low as 55 or 54.<sup>74</sup> This is because more than half of the nation’s wealth is controlled by few powerful individuals who explore the leakages in the system to make illegitimate money; and these powerful people are in the corridors of power.

The manner with which those in the corridors of power corner the wealth of this country through unbridled embezzlement of the nation’s resources is capable of causing poverty. Also, the manner in which the leaders, past and present implemented the various policies aimed at poverty reduction did not help the poor out of poverty. Instead, the poor remain poorer because they could not benefit from the policies and programmes hence the status quo the country finds itself today. The structures that were put in place to implement the various policies and programmes were either weak or were tilted towards the direction of those in power. If institutions and structures are not properly established or funded, the impact of policies and programmes would not be felt by the target beneficiaries.

One of the outcomes of good governance is the provision of the specific needs of the people or nation. The basic things are those things which the citizens should have to assist them survive as human beings. These include clean water, air, balanced food, physical and emotional security, physical and mental rest, shelter and infrastructural facilities, provision of enabling environment for private sector to thrive. A nation where these are lacking shows that there exists bad governance and such country cannot run away from poverty. In fact, poverty is not a creation of the individual. A society causes poverty. The individual is a victim of poverty. Good governance can reduce poverty through proper management of an economy.

In spite of the microfinance policy which has formally brought micro-credit scheme to the knowledge of the larger society, a large segment of the low income group and the poor still find it hard to live above the poverty line. This is because almost all the above mentioned needs are lacking. For example, the people need energy (electricity) to operate their businesses in order to survive. They need good roads and drinking water. The absence of these basic needs is diminishing their capabilities and efforts to leave the shackle of poverty.

It is necessary to further state that the state or society (through its representatives called government) should use its powers – political, economic, and social, to motivate and create the right frame of aptitude to create wealth for the people. It is the people (masses) that make up the state or society, and government exists for the people hence it is for their benefit government must act at all times. It is also the duty of government to create the conducive atmosphere for people to create wealth for themselves so as to enable them live a comfortable life. This would enable the people, both rich and poor, contribute to the good and progress of the society. Good atmosphere or environment can create good aptitude. Similarly, good governance can create abilities for the people to express themselves productively. Productive people beget a progressive and productive society or nation.

### **Conceptualisation of Microfinance**

Microfinance is the provision of financial services to poor or low-income groups, including consumers and the self-employed. Microfinance is a movement that envisions “a world in which as many poor and near-poor households as possible have permanent access to an appropriate range of high quality financial services, including not only credit but also savings, insurance, and fund transfers” (U.N.D.P., 2004). In fact, those who promote microfinance generally believe that such access will help poor people out of poverty.

Microfinance refers to that part of the financial sector that responds to the financial demands of low-income households or individuals who were traditionally shut out of the credit market because they could not provide collateral. Microfinance extends

small loans to poor people for self-employment projects and economic activities that generate income, allowing them to care for themselves and their families. As an anti-poverty tool, it has great scope for empowering poor people to alleviate their poverty to a great extent. Microfinance is usually conceived of as the provision of small units of financial services to low-income clients or earners who are usually excluded from the main stream financial systems. It is a form of financial intermediation which primarily focuses on alleviating poverty through provision of financial services to the poor or owners of micro enterprises.

Microfinance is also the extension of small loans to entrepreneurs too poor to qualify for conventional bank loans. It has proven to be an effective and popular measure in poverty alleviation programmes, enabling those without access to formal lending institutions to borrow at competitive rates, and start small businesses (United Nations Environment Programme, 2003). The key implication of microfinance is in its name: 'micro'. A number of issues came to mind when 'micro' is considered, that is, the small size of the loans made, small size of savings made, the smaller frequency of loans, shorter repayment periods and amounts, the micro/local level of activities, and the community-based immediacy of microfinance (United Nations Environment Programme, 2003).

