European Journal of Business and Management
ISSN 2222-1905 (Paper) ISSN 2222-2839 (Online)
Vol 4, No.21, 2012
www.iiste.org

Impact of Microfinance Banks on Poverty Alleviation in Selected Local Government Areas of Oyo State, Nigeria

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Abstract

The study examined the impact of microfinance banks on poverty alleviation in selected Local Government Areas of Oyo State. Standard of living of the respondents was examined; relationship between size of loans and standard of living and the extent to which women has benefitted from microfinance bank activities were also evaluated. The study was carried out in three Local Government Areas which were selected using stratified and purposive sampling techniques. 150 customers of microfinance banks were selected. Primary data were analyzed using Foster Greer Thorbecke; Matching Framework Analysis and Partial Correlation. The results revealed that poverty index of the respondents reduced from 0.1668 to 0.1551 after collection of loans which implied that microfinance banks has impacted positively on their living standards. The extent at which women has benefitted from microfinance banks ranges from 65% to 74% between 2007 and 2010. The result indicated that women are increasingly benefitting from microfinance activities in contrast to yester years when there was gender disparity skewed against women. Moreover, the relationship between size of loan, asset acquisition and profit after loan were positive and significant with P = 0.085 and r = 0.152, this revealed that as the size of loan increases, asset acquisition and profit also increases. It was recommended that the size of loans given to customers should be increased in order to enhance their standard of living and consequently alleviate poverty. Microfinance banks should encourage formation of cooperative societies through which they can give out loans to customers.

Keywords: Microfinance bank, Poverty, Living standard, Nigeria

1. Introduction

The word "micro" literally means small and finance also mean investment or support, therefore microfinance can be defined literally as small investment or support. Microfinance can be defined as the practice of offering small, collateral free loans to member of co-operatives who otherwise would not have access to the capital necessary to begin small business or other income generating activities. Littlefield, Morduch and Hashemi (2002) said that increase access to credit reduces poverty. According to Sirajul (2007) the poorest of the world form the vast majority of those without access to health, basic education and majority of those without access to microfinance as well.

The concept of microfinance bank is not new, savings and credit groups that have operated for centuries include the "Susus" of Ghana, Chit funds in India, "Landas" in Mexico, "Arisan" in Indonesia, "Ajo', "Esusu" in Nigeria, "Cheelu" in Sri Lanka, Tontines in West Africa and "Pasanaku" in Bolivia, as well as numerous saving clubs and burial societies found all over the world (Yahaya *et al*., 2010). Microfinance is about providing financial services to the poor who are not served by the conventional financial institutions. This indicated that people live in poverty when they are denied an income sufficient for their material needs and when these circumstances exclude them from taking part in activities which are accepted part of daily life in that society.

In Nigeria poverty is pervasive with frightening depth and breath. It affects all geopolitical zones of the country. The poor in Nigeria like those elsewhere are powerless, voiceless, lack basics of live and are generally deprive. Poor people have insufficient income, lack access to basic services, have limited access to credit and shelter, they survive on menial jobs and can barely afford to send their children to school Adeola (2000) Bamisile (2006) reported that despite apparent success of microfinance bank and the efforts of supply led policies and financial liberation, there are still' "important" gaps to be filled by this institutions in Nigeria. Anyanwu (2004) observed that microfinance bank have not been able to adequately address the gap in terms of credits, savings and other financial services required by the poor. Due to inconsistencies in these reports, the study seeks to address the following questions.

1.2 *Objectives of the study*

The general objective of the study is to determine the impact of microfinance on poverty alleviation in Oyo State. The specific objectives are to:

1. Examine the impact of microfinance bank on the standard of living of the people in the selected local government areas of Oyo State
2. Ascertain the extent to which women has benefited in the microfinance activities in selected local government of Oyo State.
3. Determine the relationship between size of loan and standard of living.

