

**THE CONTRIBUTION OF MICROFINANCE INSTITUTIONS TO  
POVERTY REDUCTION AT SOUTH DISTRICT IN ZANZIBAR**

**HAJI YUSSUF HAJI**

**A DISSERTATION SUBMITTED IN PARTIAL FULFILLMENT OF THE  
REQUIREMENTS FOR DEGREE OF MASTER OF BUSINESS  
ADMINISTRATION OF THE OPEN UNIVERSITY OF TANZANIA**

**2013**

**CERTIFICATION**

The undersigned certifies that, he has read and hereby recommends for acceptance of this dissertation titled “*The Contribution of Microfinance Institutions to Poverty Reduction at South District In Zanzibar*” in partial fulfilment of the requirements for the degree of Master in Business Administration of the Open University of Tanzania.

.....

Dr. Salum Soud Mohamed  
(Supervisor)

.....

Date

## **COPYRIGHT**

No part of this dissertation may be reproduced, stored in any retrieval system, or transmitted in any form by any means, electronic, mechanical, photocopying, recording or otherwise without prior written permission of the author or the Open University of Tanzania in that behalf.

**DECLARATION**

I, Haji Yussuf Haji, hereby declare that this research paper is my original work and it has not been presented anywhere or will not be presented to any other institution for any award.

.....

Signature

.....

Date

## **DEDICATION**

I dedicate this dissertation to Almighty God who gave me life, idea, courage and power to pursue the study and my beloved parents Mr. Haji Haji and Ms Asia Pandu. Also it is dedicated to my brothers and sisters, just mentioning a few, Mr. Hussein Haji, Hassan Haji and Ms. Rehema Haji from our family for their encouragement, assistances, financial support, advices, understanding and prayers during the entire period of my study.

## **ACKNOWLEDGEMENTS**

I wish to convey my heartfelt thanks and appreciation to all those who, in one way or another, contributed to the successful completion of this dissertation. Particularly, special thanks should go to my supervisor, Dr. Salum Soud Mohamed for his guidance, support, monitoring and being involved with me in this study from the initial stage up to the end.

I would also thank my father Haji Haji for, among other things, their lifelong support in my academics and my wife, Amina, and our children, Haji, Omar, Abduli, Kauthar, and Mahir, for their moral support and patience during the whole period of my course.

My deepest and heartedly words of appreciation go to class mates, for being a strong supporter to me throughout my studies. I wish to thank Mr. Said Othman and Mr Suleiman Seif for providing me with their constructive inputs that have been very useful in completing this work.

Lastly, I acknowledge the contributions and supports of all who gave me constructive ideas and participation during the whole process, from the research proposal to the dissertation report production and to those who have helped me during the survey phase, data collection phase and data analysis phase, I thank them all. Errors or omissions are solely mine.

## **ABSTRACT**

The overall objective of this study was to assess the contributions of Microfinance Institutions (MFIs) in Zanzibar and determine their effectiveness in reducing poverty. The problem behind this study was that, there was no adequate MFI's contribution to SMEs in Zanzibar. The study used a mixed methods approach in data collection and analysis. It was conducted in South District of Zanzibar. The study focused on 50 participants that responded to all questions and one MFI surveyed in order to assess its breadth and depth of its contributions in its respective operational areas. Following the information collected from both microfinance institutions and their clients, it was revealed that MFIs have changed the life of poor people in a positive way. MFIs' clients have increased their incomes, capital invested and therefore expansion of their businesses. Despite these achievements it was further observed that some conditions like grace period for loan repayment, loan deposit (loan security) and MFIs coverage have been limiting factors for poor people to access the MFI services. Based on the results of this study, it was recommended that, MFIs should be able to issue loans to needy potential customers and collaterals shouldn't act as barrier. It was further recommended that MFIs need empowerment initiatives including special tax incentives, business and entrepreneurship skills, and special policies that focus to empower in providing loans to indigenous enterprises and individuals who lacks collateral to access financial resources that will results into increasing income, creating employments, eradicating poverty and attaining development sustainability unless the poor will remain poor forever.

## TABLE OF CONTENTS

<b>CERTIFICATION .....</b>	<b>ii</b>
<b>COPYRIGHT .....</b>	<b>iii</b>
<b>DECLARATION.....</b>	<b>iv</b>
<b>DEDICATION.....</b>	<b>v</b>
<b>ACKNOWLEDGEMENTS .....</b>	<b>vi</b>
<b>ABSTRACT .....</b>	<b>vii</b>
<b>LIST OF TABLES .....</b>	<b>xii</b>
<b>LIST OF FIGURES .....</b>	<b>xiii</b>
<b>LIST OF ABBREVIATIONS .....</b>	<b>xiv</b>
<b>CHAPTER ONE .....</b>	<b>1</b>
<b>1.0 INTRODUCTION.....</b>	<b>1</b>
1.1 Background of the Problem .....	1
1.2 Statement of the Research Problem .....	4
1.3 Research Objectives.....	5
1.3.1 General Research Objective.....	5
1.3.2 Specific Research Objectives.....	6
1.4 Research Questions .....	6
1.4.1 Specific Research Questions.....	6
1.5 Significance of the Study.....	7
1.6 Scope of the Study.....	8
1.7 Organization of the Study.....	9
<b>CHAPTER TWO .....</b>	<b>10</b>