However, it needs to be emphasised that microfinance is not new in Nigeria. The precedence for microfinance lies in the numerous traditional and informal systems of credit that have existed in developing economies like Nigeria for centuries, long before modern, western-based commercial banking came into being. Savings and credit groups that have operated for centuries in developing countries include the "susus" of Ghana, "Ajo or Esusu/Osusu" in Nigeria, "chit funds" in India, "tandas" in Mexico, "arisan" in Indonesia, "cheetu" in Sri Lanka, and "pasanaku" in Bolivia (Central Bank of Nigeria, n.d.).

Microfinance is an enabling, empowering, and bottom-up tool for poverty alleviation that has provided considerable economic and non-economic externalities to low-income households in developing countries. Microfinance is being hailed as a sustainable tool to combat poverty, combining a for-profit approach that is self sustaining, and a poverty alleviation focus that empowers low-income households. Microfinance is increasingly becoming a tool to exercise development priorities for governments in developing countries (Central Bank of Nigeria, n.d.).

### **Clients of Microfinance**

Microfinance clients are usually the self-employed, low-income entrepreneurs located in both urban and rural areas. The clients are often traders, street vendors, small farmers, services providers like hairdressers, cart pushers; artisans and small producers such as black smiths and seamstresses. In fact, their activities provide

income (often from more than one activity) for the individuals and their households. It should be noted that the clients are often poor, but they are generally not considered to be the “poorest of the poor” (Ehigiamusoe, 2000).

In the absence of commercial bank loans, access to microfinance affords low-income groups to receive loans for their economic activities. Programmes and organisations that provide credit to low-income groups make a clear match between the quality and quantity of credit, and the capacity of the poor to utilize that credit – at the same time being organizationally sustainable.

### **Misconceptions about the Poor and Economic Activities**

Before now, the poor were not taken into recognition as people who can borrow money and pay back. The poor were thought as those who cannot save. However, events of over two decades ago have proved that the poor can save, not only can the poor save but can borrow and pay. That is why the attempts of very poor people to help themselves through self-employment were ignored by the formal financial sector (UNDP, 1997). The reasons were that, traditionally, the very poor have not been recognized as credit worthy or able to have savings and also because, using traditional commercial banking methods by lending to the poor was not believed to be cost-effective (UNDP, 1997).

However these misconceptions were debunked by the United Nations Development Programme thus:

S/N	Myth	Reality
1.	Micro entrepreneurs need to be cared for because they are poor.	Micro entrepreneurs are knowledgeable about doing business in their local economy. They often have years of experience in their trade working with dedication and determination. Belief in the intelligence and business knowledge of clients is critical.
2.	Micro entrepreneurs are redundant activities that should be replaced by larger businesses employing many people.	While often marginal, micro-entrepreneurs are viable, locally important activities that should be upgraded. These small-scale economic activities are valid business activities to be taken seriously.
	Credit alone is useless. It must be	Although programmes which package credit with other services may seem ideal, they require large

	packaged with training, marketing, technology, and other services.	subsidies and have proven to be largely unusable. The minimalist approach used by the Grameen Bank and many others has shown that clients can use credit in small amounts to start or improve the profitability of their microenterprises. Providing marketing and many other areas of services is valid, but best managed separately.
3.	The poor cannot be trusted with credit. The consumption needs of the poor are so pressing that any loan will find its way quickly to consumption.	The high repayment rate of millions of microfinance clients is empirical proof that the poor are creditworthy.
4.	The poor are unable to save.	The high rate of savings reported by many microfinance organizations demonstrates that the poor can value savings as much as credit.

**Source:** UNDP (1997) Microcredit, a guide for planning, starting and managing a microfinance programme. Culled from *Poverty Alleviation in Nigeria*; Nigerian Economic Society, 1997 Annual Conference, p.371

According to Muhammad Yunus (1995), “all human beings are born entrepreneurs. Some get the opportunity to find this out, but some never get this opportunity. A small loan can be a ticket to exploration of personal ability. All human beings have a skill – the survival skill. The fact that they are alive proves this. Just support this skill and see how they will choose to use it.”

