Financial Decision and Poverty: Examining the Financial Behavior of the Extreme Poor in Nigeria

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Abstract

The study examines the relationship between poverty and finance so as to ascertain if poverty has an impact on the quality of financial decision taken by the poor and financially vulnerable individuals. The study utilised a unique methodology (truncated regression) and applied a survey data to investigate the quality of loan usage among the extreme poor in Nigeria. We allowed for the inclusion of other policy relevant variables that may likely inform the direction of new generation poverty alleviation policies like gender, education and age of the individuals. We find that the extreme poor use more of the loans for other non-developmental issues like funeral and marriage celebrations than for productive and poverty alleviating ventures. However, the younger males engage more in this act than the females. Also, as the poor become more educated, they are able to use more of the loan for development-oriented investments like purchase of assets, building houses and even furthering their education. A major policy implication of this result is that loans should be directed towards younger individuals, and education should be a focal priority in selecting who to fund.

Keywords*:* Financial Decision, Poverty, Finance, Financial Behaviour.

Introduction

The relationship between finance and poverty has been a controversial one. While some authors consider the macro dimension to the debate (e.g. Beck, Demirguc-kunt and Levine, 2007; Guillaumont and Kpodar, 2008), others see an important role of the financial sector on poverty alleviation (Beck, Ayyagari and Hoseini, 2013). There is a long standing assumption that increased access to credit has a positive correlation with promotion of economic activities, suggesting that individuals who are able to access credit and other forms of financial support will most likely come out of the poverty trap. This has also been questioned with critics arguing that excessive interest rates charged by financial institutions on credits hold the poor back in poverty. Despite these controversies, this study seeks to determine whether the quality of the loan/credit utilization by the poor has an important role in the finance-poverty nexus.

It is a common assumption that the quality of financial decisions varies across the income quartile of individuals. For example, it is assumed that the rich will often make better and informed financial decisions – such as investments, asset acquisition, education, etc., than the poor individuals (Anuj, 2015). Some arguments to support this stance include: poverty - in itself - hurts the individuals' ability to make sound judgement about school, finances, and other life decisions (Derek, 2013). As documented in literature, sound judgement entails the ability to process information and make financial calculations (Agarwal and Mazumder, 2013), which suggest that poor individuals may just be disadvantaged. It is possible that apart from the myriad of problems that may inhibit positive outcomes from credit/loans for the poor, the behavioural conditions of the poor, in terms of their decisions on what to use the loan for, may be another important finding in this subject matter. We align with the argument of Beck, Ayyagari and Hoseini (2013)[1] to use country-level studies to explain individuals' quality of loan usage amongst the extreme poor. We also examine the extent to which capacity development, gender and age of the individuals may affect the usage of the loan.

Nigeria presents an interesting case, close to an ideal testing ground, to conduct our inquiry. Apart from poverty alleviation among the extreme poor dominating the Millennium Development Goals (MDGs), and resurfacing in the Sustainable Development Goals (SDG), Nigeria is seen as having a very huge population of extreme poor as well as a good number of palliatives aimed at improving fund flow to the poor and vulnerable groups. A recent publication by the World Bank on the attainment of the MDGs established that extreme poverty has been decreasing in all regions of the world with the exception of sub-Saharan Africa (SSA) (Caulderwood, 2015; World Bank, 2015) and Nigeria still has about 60% of its population living in absolute poverty[2] as at 2010, with almost 100 million people living on less than $1 a day (BBC, 2012).

As part of the indigenous effort to reduce this statistic, the Nigerian government, through the Central Bank of Nigeria (CBN) is campaigning for better access of the poor to financial support in the form of loans or credit. For instance, the initiative to ensure better bank breadth to reach rural communities (where the majority of the poor reside) and also setting up community banks and now micro-finance banks are important milestones in this regard. The essence of these strategies is to take financial services to the rural poor and low-income clients thereby promoting financial inclusion. The effect of this strategy is seen in the number of bank accounts per 1,000 adults which increased from 289 in 2007 to 507 in 2011 as well as the percentage increase in the proportion of private sector credit by deposit money banks and other financial institutions to GDP from 18.16% to 31.29% in the respective years. Nonetheless, in spite of these positive indices there has not been a clear evidence of transmission of positive impact of finance on poverty reduction in Nigeria. According to a 2008 survey, about 80% of Nigerians do not own bank accounts with financial institutions which make them financially excluded and lack access to finance (Faboyede, Ben-Caleb, Oyewo & Faboyede, 2015). The primary reasons are hardcore poverty and a low level of financial literacy (Credit Awareness Nigeria.com, 2013).