<b>2.0 LITERATURE REVIEW .....</b>	<b>10</b>
2.1 Introduction.....	10
2.2 Conceptual Definitions .....	10
2.3 Theoretical Literature Review .....	13
2.3.1 History of Microfinance on Poverty Reduction.....	14
2.3.2 Transaction Cost Theory.....	14
2.3.3 The Link between Micro Finance Institutions and Poverty Alleviation.....	15
2.3.4 Indicators of Growth .....	16
2.3.5 Contribution of SMEs to the Economy.....	16
2.3.6 Challenges Facing MSEs .....	17
2.4 Empirical Literature Review.....	19
2.4.1 Review of Studies Done Outside of Tanzania .....	19
2.4.1.1 Studies Done in Bolivia .....	19
2.4.1.2 Study Done in Bangladesh.....	20
2.4.1.3 Study Done in Turkey.....	23
2.4.2 Review of the Studies Done in Tanzania .....	27
2.5 Research Gap Identified .....	30
2.6 Conceptual Framework.....	31
2.7 Theoretical Framework.....	31
<b>CHAPTER THREE .....</b>	<b>33</b>
<b>3.0 RESEARCH METHODOLOGY .....</b>	<b>33</b>
3.1 Introduction.....	33
3.2 Research Design.....	33
3.3 Area of Study .....	34

3.4	Survey Population .....	34
3.5	Sampling Design and Procedures .....	34
3.6	Nature and Type of Data .....	36
3.7	Data Collection Tools .....	36
3.8	Data Validity and Reliability .....	39
3.9	Data Processing and Analysis .....	40
3.10	Ethical Consideration .....	40
	<b>CHAPTER FOUR.....</b>	<b>42</b>
	<b>4.0 DATA ANALYSIS AND INTERPRETATIONS.....</b>	<b>42</b>
4.1	Introduction.....	42
4.2	Demographic Characteristics .....	42
4.2.1	Clients Coverage by BRAC .....	42
4.2.2	Age Composition of the Study Participants .....	43
4.2.3	Education Levels of Study Participants .....	44
4.2.4	Marital Status .....	45
4.3	Source of Livelihoods for Clients .....	46
4.4	Findings Related to the First Objective.....	47
4.4.1	Micro and Small Enterprises Achievements .....	47
4.4.2	Goal of Loan .....	47
4.4.3	Income Increment and Business Expansion.....	48
4.4.4	Employment .....	49
4.5	Findings Related to the Second Objective .....	49
4.5.1	Loan Interest .....	49
4.5.2	Grace Loan Period .....	51

4.5.3 Loan Size .....	51
4.5.4 Loans Conditions .....	52
4.6 Findings Related to Third Objective.....	53
4.6.1 Saving for Clients .....	53
4.7 Findings Related to the Fourth Objective .....	54
4.7.1 Constraints and Future Prospects of BRAC.....	54
4.8 Constraints and Future Prospects of Clients .....	56
4.9 Performance of BRAC .....	57
<b>CHAPTER FIVE .....</b>	<b>59</b>
<b>5.0 SUMMARY, CONCLUSION AND RECOMMENDATIONS.....</b>	<b>59</b>
5.1 Introduction.....	59
5.2 Summary of the Main Findings .....	59
5.3 Implications of the Findings .....	60
5.4 Conclusion .....	60
5.5 Recommendations.....	61
5.6 Limitations of the Study.....	63
5.7 Delimitation of the Study.....	63
5.8 Areas for Further Research .....	64
<b>REFERENCES.....</b>	<b>65</b>
<b>APPENDICES .....</b>	<b>71</b>

**LIST OF TABLES**

Table 4.1: Clients Coverage by BRAC.....	43
Table 4.2: Age of Clients .....	44
Table 4.3: Education Level of Clients .....	44
Table 4.4: Grace Loans Period.....	51
Table 4.5: Amount of Loans Taken .....	52
Table 4.6: Saving for Clients .....	54
Table 4.7: Repayment Rates of BRAC .....	55

**LIST OF FIGURES**

Figure 2.1: The Link Between MFI Loans and Household Level ..... 31

Figure 4.1: Marital Status of the Clients ..... 45

Figure 4.2: Source of livelihood of Clients ..... 46

Figure 4.3: Goal of Loan ..... 48

Figure 4.4: Classification of Loan Interest to Clients ..... 50

Figure 4.5: Reasons of Unsatisfaction for Loans Conditions ..... 53

## LIST OF ABBREVIATIONS

BRAC	-	Building Resources Across Community
CGAP	-	Consultative Group to Assist the Poorest
CMI	-	Chr. Michelsen Institute
etc	-	et cetera
FIs	-	Financial Institutions
FFI	-	Formal Financial Institutions
GB	-	Grameen Bank
GDP	-	Gross Domestic Product
HBS	-	House Budgetary Survey
IFC	-	International Finance Cooperation
MAWF	-	Ministry of Agriculture, Water and Forestry
MBA	-	Masters of Business Administration
MTI	-	Ministry of Trade and Industry
MFI	-	Microfinance Institutions
MKUZA	-	<i>Mkakati wa Kupunguza Umasikini Zanzibar</i> (Zanzibar Strategy for Growth and Reduction of Poverty)
MSEs	-	Micro and Small Enterprises
NGO	-	Non-Governmental Organization
PRIDE	-	Promotion of Rural Initiative and Development Enterprise
SACCOS	-	Savings and Credit Cooperative Society
SDC	-	South District Commissioner
SMEDP	-	Small and Medium Enterprises Development Policy

- SPSS - Statistical Package for Social Sciences
- URT - United Republic of Tanzania
- VDC - Village Development Community

## **CHAPTER ONE**

### **1.0 INTRODUCTION**

#### **1.1 Background of the Problem**

Zanzibar is a part of the united republic of Tanzania. Comprises of two islands Unguja and Pemba. Tanganyika is a part in the African continent which is 22 miles of the west of Zanzibar Indian ocean coast, it united with Zanzibar to form the united republic of Tanzania on 26th April,1964. Presently Tanzania has two central governments namely the union government and the revolutionary government of Zanzibar.