#### **Importance of access to finance by the poor**

Access to financial services enables the poor to increase their household incomes, build assets and reduce their vulnerability to crises that they face on daily lives. Financial services can put power into the hands of poor households, allowing them to progress from hand-to-mouth survival to planning the future, acquiring physical and financial assets and investing in sustainable livelihood initiatives. Access to financial services also translates into better nutrition, improved health and long-term plans for their future and those of their children. One of the most important roles of access to credit is that it enables the poor to diversify their incomes. Most poor households do

not have one source of income or livelihood. Instead, they pursue a mix of activities depending on the season, prices, their health and other contingencies.

Financial services can play a critical role in reducing poverty. The ability of the poor to borrow a small amount of money to take advantage of a business opportunity not only impacts positively on the eradication of poverty but also tends to increase the ranks of micro entrepreneurs.

In 2004, a group of organisations known as Consultative Group to Assist the Poor (CGAP) and endorsed by the Group of Eight (G8) leaders at their summit on 10th June, 2004 came up with some principles to re-emphasise the need for microfinance. Among the principles are that:

- i. poor people need not just loans but also savings, insurance and money transfer services.
- ii. microfinance must be useful to poor households – helping them raise income, build up assets and/or cushion themselves against external shocks.
- iii. microfinance also means integrating the financial needs of poor people into a country's mainstream financial system.
- iv. the job of government is to enable financial services, not to provide them.
- v. interest rate ceilings hurt poor people by preventing microfinance institutions from covering their costs, which chokes off the supply of credit.

### **The microfinance policy**

Realising the need to help the poor have access to credit (finance), the federal government, in December 2005, came up with the microfinance policy and regulatory framework. The policy encompasses three strands, that is, of policy objectives, policy targets, and policy strategies. The policy objectives comprised, among others: to make financial services accessible to a large segment of the potentially productive Nigerian population which otherwise would have little or no access to financial services; to promote synergy and mainstreaming of the informal sub-sector into the national financial system; enhance service delivery by microfinance institutions to micro, small and medium entrepreneurs; contribute to rural transformation. The policy targets comprised, among others: to cover the majority of the poor but economically active population by 2020 thereby creating millions of jobs and reducing poverty; to increase the share of micro credit as a percentage of total credit to the economy from 0.9 percent in 2005 to at least 20 percent in 2020; and the share of micro credit as a percentage of GDP from 0.2 percent in 2005 to at least 5 percent in 2020; to eliminate gender disparity by improving women's access to financial services by 5% annually; and the policy strategies also contained, among others, to



mobilise domestic savings and promote the banking culture among low-income groups.

### **Objectives**

The objectives of the paper are

- i. to find out if the poor has access to loans from microfinance banks and institutions
- ii. ascertain if microfinance has assisted in alleviating poverty in the Egor and Oredo local government areas of Edo State.

### **Methodology**

In order to get proper response for the objective, two sets of audiences were targeted. These were the staff of microfinance banks and their clients/customers in the two local government areas.

### **Research questions**

Two research questions for the study are:

- (i) Are the poor able to access loans (credit/finance) from the microfinance banks?
- (ii) Has microfinance enhanced the welfare of the poor in the two local government areas?

### **Research Design**

To get the true impact of microfinance on poverty alleviation in the two local government areas, the survey method was adopted for the author. A total of 360 respondents were interviewed. Out of the number, 60 were staff of microfinance banks and institutions, while 300 were clients/customers who patronize microfinance banks in the two local government areas of the state.

Two separate questionnaires were designed for the purpose and research. The first questionnaire for staff contained 33 questions while the second, for clients, contained 25 questions. The two questionnaires were divided into sections A and B. Section A contained the bio-data of the respondents while the section B contained microfinance activities.

### **Data analyses**

After the collection of data from the field, the percentile method of analysis was adopted to analyse the information that were got from the respondents. The results from the field survey are indicated on the tables below.

**Table 1:** Respondents by sex (staff and clients)

Sex	No. of staff	%	No. of Clients/beneficiaries	%
Male	27	45	99	33
Female	33	55	201	67
Total	60	100	300	100

Source: Field Survey 2013

The results show that the female folk patronized microfinance services more than the males. It is also an attestation that the female folk are more prone to poverty than the males; and female are more than males among the staff of microfinance banks.

