

Micro Finance and Small Enterprises Development: Client Perspective Study of Baluchistan, Pakistan

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ABSTRACT

This paper presents findings of a user perspective study on the impact of micro finance on small enterprises development in Baluchistan, Pakistan. The study is based on primary research conducted by the authors in Quetta city of Baluchistan, Pakistan to examine if micro credit program has sufficient impact on the development of small enterprises. Following Eoin Wrenn model, strong evidence was found that access to external credit increases the social and economic growth. The data showed that income of the clients was increased, their businesses were improved, and their social mobility and social network were increased after the utilization of micro credit. Microfinance helps women by providing them social mobility and opportunities to interact with the business related persons that boost their confidence and managerial skills. So it confirms that micro-finance and micro enterprise development may serve as a catalyst towards social and economic change and poverty alleviation.

1. BACKGROUND/ INTRODUCTION

Most productive activities entail a time lag between the time when inputs are acquired and the time when output is obtained. For this reason, when self-financing is not possible, the inputs must be purchased using credit from financial institutions or informal sources. The financial contracts available in rural and urban areas vary substantially depending on the characteristics of the borrowers and lenders and the type of input being financed. Credit plays an important role in development. It capitalizes farmers and entrepreneurs to undertake new investments or adopt new technologies. It helps smooth consumption by providing working capital and reduces poverty in the process (Khandar, Shahidur). Credit is a very important component for the development /growth of businesses whether it is small, medium or large, but its importance varies with respect to the life cycle of the enterprise. In its initial stage it has much importance as well as in the growth period but when it becomes stables then its importance decline. When we talk about business enterprise then there are two sources of credit

available to them, informal and formal. Informal credit is the credit provided to them by friends, moneylenders, shopkeepers, and other relatives. Unlike formal finance, informal finance may not be as conducive to development because: (i) it is expensive, (ii) it is short-term and largely used for consumption, and (iii) it is not large enough to spur investment and growth (ibid).

Microfinance is a tool for poverty reduction. As such microfinance addresses poverty by providing poor households with access to working capital and financial services that are essential for availing an economic opportunities. Microfinance also facilitates household investments in the diversification of income generation, thereby reducing the risk of sliding back into chronic poverty. An important outcome of microfinance is the impact it has on the transformation of household level balance sheets through the accumulation of additional productive assets and stores of value that are more profitable than traditional approaches to savings activity that are little more than hoarding (Remenye, Joe 2002) .

Many believe that vicious cycle cannot be overcome unless many of the social disadvantages faced by the poor are addressed properly (Hassan; Kabir M, 2002). Access to transfers and credit, whether cash or in-kind, is a major source of poverty alleviation in many developing countries around the world. For many poor households, these public and private gifts and loans make up a substantial portion of their yearly incomes and provide an important means to generate additional income (Mary Mackeman, Pitt M. Mark 2004).

Micro enterprises are also an important vehicle for low-income people to escape poverty through market-driven productive activities and break the “vicious cycle” (Siebert, Horst 2000) of poverty by using the microfinance for the production activities with their low savings, which results in a moderate investment thus increasing their productivity which leads to increase in income. In this way, slowly and gradually they can escape from this “vicious cycle” of poverty. There are now over 1600 major microfinance institutions working in a co-ordinate effort to reach 100 millions of the world’s poorest households with access to capital by the year 2008. Reports from 1065 of these institutions reveal that there are now at least 23.5 million households served by microfinance institutions world-wide, including 18.4 million in Asia, 3.8million in Africa, and 1.1 million in Latin America (Microcredit Summit 2000).

Financial institutions can extend loans to the poor while, at the same time, making a reasonable profit, by charging high interest rates. Microfinance institutions can afford the high transaction costs of processing large volumes of loans as small as a few dollars. The idea that the free market can help break debt cycles and foster income-generating market activities within poor communities did not gain acceptance until the establishment of the Grameen Bank. Traditionally, several major obstacles have denied poor people access to credit, such as lack of collateral. Also, no standard existed to affirm that financial institutions could benefit from bearing the administrative costs and the risks of loaning to the poor. Over the past decade or so, however, an institution such as Grameen Bank have proven that credit must be extended in large quantities in order to be profitable is false. Grameen Bank and others have given loans to “solidarity groups” of about five people, using the opportunity for everyone in the group to secure future credit as collateral, with peer pressure as an additional incentive. By charging market interest rates or higher interest rate than market interest rates, these institutions are able to cover their administrative costs, and most institutions enjoy repayment rates that are higher than that of traditional commercial banks. Group lending programs such as the Grameen Bank affect the behavior of the

poor both by altering economic incentives through the provision of credit and by providing social development inputs intended to influence behaviors.