1.3 *Hypotheses of the study*

The following hypotheses were tested:

Ho_1: There is no significant relationship between microfinance bank activities and standard of living of people in the selected local government areas of Oyo State.

Ho_2: Women have not benefited from microfinance bank in the selected local government areas of Oyo States.

Ho_3: There is no significant relationship between size of loan acquired and standard of living/asset acquisition

2. Theoretical Framework

A country suffering from abject poverty is described as underdeveloped, having developing economy or third world country. The attributes of third world countries are manifested in poor nutrition, poor or inadequate shelter, poor health facilities, low life expectancy as well as poor infrastructure, majority of her active citizen are living in poverty (Adewole, 2008). Poverty in the developing nation hinders economic and social progress several policies implemented since the end of Second World War has been largely unsuccessful at battling global poverty. Many researchers, development workers and institution haul microfinance as a potential solution to alleviation of poverty (Yunus, 2004).

On the other hand, according to the World Bank Organization, "the most commonly used way to measure poverty is based on income. A person is considered poor if his or her income level falls below some minimum level necessary to meet basic needs. This minimum level is usually called the 'poverty line." What is necessary to satisfy basic needs varies across time and societies. Therefore, poverty lines vary in time and place and each country uses lines which are appropriate to its level of development, societal norms and values.

However, Bentu (2008) citing Khawari (2004) states that the point is not the irrelevance of economic variables such as personal incomes, but their severe inadequacy in measuring many of the casual influences on the quality of life and survival chances of people. It is possible to infer from this that an inadequate or inconsistent income level generates poverty; hereby depriving people of some basic human needs (Khawari, 2004).

World Bank standard quoted in United Nations Capital Development Fund (2004) report poor people are those earning between ₦160 and ₦320 per day, that is, people earning between $1 and $2 per day. The very poor are those earning below ₦160 per day.

The problem of poverty and the recognition of the government to the need to encourage the poor and small enterprises through the provision of credit brought about policy reform with respect to replacing formal community banks with microfinance bank in Nigeria and bringing the micro finance institution under the control of the Central Bank of Nigerian and the policy became operational in 2005.

2.1 *Justification for the Establishment of Microfinance Banks*

According to Central Bank of Nigeria (2005), justification for the establishment of microfinance bank includes weak institution capacity, that is the prolonged sub–optimal performance of many existing community banks. The existence of a huge un-served market**,** the size of the unsaved market by existing financial institutions is large. The average banking density in Nigeria is one financial institution outlet to 32,700 inhabitants. In the rural areas, it is 1:57,000 that is less than 2% of rural households have access to financial services. Utilization of SMEEIS Fund: As at December, 2004 only ₦8.5 billion (29.5%) of the ₦28.8 billion Small and Medium Enterprises Equity Investment Scheme (SMEEIS) fund had been utilized.

2.2. *Target and Goals of Microfinance Banks*

The target of microfinance banks include but not limited to:

1. To cover the majority of the poor but economically active population by 2020 thereby creating millions of jobs and reducing poverty.
2. To eliminate gender disparity by improving women's access to financial services by 5% annually; and
3. To increase the number of linkages among universal banks, development banks, specialized finance institutions and microfinance banks by 10% annually (CBN, 2005).

The goals are to:

1. Provide diversified, affordable and dependable financial services to the active poor, in a timely and competitive manner that would enable them to undertake and develop long-term, sustainable entrepreneurial activities;
2. Mobilize savings for intermediation;
3. Create employment opportunities and increase the productivity of the active poor in the country, thereby increasing their individual household income and uplifting their standard of living.

2.2.1 ***The Grameen Bank***

The Grameen Bank is a microfinance institution that supplies loans to the most poor and destitute villagers in rural Bangladesh (Armendariz de Aghion & Morduch, (2005). Grameen Bank microfinance is based upon the Baker-Hopkins Credit Model, which indicates that as long as the return on assets is larger than the rate of interest paid on loans, credit (will) increase the income of the household that receives the loan. The larger the share of loan to capital the higher the growth of household income (Wahid, 1994).