**Table 2:** Patronage of microfinance services by sex

Response	No.	%
Males	9	15
Females	51	85
Total	60	100

Source: Field Survey 2013

Table 2 shows that 9 of the respondents, representing 15% of the staff said male clients are more in number than females, while 51 of them, representing 85% said female clients are more in number than male clients. These results are confirmation of the theory of microfinance that the services are more targeted at the female folk. It also confirms that females (mostly women) are more prone to poverty, and are more in the poverty bracket than the males.

**Table 3:** Sources of credit/finance for trade/business start-up

Response	No.	%
Personal savings	105	35
From Osusu	44	15
Microfinance bank/institution	148	49
Others, specify	3	1
Total	300	100

Source: Field Survey 2013

Table 3 shows that 105 (35%) of the respondents started their businesses/trades from personal savings, 44 (15%) started with money from osusu, 148 (49%) started from capital/credit accessed from microfinance banks/institutions, 3 (1%) specified others other sources like assistance from relatives. This shows that many people in the low income group have embraced the formal financial sector to source for credit facilities.

It also means that they have been mainstreamed into the formal financial sector of the economy.

**Table 4:** Business performance since clients embraced micro-financing as source of credit

Response	No.	%
Fairly good	21	7
Good	69	23
Better	108	36
Very good	89	30
Abstention	13	4
Total	300	100

Source: Field Survey 2013

Table 4 shows that 21 (7%) of the client-respondents said their trade have been fairly good, 69 (23%) said their businesses have been good, 108 (36%) said their businesses have been better, while 89 (30%) said their businesses have been very good, 13 (4%) abstained from the question.

This shows that microfinance services have helped most people in the low income group since the last five years. It is an indication that many of the client-respondents are being moved from the shackles of poverty. Similarly, it shows that microfinance is contributing to Nigeria's Gross Domestic Product (GDP).

**Table 5:** Number of persons that operated business before clients embraced micro-financing as source of credit

Response	No.	%
Only me	181	60
Me and my family members	56	19
I employed one person I paid	20	7
I employed more than one person I paid	30	10
Abstention	13	4
Total	300	100

Source: Field Survey, 2013

Table 5 indicates that 181 (60%) of the client-respondents said they have been operating their businesses alone before they started taking loans from microfinance banks, 56 (19%) said only themselves and their family members have been operating their business activities, 20 (7%) said they employed one person they paid, 30 (10%) said they employed more than one person they paid, 13 (4%) abstained from the

question. This means that majority of them have been operating their businesses alone before they started taking loans from microfinance banks/institutions.

**Table 6:** Number of persons that operated business after clients embraced micro-financing as source of credit

Response	No.	%
I employed one person I pay salary	128	43
I employed two persons I pay salary	52	17
I employed more than two persons I pay salaries	55	18
I cannot employ any person because the business/trade is not moving	33	11
Abstention	32	11
Total	300	100

Source: Field Survey, 2013

Table 6 shows that 128 (43%) of the client-respondents said they employed one person they pay salary, 52 (17%) said they employed the two persons they pay salaries, 55 (18%) said they employed more than two persons they pay salaries, 33 (11%) said they cannot employ any one because their businesses are not moving; 32 (11%) abstained from the question.

This is an indication that microfinance service is yielding the desired results because most of the respondents have employed additional persons to themselves since they started borrowing money from microfinance banks/institutions. Beside the reduction of poverty, microfinance is gradually reducing unemployment in the economy thereby contributing to the nation's Gross Domestic Product, economic growth and development.

#### **Flaws in the Nigeria microfinance sector**

In spite of the little success microfinance has made in poverty reduction in the country in general and the two local governments in particular, there are some fundamental flaws that are equally noticeable in the sector. The microfinance banks/institutions and the regulators of the sector are responsible for these flaws. The flaws are:

(a) Not for the poor

The manner with which microfinance banking is operated in the country negates the main purpose which it was enunciated. This is because it is not meant for the poor, or the poorest of the poor. Rather it is for only traders, suppliers and importers. This practice is responsible for the cut throat interest rates charged by the microfinance banks/institutions. It is targeted at the rich.