Large parts of business in Zanzibar are Micro, small and medium enterprises. The Small and Medium enterprises are easy to establish according to their requirements in terms of capital, technology, management and even utilities can also as demanding in rural settings and thus add value to the products and sometimes facilitate the dispersal of enterprises. Majority of Zanzibar people live in rural communities are categorically the small farmers, tenants and landless poor. Meeting basic food and cash requirement for family maintenance is the main challenge for the farm families of rural areas. Survival strategy is the main philosophy of farming transformed from generation after generation. Most Zanzibar micro entrepreneurs are economically isolated, which means that their market is often local, small and does not offer any demand growth prospects.

Due to the decline of the public sector, in 2002. The Zanzibar Government recognised the importance of private financial service. From that period the Microfinance

Institutions were started to be established based on the Government's microfinance policy whose aims at raising the income of both households and enterprises, by facilitating savings, payments, and insurance and credit services (MKUZA, 2007). The introduction of Microfinance Institutions (MFIs) is seen as the best alternative source of financial services for low income earners in rural areas as a means to raise their income, hence reducing their poverty level. Microfinance can be a critical element of an effective poverty reduction strategy. Improved access and efficient provision of savings, credit, and insurance facilities in particular can enable the poor to smooth their consumption, manage their risks better, gradually build their asset base, develop their micro enterprises, enhance their income earning capacity and enjoy an improved quality of life.

MFIs provide two types of services: financial services and non-financial services. On financial services, they offer different types of loans of not more than one year's duration. The non-financial services provided by MFIs are business advice and business training. BRAC is the one among MFIs which puts its operations in Zanzibar. BRAC is non-governmental organisation (NGO) which was incorporated on 1972 in Bangladesh. BRAC has been working in Tanzania since June 2006, its headquarter is located at Plot 2329, Block-H, Mbezi Beach, P O BOX-105213, Dar-es-salaam, Tanzania and have substantial operations through the country, including the poor coastal communities of Zanzibar. BRAC is working through 112 branch offices in 18 Administrative Regions of Tanzania. These regions include:

Pwani, Arusha, Kilimanjaro, Manyara, Kagera, Mwanza, Shinyanga, Mara, Iringa, Dar-es-salaam, Singida, Tabora, Morogoro, Dodoma, Tanga, Zanzibar South and

Zanzibar Urban west. Zanzibar's main area office is located at Mbweni Street Plot-52, P O BOX-2635 and its sub branches are at Kikwajuni, Darajabovu, meli nne, Jang'ombe, Bububu, Mikunguni and Mwera.

The main objective of BRAC in Zanzibar is to provide financial services to the low income entrepreneurs but the overall objective is to increase access to financial service to the people of Zanzibar with a particular emphasis on women who have been left out by the mainstream financial system and this is in line with its vision and mission statements. The vision of BRAC is to create a world free from exploitation and discrimination where everyone has the opportunity to realise their potential while its mission is to empower people and communities in situations of poverty, illiteracy, disease and social injustice. Its inventions aim is to achieve large scale, positive changes through economic and social programmes that enable women and men to realise their potential. And these can be achieved by having innovation, integrity inclusiveness and effectiveness. Since its inception, BRAC has been financed mainly by grants from different donors in and outside of Bangladesh.

The target beneficiaries of BRAC are women only who are poor, but economically active. BRAC provides platform for them to come together, access services, exchange information, analyse and raise awareness on economic, social, legal, gender and other issues concerning their daily lives and their communities.

Generally, the performance of BRAC is regarded as good though there are some limitations. According to the Consultative Group to Assist the Poorest (CGAP) MFIs Best Practice (2001), MFI is said to have a good performance if it has attained

among other things, a minimum annual repayment rate of 95% and at least 88.8% operational self-sufficiency. BRAC has managed to maintain an average annual repayment rate of 99.6% for 6 years. These are 100% from 2006 to 2008, 98.9%, 99.8% and 99% in 2009, 2010, 2011 and 2012 respectively. Operational self-sufficiency is referred to as the degree to which operating income covers operating expenses. BRAC's operational self-sufficiency was very low (29.6%) in 2006.

However it started to increase from 53% in 2007 to 100% in 2012. The increasing trend was due to the increased operating income which is partly contributed by interest from the loan. The number of clients per staff member in BRAC increased from 107 in 2006 to 216 in 2011, above the minimum requirement of CGAP which is 154 clients per staff member. BRAC has managed to reach a large number of clients in the country by increasing the number of sub-branches in various areas in Zanzibar, making it one of the few MFIs which cover large parts of the country. The success of BRAC in reaching a large number of clients while achieving operational sustainability is explained by excellent management team.