Theory predicts differently: bank accessibility and the provision of funds in the form of credit and microloans empowers the poor to be involved in productive activities and help to improve their income level (Beck, Demirgüç-Kunt and Levine, 2007; Awojobi and Bein, 2010). Also, access to finance helps to improve entrepreneurship among the extreme poor, and improves inter-state migration of workers (Beck, Ayyagari and Hoseini, 2013). Promoting financial literacy and credit awareness among Nigerians provides essential knowledge and financial responsibility to make informed decisions that will better lives and ultimately grow the economy (Faboyede, et al., 2015).

Our study extends the literature by focusing on a wider category of usage for which loans can be channeled by the extreme poor. We focus on the prevalence of the extreme poor in Nigeria accessing loans for purposes like “funeral/wedding”, “emergency/health”, “school fees”, “home construction”, and “home purchase”. We examined the usage effect of rural credit in the areas of education as well as the effect of human-specific factors as age and gender on taking decisions capable of improving the quality of life of the rural poor. These lines of enquiry are significant for the following reasons: First, to our knowledge, there are no evidence-based studies that address these issues, especially with special attention directed to developing countries of sub-Saharan Africa. Second, the choice of Nigeria was based on its relative economic, social and political importance in sub-Saharan Africa in particular and the African continent in general.

Apart from government’s intention to reduce the poverty rate and the role of financial institutions in making credit available to the poor, our study presents a critical view to the finance-poverty policies that may be applicable to other African countries. Knowing whether policies that aim at reducing poverty rate (by making credit available) could integrate the quality of the credit usage and other factors that may improve this outcome, would help to set a direction for a new generation of poverty reduction strategies for Nigeria and other African countries. This is even very important when considering the SDG regime.

The remainder of the study is organised as follows: the second section situates our paper in the light of relevant literature and theoretical explanations on how access to credit affects the poor. We proceed to present stylised facts in the third section on the rate of poverty and the development of the financial system in Nigeria, with emphasis given to credit provisions and other financial development indicators. An overview of the data used for the analysis and the econometric and methodological issues are presented in the fourth section. The fifth section discusses the empirical results, while the sixth section concludes and summarizes the findings from the study.

Conceptual and Theoretical Issues

The United Nations (1998) defines poverty as inability of getting choices and opportunities, a violation of human dignity, a lack of basic capacity to participate effectively in society, not having enough to feed and clothe a family, not having a school or clinic to go to, not having land on which to grow ones food or a job to earn a living, not having access to credit. According to the organization, poverty also means insecurity, powerlessness and exclusion of individuals, households and communities. It includes susceptibility to violence, and often implies living in marginal or fragile environments, without access to clean water and sanitation.

The World Bank (2000) defines poverty as deprivation in well-being and comprises many dimensions including low incomes and inability to acquire basic goods and services required for survival in dignity. It also encompasses low levels of health and education, poor access to clean water and sanitation, inadequate physical security, lack of voice and insufficient capacity and opportunity to better one’s life.

Within the context of this paper, finance is conceptualized as an economic resource and it refers to all means of settlements or payments for exchange transactions (Okafor, 2014). As an economic resource, Okafor explains that finance includes money and all money substitutes generally accepted as means of final settlements as well as credit.

Financial Decisions - Poverty Nexus

Financial decision is often a challenging activity for the both rich and the poor. However it is assumed to be a much more challenging activity for the poor partly because their will-power or self-control is easily run down. The poor are often poorly educated and are therefore more likely to make ill- informed, misguided or poor quality financial decisions thereby perpetuating themselves in poverty. This explains the high rate of diversion of funds, by the poor, to consumption and ceremonial expenses rather than investment and capacity building.

Methodology

In this study, the dependent variable is the measure of financial decision. We used the dichotomous measure of owning a bank account as a proxy for this variable. The choice for this being that this form of measure is the most referenced measure of financial decision that confront a wide range of individuals compared to other forms of proxy like taking credit from the bank. The responses range from 0 (do not have a bank account) to 1 (has a bank account).