Generally, to be eligible for bank credit, asset based collateral must be provided. This has made bank credits unreachable to the poor, in order to make credits available to the poor in rural Bangladesh, a new credit system of collateral free lending was introduced (Yumus, 2003). The Baker-Hopkins Model gives the theoretical underpinnings to ensure credit repayments. Thus, in order to guarantee the timely recovery of credits, Grameen Bank add a "peer monitoring" system to the Baker-Hopkins credit equation and thus, completes its theoretical construct.

Under this system, if the recipients take loans in groups and agree to monitor the activities of one another, then the recovery rate may improve substantially (Wahid, 1994). Yunus (2003) asserted that the need for collateral to qualify for a loan prohibited the poor from participating in the banking sector; he said collateral makes it such that only the rich individual can borrow.

Usually, it is very difficult for the destitute to repay loans in a lump-sum, so the Grameen Bank Model allows patrons to repay their loans on a gradual installment basis; since the impoverished generally do not have access to collateral for loans.

The Grameen Bank developed a model to offer a guarantee for person lacking traditional collateral - "Grameen style" through group lending (Armendariz de Aghion and Morduch, 2005). With this model, poor villagers form groups of five, known as solidarity groups. These group members become social capital for one another. As such, the bank grants loans to two people from each solidarity group. Provided that these two individuals repay their loans on time over a designated probation period (approximately six weeks), two more group members become eligible for loans.

2.2.2. *Women and Micro Finance Bank in Nigeria*

Nigeria is the seventh world largest exporter of oil, yet ranks 158 out of the 188 countries of the world in terms of quality of life (UNDP, 2007). Out of these numbers of poor Nigerian, women represent greater proportion due largely to their ascribed and acquired role, for instance about 65 percent of active population, most of them women have been excluded from the formal financial institutions (Bamisile, 2006).

The increased focus on gender and development debate has been an important development of the last three decades. The Millennium Development Goal 3, which is the Promotion of Gender Equality and Empowerment of Women is recognized not only as a goal in itself but also as an essential step for achieving all other goals Yeshiareg (2009).. According to UNECA (2005) cited in Yeshiareg (2009), one of the reasons why Africa is off track in terms of meeting the Millennium Development Goals targets, includes persistent gender inequality and discrimination. The current challenge facing the continent (Africa) and Nigeria in particular is how to achieve a reversal of inequalities. the emergence of microfinance banks was largely aggravated by the exclusion of the informal sector by the former financial system in Nigeria and indeed order developing countries.

2.2.3 *Microfinance and Standard of Living*

Income is one of the important elements of living standards of the poor people as well as saving Mohammad and Mohammed (2007). The microfinance banks are to provide loans to the poor not only to increase their income but also to mobilize their saving and CBN, (2005). Apart from these, other factors that contribute to human development, like education, empowerment can also be included as variables indicating a level of standard of living. This study therefore went out to determine if the standard of living of customers of microfinance bank has improved in the selected Local Governments of Oyo State since they joined the microfinance program. Microfinance programs target both economic and social poverty (Ghalib 2007).

To assess the success of microfinance bank there is a need to measure the impact on borrowers, which in this study are the customers of microfinance bank in the three selected Local Governments. Mohammed and Mohammad (2007) concluded that improvement in standard of living is positively affected by better access to education, healthcare, financial situation, that is increases in income and savings, which are also affected by level of interest.

2.3. Conceptual Framework

The review of literature points to several specific conclusions about the impact of microfinance bank on poverty alleviation. Evidence showed the positive impact of microfinance on poverty alleviation as it relates to the first six out of seven Millennium Development Goals. There is an overwhelming amount of evidence substantiating a beneficial effect of microfinance bank on increase in income recorded by various researches (Wright 2000; UNICEF 1997; Khandker 1998, 2001) and reduction in vulnerability in some studies (Mcculloch and Baulch 2000; Wright 2000 and Zaman 2000).