In Zanzibar, there were two types of MFIs, namely BRAC and PRIDE. Though they are in town area they also put their operations in South region of Zanzibar. The PRIDE is about one kilometre from Zanzibar town, it is in Mlandege Street while the BRAC is about ten kilometres from Zanzibar town, and it is in Kwerekwe Street.

## **1.2 Statement of the Research Problem**

It was thought by the Zanzibar Government that, allowing the establishments of the private financial services could overcome the poverty (MKUZA, 2007). According

to the Household Budget Survey (HBS) of 2009/2010, many people in Zanzibar still shackled to poverty. Prevalence of poverty is quite high among rural population. There is substantial variation in poverty levels across district. In 2010, the proportions of the poor population ranged between 28.25 per cent in Urban to 74.59 per cent in Rural district (the range of 46.34% points). In 2004/05 HBS, the lowest incidence was 37.62 in Urban and largest was 74.23 in Rural (the range of 36.61% point). The increase in the range indicates divergence. As such, while poverty increased marginally in South Region it declined substantially in North Region from 42 per cent in 2004/05 to 52 per cent in 2009/10.

All the evils i.e. dissatisfaction, desperation, anger, anxiety, diseases and hunger are the consequences of poverty. Most of the poor people live in rural areas have little opportunity. People's access to credit is limited because both formal and informal credit institutions are geared to fund property owners (HBS, 2009/2010). Therefore, this study examined the contributions of these private institutions to poverty reduction. The research took a case of rural area of South District in Zanzibar.

### **1.3 Research Objectives**

This study has both general objective and specific objectives as presented here under:

#### **1.3.1 General Research Objective**

This study aimed at finding out the extent to which Microfinance Institutions (MFIs) contribute to poverty reduction in Zanzibar, and whether they meet the objectives of the policy (Government's microfinance policy aims at raising the income of both

households and enterprises, by facilitating savings, payments, and insurance and credit services) that led to their establishment.

### **1.3.2 Specific Research Objectives**

In order to deal with the above problem, this study has four specific objectives, which take into consideration the comparative nature of the study:

- (i) To assess the general achievements (growth, creation of self - employment and generation of income) of rural farmers after being the members of the MFIs.
- (ii) To analyse the conditions set by MFIs in the whole process of granting credits to rural farmers.
- (iii) To find out the impacts of MFIs in delivering service in rural society.
- (iv) To find out the constraints faced by the MFIs in the delivery of Micro finance services to the rural farmers.

### **1.4 Research Questions**

To be able to meet the above objectives, the study adopts the following key guiding question:

To what extent do MFIs services contribute to poverty reduction?

#### **1.4.1 Specific Research Questions**

- (i) How do the rural farmers be achieved after being the members of MFIs in generally
- (ii) Do the conditions and procedures set by MFIs in the whole process of granting credits favour the rural farmers?

- (iii) What are the impacts of MFIs in delivering service in rural society?
- (iv) What are the constraints faced by the MFI in the delivery of microfinance services to the rural farmers?

### **1.5 Significance of the Study**

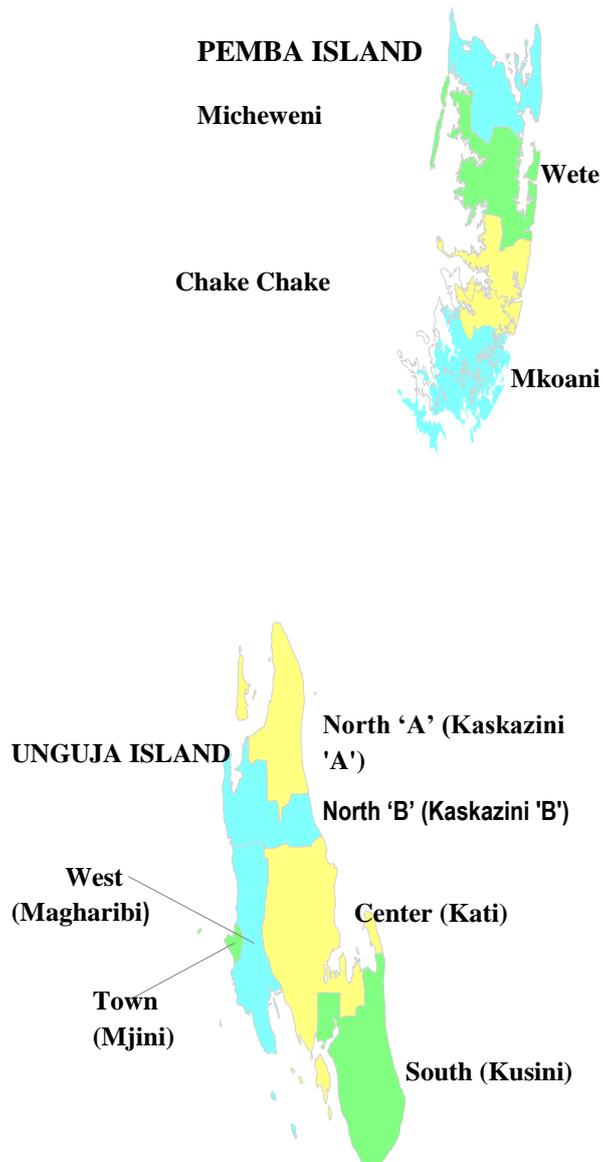
The study provided suggestions to be used in controlling credits by improving procedures in agricultural sector. Suggestions from the study also advised relevant stakeholders involved in micro finance institutions management in awareness and understanding of the procedures. The study also generated the following benefits.