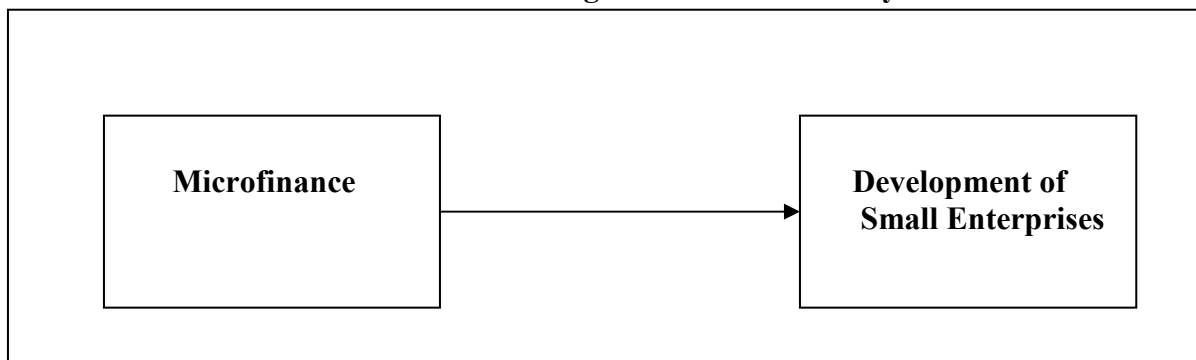
Micro credit programs have brought about desirable impact at different level in terms of income, employment, and production, especially in the non-farm sector, e.g. program placement of Grameen Bank, Bangladesh Rural Advancement Committee (BRAC), and RD-12 increased average household income of the poor. Grameen Bank and other programs have managed only to increase employment and production in rural non-farm activities where technology is traditional. Micro credit programs are increasingly sought as a way to enhance the income and employment of the poor who can be self-employed in a variety of informal activities (Hulme; Mosley 1996). 90 million Pakistani people live in rural areas out of 140 Million where there are few opportunities for employment other than self-employment. Access to credit for the rural poor is typically limited to local moneylenders who can charge in excess of 350% per annum. There are thousands of stories where poor households facing extreme financial distress, have resorted to borrowing money at such exorbitant rates. Research has revealed that a majority of such transactions are based on life cycle needs of poor households like marriage expenses or healthcare requirements, rather than for productive purposes. Productive credit to the poor is therefore an anomaly and a rough estimate of the coverage of microfinance in Pakistan reveals that only 5% of the households requiring access are actually covered by institutional credit.

Pakistan is the seventh most populous country in the world. Eighty percent of Pakistan's 145 million people live on less than \$2 per day. In per capita terms, Pakistan's production and income levels are less than half of those of Indonesia and the Philippines. After experiencing three decades of relative and somewhat impressive decline in poverty, in the 1990s poverty increased in Pakistan, both in relative and in absolute terms. Between 1993 and 1999 12 million people were added to those living on \$1 a day or less, and overall poverty statistics reveal that poverty has increased from 17% in 1987 to 34% in 1999 (Pakistan Micro Finance Network November 10th, 2002). Gender disaggregated analysis on poverty is not widely available; however, existing evidence strongly suggests greater exposure to poverty for women.

2. Theoretical Framework

There are two main factors that are affected by the micro credit in development of the small enterprise i.e economic development and social development. We have operationally defined the dimension and found out that the dimensions can be assessed by finding out the changes in the income, business assets, associated employment, social networks, and empowerment of women, skills of the entrepreneur, education, health awareness, and social mobility after utilization of micro credit. Microfinance is considered as an independent and small enterprises development as a dependent variable as showed in the study model".