(b) Urban-oriented

The other flaw is that majority of the microfinance banks are located in the cities and urban areas of the country. It ought to be rural-oriented or rural base. They ought to be located in the villages. The remoter they are located from the cities/towns, the better it is for the poor.

(c) Collaterals

Microfinance banks in the country demand for collaterals. This equally negates the practice of microfinance banking. On the other hand, many of these banks do not lend to start businesses/trade. Also, many of them do not educate their clients on how to operate businesses/trade. All they need is profit or interests.

(d) Ownership

The microfinance banks are owned and financed by the rich. Hence the cut throat interest rates. Microfinance banks ought to be owned by the poor themselves. It is when it is owned by the poor, particularly the women, that the poor can benefit maximally.

(e) High interest rate

Microfinance banks in the country are allowed to charge interest rates; some rates are too high that the poor cannot pay. The regulators do not show concern. If the scheme is meant for benefit of the poor as the policy intends, the poor, and the poorest of the poor should be excluded from paying interest rates. If they are required to pay interest rate it should be very low and should be graduated according to the activities the loans are invested in.

(f) Cost of operation

The microfinance banks spend much on their operations. They always operate from costly edifices/buildings which rents are costly; they also acquire exotic vehicles for their operations. Instead of doing the business at the door steps of the poor they prefer the poor to come to them. These increase cost of operations.

(g) Profit oriented

The promoters of microfinance banks in the country are always profit oriented. They see microfinance banking as a cheap access to owning a bank. This is the reason why targets are set for staff and management. By so doing, the microfinance banks are not solving the problems for which they are intended, that is, poverty. According to Yunus (2011), "microfinance is a

social business; it is not for profit but to help people out of poverty. This is because poverty is the fault of the society, the individual is just a victim of poverty”.

### **Findings**

Findings show that

- (a) more females benefit from the microfinance services than the males, similarly, more females were employed than males by the microfinance institutions and banks.
- (b) almost fifty per cent of the clients/respondents sourced their credit/finance from microfinance banks/institutions for their trade or business activities.
- (c) the business performances of most of the respondents who sourced their credits from microfinance banks/institutions improved significantly.
- (d) most of the respondents employed more hands to operate their businesses after they embraced micro-financing.

### **Conclusion**

Micro-financing is a good strategy to tackle poverty. It is heart-warming to know that the poor and low income group are fast embracing the scheme. It is a demonstration that the low income group and the poor are being mainstreamed into the economic hub of the country through the strategy. This is good for the economic growth and development of the entire country. The continuous promotion of the strategy, particularly the microfinance policy, would propel those in the low income segment of the society to contribute to the country's Gross Domestic Product and at the same time enhancing the wellbeing of the poor on the long run.

### **Recommendations**

The following recommendations are the fall out of the empirical study conducted during the research.

- (i) The poor and low income group should not be misconstrued as people who cannot be trusted with credit facilities.
- (ii) The issue of collaterals should be reviewed so as to enable more poor and low income group access credit. Many of them, the poor and low income group, cannot afford stringent collaterals.
- (iii) The interest rate of microfinance banks and institutions should be reduced so as to make the scheme and strategy properly pro-poor.

- (iv) The poor should be incorporated into the mainstream of the sector by creating avenues or opportunities for them to be co-owners or stakeholders in the microfinance banks and institutions.

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**Table 7:** Reasons why some microfinance banks/institutions have no branches in rural areas

Type of Reasons	No. of staff	%
Most rural people are not embracing microcredit scheme	12	20
Rural people prefer the informal type of microcredit scheme	9	15
Rural people always default in payment	7	12
They are hard to manage	3	5
Lack of sufficient fund to service the rural areas	18	30
Inadequate manpower to man the branches	9	15
Abstention	2	3
Total	60	100