- (i) As the study main objectives is to find out the the extent to which MFIs contribution to poverty reduction in Zanzibar. The study will help the industry on how to manage the Credits.
- (ii) To the academicians, students etc, as there is no study like this done before in the industry; this study will motivate them in carrying out further studies for the purposeof contributions about micro finance institutions.
- (iii) To the standard makers like commercial banks, they can see if there could be a way to modernize the standard so that it can be exercised for the benefit of the entire industry to avoid future financial crisis in the rural areas.
- (iv) To the researcher, as a partial fulfillment for the award of the degree of masters in business administration (MBA) at Open University of Tanzania.
- (v) The study may serve as guidelines to the future reference for research intending to study on similar problems.

### 1.6 Scope of the Study

The research was conducted at South District of Zanzibar especially in rural areas.

Figure 2.1 shows the occupied area of Districts obtained in Unguja and Pemba Islands geographically.



**Figure 1.1: Districts in Zanzibar**

**Source: HBS Construction, (2010)**

## **1.7 Organization of the Study**

This study is divided into five chapters. Chapter one is on background information, statement of the problem and objectives of this study. Chapter two looks at the Literature review, conceptual definitions and research gap. Also empirical literature review is dealt with in this chapter. Research methodology is found in Chapter three. Chapter Four covers Presentation of the findings of the study and discussion on the findings and finally Conclusions and Recommendations is dealt with in Chapter five.

## CHAPTER TWO

### 2.0 LITERATURE REVIEW

#### 2.1 Introduction

This part covers the review of the secondary data related to the subject matter which is the contribution of MFIs to poverty reduction. At the beginning it tries to provide conceptual definitions of key terminologies used in this study. It also provides critical review of supporting theories or theoretical analysis. In addition, it gives theoretical links of relevant studies and it winds up with research gap identified that would assist in the analysis of the study findings.

#### 2.2 Conceptual Definitions

**Microfinance:** Maanen (2004) states that microfinance, is about banking the unbankables, bringing credit, savings and other essential financial services within the reach of tens-or rather hundreds of millions of people who are too poor to be served by regular banks, in most cases because they are unable to offer sufficient collateral. Microfinance can embrace a range of financial services that seek to meet the needs of poor people, both protecting them from fluctuating incomes and other shocks and helping to promote their incomes and livelihoods.

**Microfinance Institutions (MFIs):** Microfinance Institutions refer to financial institutions which provide financial services to the poor who are typically excluded from the formal banking system for lack of collateral (Ledgerwood, 1998). Lack of access to credit is readily understandable in terms of the absence of collateral that the poor can offer conventional financial institutions coupled with the various

complexities and high costs involved in dealing with large numbers of small, often illiterate barriers through innovative measures such as group lending and regular savings schemes.

**Micro and Small Enterprises (MSEs):** There is a wide range of definitions for MSEs, but for the purpose of this study, MSE is defined as a productive activity either to produce or distribute goods and or services, mostly undertaken in the informal sector. A typical micro enterprise employs fewer than five workers, usually family members and has very limited fixed assets.

A small enterprise on the other hand, employs more than five workers and most of them are in a formal sector with much higher fixed assets compared to micro enterprise. Small enterprises are formal undertakings engaging between 5 and 49 employees, or with capital investment ranging from Tshs. 5 million to Tshs. 20 million (URT, 2003).

**Finance:** Finance is the application of economic principles and concepts to business decision making and problem solving (Fabozzi et al, 2006).

**Poverty:** Poverty at its broadest level can be conceived as a state of deprivation prohibitive of decent human life (URT, 1999). This is caused by lack of resources and capabilities to acquire basic human needs as seen in many, but often mutually reinforcing parameters which include malnutrition, ignorance, prevalence of diseases, squalid surroundings, high infant, child and maternal mortality, low life expectancy, low per capita income, poor quality housing, inadequate clothing, low

technological utilisation, environmental degradation, unemployment, rural-urban migration and poor communication (URT, 1999).

**Poor:** Kimenyi et al citing Brody et al (1998) define the poor as a heterogeneous group with diverse livelihood needs and potential that change overtime due to lifecycle, new opportunities and external shocks.

**Poverty Reduction:** Nalunkuuma (2006) argues that poverty reduction is a process of increasing income and economic stability, which will lead to improved fulfilment of basic needs and services and developing a range of assets that will reduce household vulnerability to physical, social and economic shock. Johnson and Rogaly (1997) emphasise that poverty can also be understood as vulnerability to downward fluctuations in income.

**Exclusion:** Qorini Iwan (2005) points out that exclusion means disintegration and fragmentation of poor people from microfinance institution because of inadequate appropriate services and products offered to meet the needs of the very poor clients they are trying to serve leading to marginalisation that lead to economic deprivation.

**Targeting:** This is a method of identifying a certain section of the population or area to benefit from the services offered. This concept is applied to analyse how the poor have been targeted and included in microfinance program (Hirway, 2003).

**Outreach:** Outreach is the number of people reached by a given project. To scale up programmes to reach a large number of clients with small amount of resources has

proved an elusive target of many micro credit schemes because of financial and other constraints. Qorinilwan citing Roglay (1996) notes that an emphasis on the scale is not always having positive impact because to some extent this effort can be counter-productive to the aim of creating sustainable financial institutions for the poor.