Figure 1: Model of Study



The model shows that when micro credit is provided to the poor, they can improve their current businesses and start up new activities; this will help in development of the small enterprise.

2.1 Independent Variable

Tero (1990) illustrates the various ways in which “microfinance, at its core, combats poverty”. She states that “*Microfinance* creates access to productive capital (amount of money) for the poor, which together with human capital, addressed through education and training, and social capital, achieved through local organization building, enables people to move out of poverty” By providing material capital to a poor person, their sense of dignity is strengthened and this can help to empower the person to participate in the economy and society.

2.2 Dependent Variables

The dependent variable in this study is the impact on the *development of small enterprises*. This can be assessed through the increase in income, inventory level, sales volume and increase in associated employment of the enterprises.

2.3 Hypotheses

The testable statement is:

H₀: Micro-credit has impact on development of Small Scale Enterprises.

H_A: Micro-credit does not have impact on the development of Small Scale Enterprises.

3. OPERATIONALIZATION OF RESEARCH PROCESS

It is not possible to directly assess the impact of micro credit on the development of small enterprises .The impact can be seen through the following two dimensions:

- Economic development
- Social development.

3.1 Economic Impact

There are many economic factors that influence the development of small enterprises. In this study, change in *Income*, change in *Inventory Level*, improvement in *Business Assets*, and *Associated Employment*, are the factors that can easily be assessed and interpreted to find the economic impact of microfinance on the development of small enterprises. Previous studies have shown that impact of microfinance on the enterprises can be seen through change in *Income*, *Inventory Level* and *Business Assets*. According to Littlefield, Murdoch and Hashemi (200) “ various studies documented increase in income and assets, and decreases in vulnerability of microfinance clients”. They referred the projects in India, Indonesia, Zimbabwe, Bangladesh and Uganda which all showed impacts of microfinance in reducing poverty.

3. Social impact

Traditionally, the impact of microfinance projects was assessed by the changes in the income or well being of the clients. Mansell-Carstens, cited in Rogaly, argued that such a focus is flawed because respondents may give false information. It is also very difficult to ascertain all the sources of income of a client, so a causal effect is difficult to establish, and it is also difficult to establish what would have happened if the loan was not given.

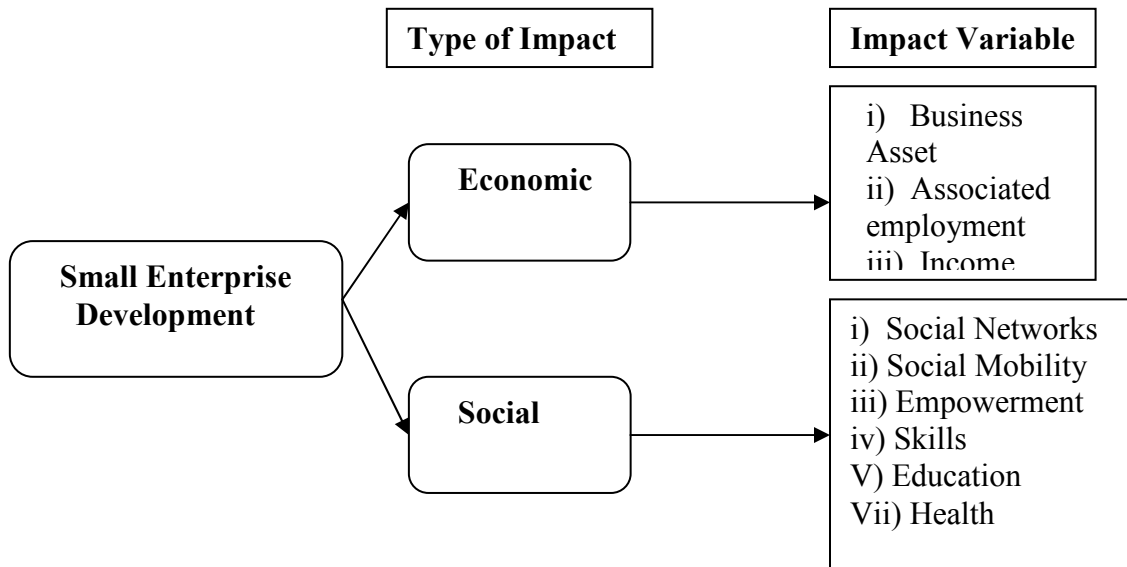
Therefore a broader analysis is needed that takes more than economic impact into consideration. The poverty and livelihood security consist of economic and social conditions, therefore, when analyzing the impact of microfinance, social impact must be assessed. So, in this study we analyzed the social impacts of micro credit on the small enterprises. Wider social impact assessment is important for an organization's internal learning process, as Microfinance institutions should be aware of the "full range of changes associated with its efforts and uses these to improve its performance". We considered social impact to relate to human capital such as *Social Networks, Social Mobility, Empowerment of Women*, Impacts were assessed on each of these issues to find true picture of the impact of microfinance. Societies are comprised of different institutional domains each with their own rules, norms and practices which can be influenced by microfinance interventions in different ways; we have taken these three elements to show different ways that micro credit can influence the development of small enterprises. Zohir and Matin (2004) make a similar point when they state that the impact of microfinance interventions is being under-estimated by "conventional impact studies which do not take into account the possible positive externalities on spheres beyond households." They propose that impact should be examined from cultural, economic, social and political domains at individual, enterprise and household levels.