Despite the disagreement on specific definitions of levels of poverty, there is a general consensus among the experts that microfinance bank is not for everyone. Various studies show that borrowing patterns and inclination to save are the same across clients of different levels of poverty (Zaman, 2000). But many of the microfinance bank exclude the poorest, reason can be easily understood by studying the financial performance of microfinance banks targeted to the poorest clients and to those of microfinance bank that do not reach the poorest (Gibbons and Jennifer 2000; Churchill 2000).

Central Bank of Nigeria (2005) in its microfinance policy regulation and supervisory framework highlighted as one of microfinance's targets, the coverage of the majority of poor but economically active population thereby creating millions of jobs and reducing poverty. The CBN (2005) also stated as part of the objectives of microfinance bank, enhancement of service to micro enterprises and mobilization of savings.

This research work examined the impact of microfinance bank on poverty alleviation by examining the impact of microfinance bank on standard of living of people, verified the extent to which women have benefited in microfinance bank and the relationship between size of loan and standard of living in the selected Local Government Areas as shown in figure 1 below:

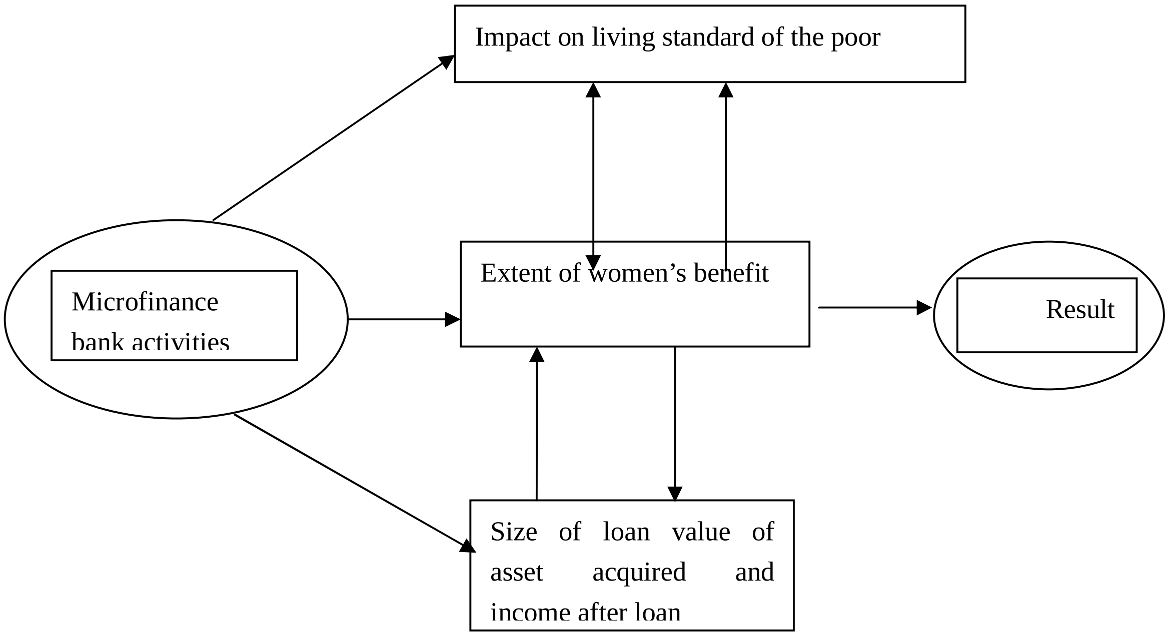

Fig. 1: Relationship between Loan size and Standard of Living

Source: Adapted from Mohammed and Mohammed (2007) Impact of microfinance banks on living standards, empowerment and poverty alleviation of poor people,

3. Research Methods

Three Local Government Areas were selected in Oyo State namely Orire Local Government, Surulere Local Government and Iddo Local Government. The Local Governments which were all rural areas were chosen one per each Senatorial District using purposive sampling. This is because studies showed that poor people in Nigeria lack access to credit facilities and mostly live in rural areas (Adeola 2000). Primary data collection instrument was employed. Data was collected through structured questionnaire that was administered to the microfinance bank clients for at least 3 years while secondary data were sourced from the records of the microfinance banks through administration of in the selected Local Government Areas.