The poverty variable was measured using relative poverty. This form of poverty is able to capture the extent of poverty in relation to each household of the individuals. The variable was captured using the responses to the following questions: in a year, how many times did you or any member of your household 1) lack enough food to eat 2) clean water for home 3) cash income at home. For robustness, we analyzed these three variables separately. The responses are 0=never, 1=just once or twice, 2=several times, 3=many times, 4=always.

Three covariates were included in our model in order to minimize any bias in our estimation through variable omission. The covariates that were selected were based on extant literature. The first covariate is the level of education of the individuals in determining their participation in financial decision. This variable was measured as the level of educational attainment, where responses range from 0 (no formal education) to 9 (post-graduate education). This variable was included because the educational attainment of individuals can inform their value judgement with regards to their involvement in opening bank account.

The other covariates that are included in the model are the age and gender of the individual. In summary, the regression model is as follows:

$$financial\ decision_i = \hat{a}_1 + \hat{a}_2 poverty_i + \hat{a}_3 X_i + \mu_i$$

Where the individual identifier is *'i'*, X_i denotes the sets of covariates included in the model and the error term is represented as $\mu_{i.}$ The logistic regression was used to estimate equation. Further, we estimated the marginal effect of the logistic regression in order to underscore the relative effect of a change in the financial decision variable as a result of a change in the value of the explanatory variables.

We accessed survey data from the *Afrobarometer* dataset. This dataset comprises of comprehensive household survey for some African countries in relation to institutional development, among others. The data include responses from the survey of about 2400 individuals. To highlight the authenticity of this data source, we list some studies that have patronised the dataset. They include Justesen (2011), who studied AIDs and poverty in Africa and Justesen and Bjorrnskov (2012), who studied bureaucratic corruption and poverty in Africa.

The Poor in Nigeria

Before moving on to understand the financial behaviour of the poor in Nigeria, it is important to establish their distribution in terms of gender, age and educational status. The essence is to enable us relate the outcome of their financial behaviour with these basic characteristics in order to suggest policy implications thereof. The poor, in this study, was categorised as those individuals in the poorest and second poorest category of our dataset. They are those individuals with income ranging from 1 US$ to 10 US$ for the poorest poor, and those with income level 11 US$ to 20 US$ for the second poorest category. From the dataset, they constitute 12.30 and 15.90 per cent respectively (see Figure 1)