Empowerment refers to the "process by which those who have been denied the ability to make strategic life choices acquire such an ability", where strategic choices are "critical for people to live the lives they want (such as choice of livelihood, whether and who to marry, whether to have children, etc)". Microfinance institutions cannot empower women directly but can help them through training and awareness-raising to challenge the existing norms, cultures and values which place them at a disadvantage in relation to men, and to help them have greater control over resources and their lives". A key objective of many microfinance interventions is to *Empower Women*. When women are empowered, they can use the resources independently and can start income generating activities and can lift up their lives. We have analyzed how micro credit can influence lives and status of women. Kabeer, Littlefield, Murdugh and Hashemi state that access to microfinance institutions can empower women to become more confident, more assertive, more likely to take part in family and community decisions and better able to confront gender inequities. Chowdhury and Bhuiya state that microfinance projects can reduce the isolation of women as when they come together in groups they have an opportunity to share information and discuss ideas and develop a bond that wasn't there previously. From studies of the Grameen Bank and BRAC, they observe that clients of these programs suffered from significantly fewer beatings from their husbands they did before they joined the MFI.

These are the reasons that we have chosen the empowerment of women as key factor for the development and improvement of enterprises in poor society, which has an ultimate impact on their social life. From a social perspective, reduced migration increases family cohesion and greatly contributes towards improving child-upbringing. Zohir and Matin (2004) notes that the interaction within MFI groups can create co-operation and trust that not only facilitates the microfinance activities, but also contributes benefits beyond the service provided, such as a greater sense of community, *Social Networks* and *Social mobility* trust and reliance on the group in times of crisis. These networks can lay the foundations for other social capital developments in the community. They state that examples of cultural impacts of social intermediation that affect the greater community could be a change in attitude of society towards the acceptable age of women's marriage, domestic violence, dowry, etc. Therefore, impact of microfinance projects should not just focus on the individual and household levels if the true impact is to be assessed. Microfinance can have a far wider impact than the

household level, as shown in Figure 2, and this must be assessed if a true representation of microfinance projects as studied by Eion Wrenn, “potential impacts of microfinance on Poverty.”

Figure 2: Operationalization of concept



4. RESEARCH DESIGN

This research study is descriptive in nature. The characteristics of variables and their relationship are defined in previous section. Hypotheses were formulated on the basis of relationship between two main variables (micro credit and enterprise development). Researches have shown that there is positive relationship between micro credit and the development of small enterprises. This research is based on hypotheses which were tested to find if there were positive relationship between microfinance and development of small enterprises. The Study was conducted in the provincial capital city Quetta of Baluchistan Pakistan to see the impact of micro-credit on small scale enterprises.

4.1 Type of Investigation

The purpose of our research was to find out if there is relation between variables, the type of investigation we have chosen is percentage.