**Rural development:** This is the improvement in welfare of rural residents and in the contribution that the rural resources make to the welfare of the population as a whole. It is an on-going and essentially interventionist process of qualitative, quantitative, and/or distributional change, leading to some degree of betterment for groups of people and individual households. Rural development is concerned with the improvement of the living standards of the low-income population living in rural areas on a self-sustaining basis, through transforming the socio-spatial structures of their productive activities. It is broader than agricultural development, which is concerned with only one aspect of the rural people's productive life: agriculture. (Buller and Wright, 1990).

**Microfinance Policy:** Microfinance is one of the approaches that the government of the country has focused its attention in recent years in pursuit of its long term vision of providing sustainable financial services to majority of its population (Rubambey, 2001).

### **2.3 Theoretical Literature Review**

The private sector is the key drive of country, regional and international economies. Economic and financial liberalization in 1991, free market and globalization policies

have resulted into fight for the fittest. The present study assess the contributions of Microfinance Institutions to poverty reduction, the study assumed that accessibility of loan funds from financial institutions operate on free market basis.

### **2.3.1 History of Microfinance on Poverty Reduction**

The types of micro – finance used in the Islamic part of the world include the Islamic micro – finance and the conventional micro – finance. Hashemi (1996) mentioned that Islamic micro finance is of the effective means to fight poverty. The authors mentioned that in Muslim world, the conventional micro finance could not be fruitful because of the Islamic social principles. Most of the people prefer Islamic micro finance on the conventional microfinance.

He concluded that micro credit and microfinance have received extensive recognition as a strategy for poverty reduction and for economic empowerment particularly in rural areas having poor population. Providing poor people the small amounts of credit at reasonable interest rates give them an opportunity to set up their own business at small scale.

### **2.3.2 Transaction Cost Theory**

The theoretical literature review for this study based on transaction cost theory. Transaction cost approach to the theory of the firm was created by Ronald Coase (1960), his theory states that: “In order to carry out a market transaction it is necessary to discover who it is that one wishes to deal with, to conduct negotiations leading up to a bargain, to draw up the contract, to undertake the inspection needed to make sure that the terms of the contract are being observed, and so on”.

The transaction cost can be conceptualized as a non-financial cost incurred in credit delivery by the borrower and the lender before, during and after the disbursement of loan. The cost incurred by the lender include; cost of searching for funds to loan, cost of designing credit contracts, cost of screening borrowers, assessing project feasibility, cost of scrutinizing loan application, cost of providing credit training to staff and borrowers, and the cost of monitoring and putting into effect loan contracts.

On the other hand, the borrowers that is MSEs for this case may incur cost ranging from cost associated in screening group member (group borrowing), cost of forming a group, cost of negotiating with the lender, cost of filling paper work, transportation to and from the financial institution, cost of time spent on project appraisal and cost of attending meetings, etc. (Bhatt, et al. 1998). The parties involved in a project will determine the transaction cost rate. They have the sole responsibility to reduce the risk they may come across.

### **2.3.3 The Link between Micro Finance Institutions and Poverty Alleviation**

MFI schemes were initiated to meet different objectives. The most commonly mentioned objectives include: poverty alleviation and improved living standards, offering financing to the poor (Harper, et al. 1999), women's empowerment, Rahman (1991) and the development of the business sector as a means of achieving high standards and reducing market failure, Chijoriga and Cassimon (1997). Empirical evidences and surveys give mixed results on the performance of MFIs. In some cases debacle stories have been reported, yet there have been success stories. In other cases the reasons for failures or successes have not been well documented.

Linking MFIs with other interventions such as poverty alleviation often complicates the functioning of MFIs by pushing them to areas not considered sustainable. This implies that there is a conflict in measuring financial performance and poverty alleviation. Most of sustainability indicators focus on the MFI as a profitable institution (loan repayment, profitability and degree of subsidisation). Thus for an MFI to meet the microfinance best practices, as given by Consultative Group to Assist the Poorest (CGAP), and be financially sustainable, it has to regard itself as a business venture. As a consequence of this and especially in the rural areas, very few people qualify for a business loan.

#### **2.3.4 Indicators of Growth**

According to Olomi (2001), Economic growth is the increase in the amount of the goods and services produced by an economy over time. It is conventionally measured as the percentage rate of increase in real gross domestic product, or real GDP. There is different range of indicators of growth. This study used income of the MSEs, accumulation of business assets, revenue and employment as indicators of growth for the enterprises while household income, household expenditure on (food, education and health), asset accumulation and self-employment will be used as indicators of livelihood of owners of MSEs.

#### **2.3.5 Contribution of SMEs to the Economy**

MSEs all over the world are known to play a major role in socio-economic development. URT (2003) estimates that about 1/3 of the GDP originates from MSE sector; they tend to be labour intensive thus creating jobs: the International Finance

Company (IFC) of the World Bank estimates that there are approximately 2.7 million enterprises in the country. A large majority of these (98%) are micro enterprises (employing less than 5 people), effective in the utilization of local resources using simple and affordable technology; and complementing large industrial requirements through business linkages, partnerships and subcontracting relationships. URT (2003).

### **2.3.6 Challenges Facing MSEs**

However, it was recognized that, MSEs are confronted with unique problems including heavy costs of compliance resulting from their size. Other constraints include insufficient working premises and limited access to finance, Business Development Services, namely services related to entrepreneurship, business training, marketing, technology development and information are undeveloped and not readily available. SMEs lack information as well as appreciation from such services and can hardly afford to pay the services. As the result, operators of the sector have rather low skills. Institutions and associations supporting SMEs are weak, fragmented and uncoordinated partly due to lack of clear guidance and policy for the development of the sector (URT, 2003).