Table 1. Measurement of variables and analysis of objectives

S/N	Objectives	Data Required	Sources	Analytical Tools
1.	To examine the impact of microfinance bank on standard of living.	Income before loan, income after loan, sex, educational level, poverty gap, head count of the poor before and after collection of loan	Customers of microfinance bank for at least three years	Foster Greer-Thorbecke Poverty Index
2.	To determine the extent of women beneficiary from microfinance bank operations.	Number of women beneficiary from total respondents and total number of male, female client that enjoyed credit facility between 2007 and 2010	Women respondents from the total respondents. Sex of clients given loams to between 2007 and 2010.	Frequency table, Percentage and Matching Frame Work Analysis
3.	To establish the relationship between size of loan and standard of living	The size of loan in Naira and asset acquisition in Naira and income after collection of loan	Size of loan obtained by respondents and asset acquisition in Naira - income after collection of loan (2010)	Partial Correlation

Source: Field-Work (2011)

4. Results and Discussion

In order to achieve objective one of the study, which was to examine the impact of microfinance bank on standard of living? Foster-Greer-Thorbecke (1988) was used to measure poverty index.

Table 2: Poverty Measurement before and after collection of loan using Foster Greer-Thorbecke Formula

	P_0	P_1	P_2
Before	0.0076	0.1668	0.0562
After	0.0076	0.1551	0.0503

Source: Field work, 2011, Where P is poverty index, is a non-negative parameter, which took the value 0, 1 and 2 and indicates the head count ratio, poverty gap and square poverty gap respectively.

$$FGT = \frac{1}{N}\sum_{i=1}^{H_1}\left(\frac{z - y_i}{z}\right)\alpha$$

and

$$FGT = \frac{1}{N}\sum_{i=1}^{H_2}\left(\frac{z - y_2}{z}\right)\alpha$$

Where: N= No of Respondents 131
H_1 = Head count of the poor before the loan
H_2 = Head count of the poor after the loan
y_1 = Income before loan
y_2 = Income after loan
Z = Poverty line using $1 per day = ₦160 × 365 = #58400

Table 3: Percentage of poor respondents before and after collection of loan

	H	Percentage
Before	88	67
After	78	60

Source: Field work, 2011

The tables above (2&3) showed Foster Greer-Thorbecke poverty index, using the international poverty line of $1 per day per person was adopted for this study. This translated to ₦58,400 per annum at the exchange rate of ₦160 per dollar that was the exchange rate ruling during the study, therefore any respondent whose income is below N58,400 is considered poor.

The result showed that the head count (H_1) is 67% (that is 88 respondents) were poor before collecting loan, while (H_2) the head count after collection of loan is 60% that is 78 respondents which showed a 8% reduction in people that are poor. This result is in consonance with UNDP (2004) publication that reported that about 70% of Nigerian lives below the international income poverty line of (₦160) per day. It was discovered that standard of living that is poverty reduced after collection of loan from 17% to 16% and severity from 6% to 5%. Hypothesis one was rejected and we concluded that there is significant relationship between standard of living and microfinance bank activities, The result from this study conformed with earlier researchers like Yunus (2003), Mohammad and Mohammed (2007); Yeshiareg (2009); Idowu and Salami (2010) Yahaya *et al.*, (2010), that reported that the microfinance bank credit has impact on standard of living.

3.1 *Extent to which women has benefited in microfinance bank activities*

To analyze objective two which is to determine the extent to which women have benefited in microfinance bank activities, the sex of the respondents as well as the total number of male, female clients that had enjoyed microfinance bank credit between 2007 and 2010 as given by the management of microfinance bank.