4.2 Extent of Researcher Interference with the Study

The primary data was collected by observations, interviews etc. The data was collected in natural environment and the interference was minimal.

4.3 Study Setting

The research was conducted in natural environment where work proceeds normally (that is, in non-contrived settings). The study was based on Field Experiment where all activities were occurring in natural work environment.

4.4 Unit of Analysis

In this study, individuals were studied separately. I studied the behavior of individuals towards the development of small enterprises, and through questionnaire found their judgment and views about microfinance and enterprise development relationship.

4.5 Time Horizon:

Time horizon was cross-sectional. We collected data once, collection duration were 3-days and from each individual data is gathered through interviews and also by personal observation.

5. METHODOLOGY

5.1 Sampling

In this study, the population comprises of micro-credit clients of **Khushhali Bank** in Quetta. Khushhali Bank's clients were limited in number so the Stratified random sampling was used. The reason for using random sampling is because every element in the population has a known and equal chance of being selected as a subject. Total 60 individuals were studied; 40 male and 20 female clients were selected, having different types of enterprises which include retail stores, service providers, and small manufacturing enterprises.

Before the data was collected, permission to conduct the preliminary interview and observations was obtained from the Regional Manager of Khushhali Bank. The purpose was to legitimize our presence in the organization. The data was collected in three ways. First, the preliminary data was collected by observation of clients, their businesses, and the number of employees working with them. Second, the data was gathered by interviewing selected clients. The information collected were about the current situation of clients, their perception about micro credit, their future planning, problems related to the process of getting micro credit and the benefits they think they can avail from micro credit facility. The third the data was collected through formal questionnaire.

5.2 Analysis

The responses were analyzed by using Microsoft Excel. The primary data was analyzed through descriptive, percentage analysis and also with the help of pie charts form. The answers were examined to see if there is relationship among variables and what the magnitude of these relations is.

6. FINDINGS AND DISCUSSION

The basic theme of this research was to find out the role of microfinance in small enterprise development in urban parts of Quetta city; hence the sample was drawn from Quetta.

The study found that most of the enterprises in the research sample availing microfinance are operating since a period of 9 years average. All are rationally aware of their businesses and the surrounding market conditions. The sample of research included 48% owned and 52% rented business enterprises; 38% service, 39% retail and 23 % manufacturing enterprises. The sample average loan amount was Rs12568 and average time period since the loan was acquired was 7.5 months. Analysis shows that 55% enterprises use the loan for expanding their businesses, 35% to start-up a new activity by utilizing the loan and only 10% diversify their products. Thus, it's observed that microfinance plays an important role in the expansion of businesses. ***Therefore, it supports our null hypothesis that microfinance is contributing in the enterprise development.***

Study also found that 81% of sample showed that the sales volume of the enterprises improved after the loan utilization, 2% showed decline in their sales volume while 17 % showed no change. It should be noted that cases of decline or no change in sales volume belong to those businesses which suffer from seasonal fluctuations as the market of Quetta slacks down for 3 to 4 months in winter season; so this might be the case with the enterprises showing decline or no change in sales volume. It was also found that the increase in the income of male respondents was 28% whereas female respondents were 37%. Thus it supports the argument that female respondents utilize the loans more efficiently than the male respondents. ***In short microfinance helps to increase the income of enterprises.*** To conclude, the majority of the respondents give acclaim to microfinance for increase in their income.

For the reasons behind indifference of enterprise businesses in this regard, 48% respondents believed that the current business conditions (slack season of Quetta, for instance) are the main reasons that cause no improvement in their businesses, 23% observed that the small amount of loans is a cause for no improvement, while 29% replied that the installment size of the loan is the main reason. The study found that most of the respondents are not satisfied with the current amount of loan; they sought an average of Rs.35000-40000. They are quiet sure that if banks provide the aforementioned amount of loans then they can improve their businesses significantly.

For the increase in associated to employment of the enterprises it was found that only 17% of the respondents told that the number of employees increased in their businesses after microfinance utilization. While 73% denied any change in their associated employment. So we can say that microfinance is not helping in generating employment opportunities for the unemployed people.