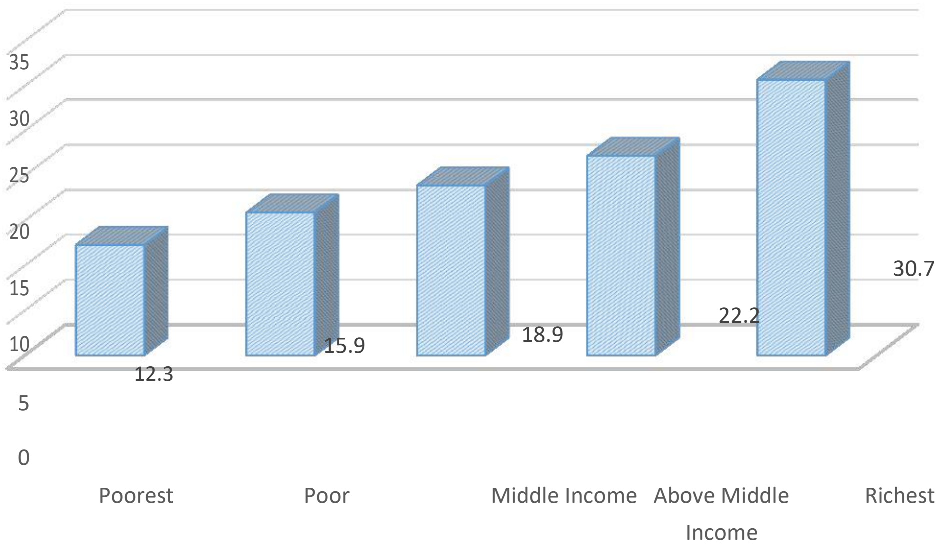

Figure 1: Categorisation of Dataset across Income Quartiles

Since our focus is directed at the individuals in the lowest quartiles, we go further to examine the basic profile of the individuals in this category. We pay particular attention to their age bracket, gender and educational attainment, before moving on to consider their financial behaviour. Table 1 presents these statistics. On the average, the female individuals are poorer than their male counterpart, recording a 52 per cent proportion of the entire survey. Among the category of individuals that have completed only primary education, 59 per cent are female, while 41 per cent are male. The trend changes when higher educational attainment is considered as more males are recorded to have completed secondary and tertiary education than the females. This trend is similar to the observations of the recent Nigerian Demographic and Health Survey (NDHS) which observed that more female than male are more likely to fall within the poverty threshold, and are more likely to be less educated (NDHS, 2013). This gives us reason to believe that we are developing a meaningful profile of the extreme poor in Nigeria.

Table 1: Basic Features of the Poor in Nigeria across Gender

	Male	**Female**
Poorest (%)	48	52
Education: *Primary* (%)	41	59
Completed Secondary (%)	52	48
Tertiary or More (%)	100	0
Age (Average years)	34	33

On the average, Table 1 also shows that individuals constituting the poorest threshold are mostly youths, with a mean age of 34 years for the male and 33 years for the female. This age bracket falls within the African Youth Charter that defines youths as individuals within the ages 15-35 years (African Union, 2006). Most of the individuals in this age bracket are termed "vulnerable" and are susceptible to economic shocks.

Who is Likely to Own a Bank Account and for What Motive?

There are multiple ways of considering the likelihood of a particular gender owning a bank account compared to the other. We can use a simple regression analysis, where the likelihood of owning a bank account is regressed against the gender of the individuals. However, this may suffer from some biases (such as variable omission) that may affect the outcome of the relationship. We chose to follow a more realistic and simplistic way by profiling the account ownership status across gender, as well as their responses to the motives for opening the accounts. The statistics are presented in Table 2.

From the Table, it is evident that more females have bank accounts than their male counterparts. On the average, more women responded in the affirmative that they have a bank account with a financial institution in their country, which is more than the average response rate for the male counterpart. Considering the reason for having a bank account, more male respondents were affirmative that they opened a bank account to enhance their electronic transactions. For their female counterparts, the response rate was lower.

More females use their bank account to receive money from their work payment and to receive money from the government payment. This probably connotes that when it comes to work and business, more women require their bank account to receive funds from these sources of income flow. This finding confirms October 26, 2016 report by a Micro-finance bank chief executive, Ms. Bunmi Lawson in her remarks:

'Of the 53billion naira loans disbursed by Accion Microfinance Bank from inception to date, small and medium scale enterprises owned and managed by women account for 68.5 per cent of the total amount. Willingness to repay and the capacity to repay are core determining factors. Importantly, loans are disbursed to clients whose means of survival is solely dependent on their business among other parameters that must be met by such beneficiaries'.

In spite of this impressive representation of women in accessing funds for their businesses from the above report, more women are poor representing 52% in Table 1 than men. Could it be that the quality of their financial decisions are poor? Is there a correlation between financial decision of the extreme poor and poverty? Unlike the females, the male counterparts had less preference to use their bank account to receive work and government payment. On the contrary, more men require their bank account for receiving money from family and as well as send money to their family members.

This is higher for male than their female counterpart.

Table 2: Profiling Account Ownership and Motives for Opening Account across Gender

	Male	Female
Own Bank Account	1.56	1.67
Uses for electronic transactions	1.93	1.89
Uses it to receive work payment	1.54	1.65
Uses it to receive government payment	1.71	1.82
Uses it to receive money from family	1.54	1.46
Uses it to send money to family	1.65	1.63

The instrument was also administered on the category of individuals that do not have bank accounts in order to find out the specific reasons for not having a bank account. Instrument administration was performed across gender in order to ascertain if the factors responsible for not having bank account vary across gender. The result of this exercise is presented in table 3 as the mean responses.