Table 4. Sex distribution of clients that obtained loan from microfinance bank in the selected Local Government Areas in Oyo State (2007 -2010)

	2007		2008		2009		2010	
SEX	**Freq**	**%**	**Freq**	**%**	**Freq**	**%**	**Freq**	**%**
Male	820	35	636	32	833	26	907	27
Female	1525	65	1378	68	2341	74	2512	73
Total	2345	100	2014	100	3174	100	3419	100

Source: Field Survey 2011.

The table above showed that majority of the beneficiaries of the credit were women, 65 percent men benefited in 2007, 54 percent in 2008, 74 percent in 2009 while 73 percent benefited in 2010.It showed a very good improvement in 2007 with 65 percent of women benefited in microfinance service compare with only 35 percent in 2006 while only 35 percent were men, in 2008 the women beneficiary was 54 percent, 74 percent in 2009 while it was 73 percent in 2010. This showed a positive and remarkable development in achieving target number four of the microfinance bank in 2008 to 2010.

3.1.2. Relationship between size of loan, Asset Acquisition and profit after loan (Standard of living)

Table 5. Partial Correlation between size of loan, income after loan and asset acquisition

Control Variables			**Size of Loan**	**Value of Asset Acquired**
Income after loan Loan	Size of loan	Correlation	1.000	.152
	Significant (2 -tailed)			.085
	Df		0	128
	Value of Asset Acquired	Correlation	152	1.000
	Significant (2-tailed)		.085	
	Df		128	0
Control Variables			**Size of Loan**	**Income After Loan**

Value of asset Acquired	Size of loan	Correlation	1.000	.396
	Significant (2-tailed)			.085
	Df		0	128
	Value of Asset Acquired	Correlation	.396	1.000
	Significant (2-tailed)		.000	•
	Df		128	0

Source: Field Work 2011

The study revealed that there is a positive and significant relationship between size of loan, asset acquisition and profit after tax. It showed that at 0.025 level of significance, for every increase by 1 unit of size of loan there will 1.52 unit increases in asset acquisition and 3.96 unit increase in profit after tax. Therefore the hypothesis which stated that there is no relationship between size of loan and standard of living is rejected consequently. There is positive impact of size of loan, on asset acquisition and profit of clients of microfinance bank.

4. Conclusion and Recommendations

Poverty is a global phenomenon, affecting almost half of the world population. Mallick (2007) reported that 96 percent of the world income goes to 40% of the population while the remaining 60 percent of the population lives on 4% of world income. One reason for poverty is that many people are derived access to financial market. A new alternative way of providing credit to people living in a vulnerable economic situation is microfinance service or operation (Yunus 2003). This study examined the impact of microfinance bank on poverty alleviation of people in selected Local Governments Areas of Oyo State.

There is significant impact of microfinance activities on improvement of standard of living. The study also showed that 73 percent of microfinance bank clients were women which positively correlated with findings of Yunus (2003); Mohammed and Mohammad (2007); Yahaya *et al*., (2010). It also showed that at 0.025 level of significance, for every increase by 1 unit of size of loan there will 1.52 unit increases in asset acquisition and 3.96 unit increases in income after loan. Therefore the hypothesis which stated that there is no relationship between size of loan and standard of living is rejected consequently. Based on the result, the following recommendations were made:

1. The regulatory body (Central Bank of Nigeria) of the microfinance bank should compel the microfinance bank to charge lower interest rate to make the loan more productive to the clients.
2. Federal Government should give out soft loan to the microfinance bank, so as to reduce cost of obtaining credit/fund that will be used for loan by microfinance bank clients.

3. The microfinance bank should encourage the formation of cooperatives with members in the similar business that can enjoy credit facility jointly to reduce operating cost which will also reduce interest rate.
4. The size of loan being given should be increased for income to increase this will in turn reduce poverty.

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