For the microfinance impacts on living standards of the borrowers here it was found that the respondents do not realize an improvement in their living standards. To add, respondents expressed their willingness to reinvest their increased proportion of income in their businesses rather than consuming it for the luxury. In short, study observed that microfinance is not contributing in improving the living standards of the people.

7. CONCLUSION

Although the importance of small enterprise for economic growth and innovation is widely recognized in all types of economies—developed, developing, and transitional—there has been relatively little research into microfinance role in the stimulate the growth of small enterprises. This research project had three important related goals. The first was to explore the implications for the enterprise choice of activity and demand for capital (microfinance). The second goal was to investigate role of microfinance to nurture enterprise development in the Quetta city and the third goal was to find out the impacts of microfinance on women empowerment, associated employment and living standards of the borrowers. Studies of managerial opinions concerning the obstacles faced by these small enterprises are useful and suggestive, but we believe that there is a need for careful quantitative studies to analyze the statistical relationship between small enterprise growth and objective measures of microfinance factors related to their development. We have attempted to find out the possible relationship between the microfinance and small enterprises' development in the Quetta city and the obstacles that cause no significance development in the small enterprises by the microfinance. Here, we

summarize the conclusions from analysis of these data and personal interviews with the borrowers, and we also discuss factors that are important in interpreting our work and that suggest how future research may proceed. The results provide strong evidence that loans are an important factor in stimulating the growth of small enterprise in Quetta. Internal finance also promotes growth, but microfinance appears to be relatively more important for their growth because small enterprise maintain very small amount in their savings and they need some portion from credit (microfinance) to improve their businesses. The data showed that small enterprises mostly use microfinance to purchase some more productive assets and inventory but the amount provided by the microfinance institutions is not sufficient for the significant development in the small enterprises businesses.

Data showed that the microfinance contributes in the income generation but does not help much in the increase of associated employment for the small enterprises of Quetta city. The data revealed that the income of manufacturing enterprise increases more than the retail and service enterprises by utilizing microfinance. We may conclude from this evidence that microfinance helps manufacturing small enterprise more than the retail and service enterprises. Furthermore, we have also learnt that if a manufacturing small enterprise develops it also create opportunities for associated employment.

The Microfinance helps in women empowerment by providing them social mobility and the opportunities to interact with the business related persons that boost their confidence as well as their managerial skills. It provides them opportunities to contribute in the local economy by producing the goods that have demand in the local market such as handicrafts and home made items. They also learn how to utilize credit efficiently and manage their businesses which helps in making a female entrepreneurship network in the society.

The microfinance and living standards relationship in many researches seems positive but we observed that there is no significant impact of microfinance on living standards. From the data and personal interviews, we came to know that rise in inflation rate is the main factor that does not support the above mention relation, the other factor being the minor amount of loan provided to them. Many of the small enterprises started-up a new activity but left it because of increase in inflation rate. If the inflation rate is controlled and the amount of loan is increased then a positive relationship between microfinance and the living standards may prevail. The small enterprise development through microfinance can help in improving living standards and education level in the Quetta but requires longer time period because of high rate of inflation and the low amount of loans. So we conclude that increase in the loan amount and a stable inflation rate shortens this time period and hence helps in improving the living standards of the small enterprises.

8. Suggestions and Recommendations

By analyzing the research data and the small enterprises' business environment, the study recommends that:

- The amount of microfinance should be at least Rs.50, 000 to 60,000 for the small enterprises.
- The government should try to maintain a stable inflation rate that should be friendly enough with the small enterprises' business activities; and the Microfinance Institutes (MFIs) should also increase the minimum amount of loans with the passage of time, adjusting with the inflation rate.
- The Microfinance Institutes (MFIs) should focus on the enterprise development rather than to increase their customers; by providing a sufficient amount of loan to few small enterprises is better than providing very low amount of loans to many small enterprises.