It is generally accepted that without permanent access to institutional microfinance, most poor households would continue to rely on meagre self-finance or informal sources of microfinance, which limits their ability to actively participate and benefit from development opportunities.

The proponents of credit approach (Yunus, 1984) argue that people who live in developing countries might improve their living standards by becoming micro

entrepreneurs and that financial institutions should support their initiatives with small loans. This is true because well established and sustainable micro and small enterprises in many societies contribute to the growth of national income, more employment opportunities, better standard of living and hence to the reduction of poverty. However, according to the International Finance Corporation, 60% to 69% of the population in many African countries have no access to conventional financial institutions (IFC, 1994). In Tanzania, Micro and Small Enterprises contribute 12% and 34% of rural and urban employment respectively as well as up to 32% of the GDP (Wangwe and Semboja, 1997).

The increased participation and contribution of MSEs has led to an increased need for financial services. Credit has been recognised as one of the tools for promoting the development of MSEs (Chijoriga, 1997). Loans enable the individual member or enterprise to enjoy both benefits of economies of scale and those of new high-value technology (Grande, 1984). Recognising the importance of financial services to MSEs, during 2000 the government of Tanzania developed the National Microfinance Policy in line with the overall financial reforms initiated in 1991 (URT, 2000). The policy aims at enabling low-income earners to access financial services. Microfinance Institutions (MFIs) have become alternative sources for financing MSEs in place of Formal Financial Institutions (FFIs), which regarded MSEs as too poor to save, having low borrowings and carrying a default risk (Chijoriga, 2000).

The poor and poverty reduction has become the object of unparalleled concentration now days both at national and international levels. Elimination of poverty has become

a key issue for all those interested in development of the developing countries (Nalunkuuma, 2006), with microfinance as one of the predominant methodologies for making finance accessible to the poor especially among the donor community. Many donor agencies and governments in developing countries are now funding a growing number of microfinance organisations (Lont and Hospes 2004).

## **2.4 Empirical Literature Review**

The paper seeks to study various financing initiatives implemented in and outside of Tanzania especially Zanzibar and examines the effectiveness and implications of MFIs in eradicating/reducing poverty in Developing Countries the case of Zanzibar through financing business activities and development projects.

### **2.4.1 Review of Studies Done Outside of Tanzania**

#### **2.4.1.1 Studies Done in Bolivia**

Some of the studies, which had a significant contribution, include the study by Mosley (2001). In his study on Microfinance and Poverty in Bolivia, Mosley assessed the impact of microfinance on poverty. The study was conducted through small sample surveys of four microfinance institutions, two urban and two rural, using a range of poverty concepts such as income, asset holdings and diversity, and various measures of vulnerability.

All the institutions studied had on balance, positive impacts on income and asset levels, with income impacts correlating negatively with income on account of poor households choosing to invest in low-risk and low-return assets. This study revealed

also that in comparison with other anti-poverty measures, microfinance appears to be successful and relatively cheap at reducing the poverty of those close to the poverty line. However this was also revealed to be ineffective, by comparison with labour-market and infrastructural measures, in reducing extreme poverty. The study further proposed actions that appear to be promising for the further reduction of poverty.

Despite this contribution, the study by Mosley (2001) has some weaknesses. The first problem is on the sample size which was only four microfinance institutions, this sample size might not be adequate for the generalisations made above. Also the poverty concepts considered excluded the number of employees, this is very important to measure, as it indicates whether the microfinance institution has created capacity to employ more people or not.

#### **2.4.1.2 Study Done in Bangladesh**

Amin (2003) used a unique panel dataset from northern Bangladesh with monthly consumption and income data for 229 households before they received loans. He found that while microcredit is successful in reaching the poor, it is less successful in reaching the vulnerable, especially the group most prone to destitution (the vulnerable poor). Coleman (1999) also finds little evidence of an impact on the programme participants.

The results, Coleman further explains were, consistent with Adams and von Pischke's assertion that "debt is not an effective tool for helping most poor people enhance their economic condition" and that the poor are poor because of reasons other than lack of access to credit.

According to Mosley (2001), microfinance makes a considerable contribution to the reduction of poverty through its impact on income and also has a positive impact on asset level. But the mechanism through which poverty reduction works varies between institutions. Generally, institutions that give, on average, smaller loans reduce poverty much more by lifting borrowers above the poverty line, whilst institutions giving larger loans reduce it much more by expanding the demand for labour amongst poor people.

Mosley and Hulme (1997) found evidence of a trade-off between reaching the very poor and having substantial impact on household income. They found that programmes that targeted higher-income households (those near the poverty level) had a greater impact on household income. Those below the poverty line were not helped much and the very poorest were somewhat negatively affected. The poorest tended to be more averse to risk-taking. They also used their loans for working capital or to maintain consumption levels rather than for fixed capital or improved technology. Since, microcredit programmes typically require loan repayment on a weekly basis; some critics argue that repayment comes from selling assets rather than from profits of micro-enterprises.