Table 3: Profiling Reasons why Account is not being opened

	Male	Female
Because the bank is far	1.68	1.71
Because it is too expensive	1.66	1.62
Because of lack of documentation	1.63	1.62
Because of lack of trust	1.84	1.90
Because of lack of money	1.26	1.18
Because of religious reasons	1.97	1.97
Because family member already has one	1.95	1.88

From table 3, it is evident that both the male and female genders almost show similar reasons for not opening bank accounts. However, there are some slight differences identified as the reason given. For instance, more female believe that the reason for not opening bank account is because the bank is far from their homes. Similarly, this category of individuals does not open bank account because of lack of trust. They may find it difficult to trust the financial institutions to put their funds for security. For the male, they do not open bank account because it is too expensive, lack of documentation, lack of money and because the family member already has one. There are no differences with regards to male and female gender not opening account as a result of religious reasons. This is not an important factor for not opening a bank account. From the literature reviewed, gender discrimination in access to loan is almost non-existent in recent time across financial institutions in Nigeria, although accessing loan/credit facilities do come with some bottlenecks (bank policy, collateral, bank charges/interest rates etc.). Provided the documentation is perfected and the borrower (male or female) has capacity for repayment, the loan is accessible and disbursed. Financial institutions oftentimes focus on loan repayment and are limited in influencing the decision on what and how the borrower spends the loan. The financial decision on what to spend/invest the loan on is that of the borrower in most cases. Sadly, the extreme poor use more of the loans for other non-developmental purposes like funeral and marriage celebrations than for productive and poverty alleviating ventures. This is found to be common among younger males than the females.

Another study by Spears (2009), Mullianathan and Shafir (2009) found that in developing countries, many individuals use informal mechanisms such as Rotating Savings and Credit Associations (ROSCAs) to commit themselves to savings rather than opening a bank account (Gugerty, 2001). For Anderson and Baland (2002), ROSCAs provide a forced savings mechanism that a woman can impose on her household with married women better-off saving with ROSCAs than at home. Additionally, women with salaried income participate in ROSCAs than others without a regular source of income.

Econometric Results

The result of the econometric estimations is presented in table 4 for all the main variables and the vulnerable income groups (i.e. the lower income groups). From the table, it is evident that the age of the individuals has a significant negative impact on individuals' decision to open a bank account with a financial institution. The implication of this is that older individuals are likely not going to make the decision to open bank accounts with financial institutions. This is most likely going to be the choice of younger individuals, probably because they are trying to inculcate the culture of saving for future occurrences, unlike older individual that may not see the need to engage the financial institution for such services.

Table 4: Econometric Results for all main variables

	(1)	**(2)**	**(3)**	**(4)**	**(5)**
Variables	**Account**	**Account**	**Account**	**Account**	**Account**
Age	-0.00713***		-0.00406***		
	(0.00110)		(0.00110)		
Education	-0.323***			-0.261***	
	(0.0328)			(0.0320)	
Gender	0.0520*				0.0710**
	(0.0278)				(0.0292)
Income Group	-0.0888***	-0.122***	-0.124***	-0.0938***	-0.120***
	(0.0105)	(0.0105)	(0.0104)	(0.0107)	(0.0105)
Constant	2.645***	2.030***	2.169***	2.395***	1.918***
	(0.0911)	(0.0387)	(0.0539)	(0.0585)	(0.0601)
Observations	997	997	997	997	997
R-squared	0.214	0.121	0.133	0.176	0.126
		Standard errors in parentheses			

*** p<0.01, ** p<0.05, * p<0.1

The result from table 4 suggests that advancement in age has the tendency of significantly reducing the odd ratios of account opening by 0.0071 per cent. Thus increase in age could facilitate financial inclusion at 1 per cent significance level. The increase in level of education of the audience shows a significant decline in the odds ratios of new accounts by 0.32 per cent holding other variables at a constant. Although gender appears to increase the odd ratios of owning an account by 0.052 per cent, it reveals a low significance level compared to age, education and income group. Consequently, higher levels of income grouping negatively influence the odd ratios of having an account. This further implies that higher income group could consider the possibility of opening an account with the financial institutions since they have more cash at their disposal compared the lower income earners. This shows that the level of income of individuals plays a significant role in determining the extent of financial inclusion in the economy.