- The associated employees of an enterprise, who can manage business activities independently, should be provided with microfinance in order to develop them as new entrepreneurs; this will help to establish a network of entrepreneurs in the market.
- The installment size of the loans should be flexible considering different types of borrowers; because of same installment size, many small enterprises cannot develop.
- The Microfinance Institutes (MFIs) should provide loans to those enterprises which have the potential to grow rather than providing loans to those enterprises which have showed stagnant growth rate.
- The microfinance Institutes (MFIs) should also provide saving account facilities to their customers which help them in their contingency planning

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Appendix A**Khushhali Bank information and data for Quetta**

Mission statement “To strengthen the economic base of low income population across Pakistan by improving their accessibility to financial services, By backing a diverse product suite with exemplary customer services, and by combining cost efficiency with next –generation delivery system, we intend to achieve our core objective of attaining operational and financial self efficiency.”

Total customers

Active= 3756

Accumulated=8938

Total loan=11641

Total disbursement (since inception) = Rs115296400

26 Nov, 2001 inaugurated in Quetta

Cumulative recovery rate= 97%

All Pakistan Branches/CS=110

Balochistan branches = 7

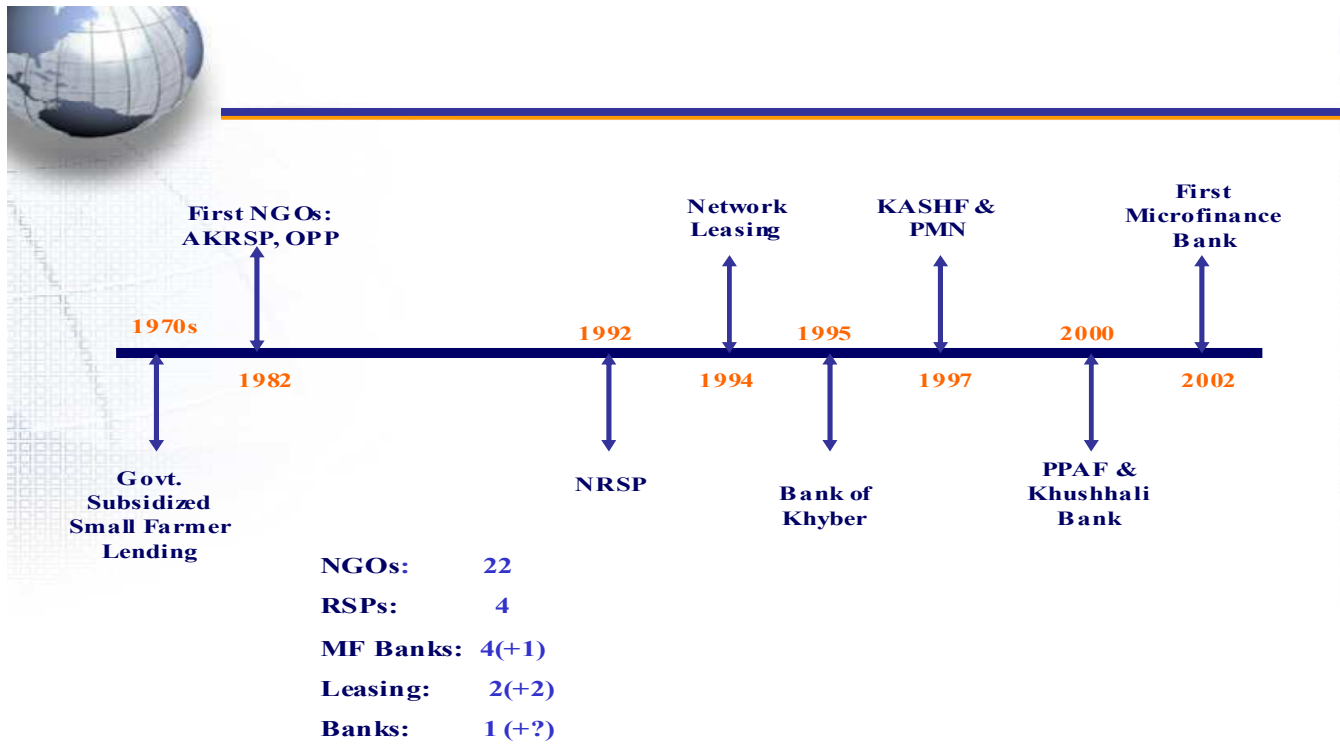
Customer Services= 4 only in Quetta

Male	Female	Total
6612	5029	11641
57%	43%	100%

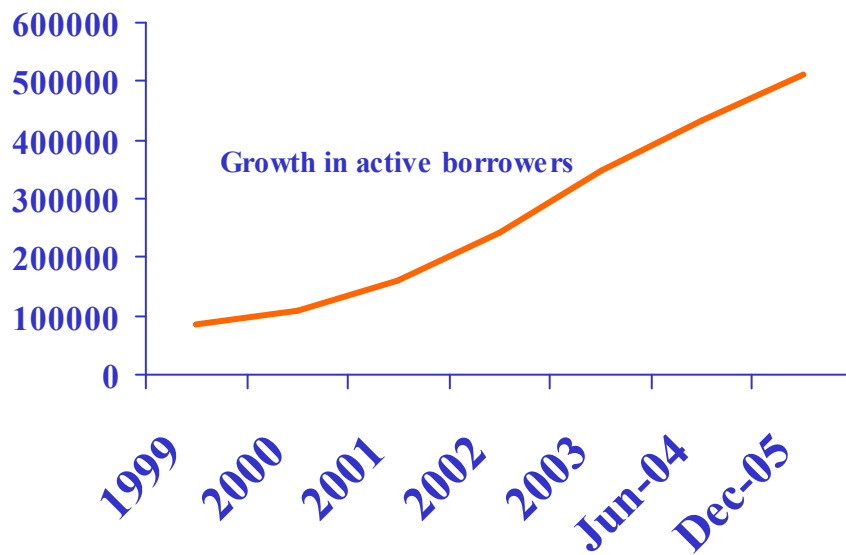
No of CSOs deployed	SC name/Urban	Tehsil	Date of intervention	Potential number of clients	Benchmark per CSO	Total		Current	
						No	Rs	No	Rs
1	Nawa killi	Quetta	7/1/2004	1200	620	681	6890873	189	1642274
1	Rehmat colony	Quetta	6/1/2004	1200	620	953	10293663	56	420135
1	Satellite Town	Quetta	7/1/2004	1200	620	534	5851253	137	906515
1	Lal colony	Quetta	6/1/2004	1500	620	970	10593602	217	1505566
1	Hudda	Quetta	1/1/2002	1800	620	1538	16937072	241	2057003
1	Saryab	Quetta	6/1/2004	800	620	470	4725681	15	138836
1	Hazara town	Quetta	1/1/2004	1500	620	1255	13898851	314	2341728
1	Killi deba	Quetta	1/1/2002	2000	620	1486	15970691	234	1702425
1	Momin abad	Quetta	11/1/2002	2300	620	2070	24687317	318	2079869
1	Shaldara	Quetta	2/1/2002	1700	620	1164	13041861	156	1154051

Appendix B

Micro finance history in Pakistan

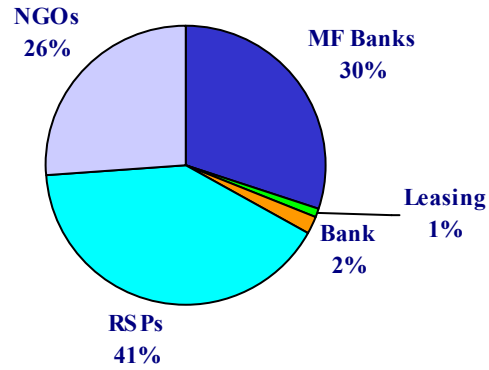
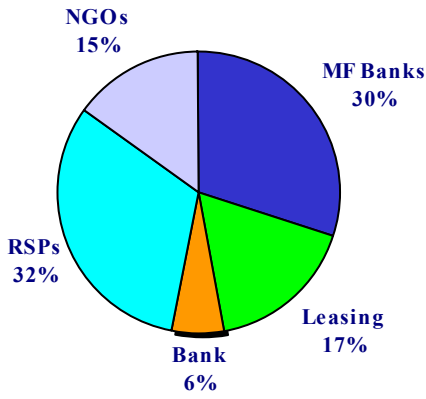


Outreach of Micro finance in Pakistan



Gross loan portfolio Rs 5 billion

Active Borrowers 510000



**Penetration:
% of Poor Families**