Evidence from the study also shows that at 5 per cent level of significance, education and income grouping have significant negative impact on the odd ratios of the participants' decision to own a bank account. Gender was observed to be a significant determinant at 10 per cent. These results imply that the main drivers of financial inclusion, in terms of opening savings account by individuals of the household, are the age, educational qualification, and income group. Gender may not be a serious consideration in financial inclusion as the estimation reveals that they do not have a significant impact on the tendency to open savings account. In terms of the size of the coefficient, the education of the individual has a higher impact on the financial inclusion variable, compared to age and income group. Therefore, it is important for policy makers to consider education of individuals when formulating policies that will foster financial inclusion of the individuals.

Summary of Findings, Conclusion and Recommendations

This paper shows that for Nigeria, individuals constituting the poorest threshold are mostly youths, with a mean age of 34 years for males and 33 years for females. This is particularly worrisome and has implications for poverty reduction and national development because this segment of the population ought to constitute the active and vibrant labour force for the nation's economy. Hence the need for government and all stakeholders concerned to seek means of reversing the negative trend.

The paper examined the financial decision of individuals across gender with a view to ascertaining the likelihood of owning bank account and the motive behind such decision. The study found that more females have bank accounts than their male counter-parts, however the motives for opening bank account vary from the male gender to the female gender. While more females opened bank account to receive money for their businesses or from government institutions for work done, the males opened account with financial institutions to enhance their electronic transactions, send money to family members and sometimes receive money from family members. There was a slight difference in the reasons for not opening bank accounts by males and females. For the females, proximity of financial institutions to their place of residence and business and lack of trust in the safety of their funds with banks discouraged them from patronizing the outlets. The males stated lack of money, documentation, and the cost of opening account among others posed major challenges for them.

The econometric result reveals that age is a significant factor in financial decision. Mostly, the young males use loans received from financial institutions for wedding ceremonies, funeral of loved ones etc. The study therefore, concludes that, from whatever source loans /credits are accessed be it from financial institutions (banks) or informal outlets (rotating savings and credit associations – ROSCAs), it is important to channel such funds into productive ventures (investments, asset acquisition, education) rather than spending it on non-profitable activities (marriage ceremonies, funerals & birthdays) that could further aggravate the poverty of the extreme poor.

On the basis of findings from this study, we recommend financial literacy and education of youths from the age bracket of 15-35years old and above on savings culture to enhance good financial decisions that could ultimately assist to reduce poverty in the region. Faboyede et al. 2015, corroborates this in their suggestion that financial education that creates different programmes for specific sub-groups of investors, consumers, i.e. young people, the less educated, aged, & the disadvantaged groups should be promoted). However, it is important for the Central Bank of Nigeria

(CBN) and other bank regulatory bodies to ensure best practices in terms of bank documentation and proximity of bank spread to enable accessibility of bank services and products to members of the society. Periodic review of banking and credit policies is a step in the right direction. The likely outcome will impact positively on the financial decision of the population, improve business, quality of life and ultimately alleviate poverty in the long run.

End Notes

[1]The authors advocated for the use of country-level data because it efficiently allows for better control for omitted variable and measurement biases, and can be used for better exploration of scenarios through which the variables of interest can be observed.

[2]Absolute poverty is measured by the number of people who can afford only the bare essentials of shelter, food and clothing

ROSCAs – Rotating Savings and Credit Associations is an informal means of savings where a group of people with similar lifestyle and interest come together to make (daily, weekly or monthly savings) contribution as the case may be. The contribution is rotated among members at agreed period with no interest charges. Members take turn to access this savings and pay back to the central purse at agreed timelines to enable other beneficiaries access the fund. A leader is chosen among them to organise the collection and disbursement of the funds. A group as small a 5-10 people can form a ROSCAs provided they agree to the terms and conditions.
ROSCAs have been found to be a cheap source of funds for small business start-ups in many parts of rural Nigeria and other African countries. It is easily accessible by both literate and non-literate members of the society. The formal documentation and cumbersome nature of opening bank account is not a requirement for ROSCAs. It is interest free, simple to operate and membership is opened to all provided there's willingness and capacity to repay.

Meaning of ROSCAs across major ethnic divides in Nigeria:
ROSCA"s among the Yorubas of southwest Nigeria is known as *Ajo.* Among the Igbo people of the East, it is popularly known as *isusu w*hile the Hausas of the Northern Nigeria refer to ROSCAs as *Adashi*

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