Hassan and Renteria-Guerrero (1997) made another empirical contribution in this area (Microfinance contributions). In their work “The experience of the Grameen Bank (GB) of Bangladesh in community development”, they examined the GB experience with a purpose of understanding the essential elements of its operations and the factors that enabled GB to reach the poor. This study revealed that the GB

has established its credentials as an institution that aims at providing credit to the landless and asset less poor in rural areas. GB credit gives the recipients the power of entitlement to society's productive goods and services with immediate effect, unlike most of the other programmes for the poor that tend to create the unintended negative effect of dependency on the service providers.

However, it was observed the credit by itself is an insufficient factor to improve poverty conditions, and thus the GB devotes a substantial amount of resources to the improvement of the social wellbeing of its members. The GB uses an unambiguous eligibility criterion which ensures that only the poor or very poor can participate. It motivates their clients to organise themselves into groups of five like-minded members. Each group elects one group leader among themselves. Every six groups form a "centre" which serves as the basic operating unit of the GB. It is at the centre that weekly meetings are conducted to openly discuss loan applications proposals and to accept weekly repayments and compulsory savings deposits. While the loans are made to individual members, the group as a whole is expected to be responsible for the regular repayments of the loans of all their members. This form of grassroots organisation not only promotes solidarity and participation among the members, at the group and centre levels, but also promotes mutual support and peer pressure to ensure that the loans are properly utilized and repayments made promptly.

In concluding their work, Hassan and Renteria-Guerrero assert that the GB's approach seems to be an effective tool for rural poverty reduction despite minor criticism that has never given alternative solution for poverty alleviation. The program supplies credit to improve the physical productive capacities of the poor and

in addition, it provides the disadvantaged with human development inputs to improve their overall productive and living standards. The success of the GB is not free from the influence of external factors. To be effective and sustainable, a credit delivery system also needs a supportive national policy framework for it to remain autonomous and free from political influence. Despite the fact that this work was just an experience and not a research work, we acclaim its contribution in the area of microfinance practices.

#### **2.4.1.3 Study Done in Turkey**

Cook, et al (2000) conducted a study in Turkey and mentioned that micro finance especially micro credit is a powerful tool to reduce poverty. The author has mentioned that one fifth of the population of turkey was at risk due to the poverty even then it is not a poor country according to global standards. Moreover the author mentioned that poverty, both in Turkey and all over the world, is not only a function of micro credit but a political problem, and political intervention of the state holds the ultimate resolution to struggle against poverty. Beck (2005) as cited by Cook (2000) concluded that micro finance is the founding stone for poverty reduction.

Their study showed that there is a fundamental linkage between microfinance and poverty eradication, in that the latter depends on the poor gaining access to, and control over, economically productive resources, which includes financial resources. Previously implemented programs not produced good results due to the non-involvement of the peoples for which the programs was designed (the poor). They suggested that the government poverty alleviation program should be restructured if not redesigned and should be cantered on the basic needs approach. Micro finance is

the mean for income generation and the way for permanent reduction of poverty through the provision of health services, education, housing, sanitation water supply and adequate nutrition. In many instances, micro enterprises rather than formal employment create an informal economy that comprises as much as 75 per cent of the national economy.

**(i) Study Done in Namibia**

From the study of Jonathan Adongo (2005), he found that: Microfinance institutions provide the full-range of financial services but on a smaller scale. This is suited to the needs of the rural poor. In Namibia, microfinance institutions operating in the rural areas can be distinguished as informal or formal. Informal microfinance institutions in Namibia are those that are not registered or governed by any legally mandated entity. They include informal groups, unregistered money lenders and burial societies.

Due to the difficulty in establishing standards or enforcing legal provisions for noncompliance informal microfinance institutions are less preferred to formal institutions. Fortunately, not much use is made of informal financial alternatives in Namibia. The FinScope survey conducted in 2006 showed that only 12% of the overall Namibian population use informal financial services. Formal microfinance institutions in Namibia are governed by the Division of Cooperative Development in the Ministry of Agriculture, Water and Forestry (MAWF), the Namibia Financial Institutions Supervisory Authority and the Ministry of Trade and Industry (MTI) Steering Committee.

The survey concluded that microfinance is an innovative step towards alleviating poverty. The author mentioned that microfinance facilities provided to the people help them to use and develop their skills and enable them to earn money through micro enterprises. Moreover provision of micro finance helps them to smooth their consumption level and manage unexpected risks. Micro finance helps the poor to build assets, educate their children and have a better quality of life.

**(ii) Study Done in UK**

Papered by Fatchamps (1997). The paper has shown that access to microcredit has increased the money income of beneficiary households by creating self-employment for the female members in societies where female-work remains largely non-marketed. While microfinance can potentially help the economies of poor households by allowing them to utilize their female labor as well as explore their entrepreneurial abilities, it has not necessarily afforded them an expeditious escape out of poverty. The crux of the problem lies in the economic environment where the poor households find themselves. To begin with, the immediate factors that affect their incomes adversely are the credit-limits and relatively high interest rates charged by the microcredit institutions. Even in the absence of difficult credit-market conditions, there are other challenging constraints to expanding the incomes of microenterprises. Of these constraints, two are fundamental to the process of graduation of the households from poverty.

The Author noted that with insufficient funds, farmers and fishers cannot invest in new equipment and machinery, and it becomes difficult to reach out to new markets and products. He further contended that without financial assistance, small farmers

and artisanal fishermen cannot cope with temporary cash flow problems, and are thus slowed down in their desire to innovate and expand. The general perception is that access to external finance is critical for poor entrepreneurs, who may never have funds proportional to their ambitions.

Pitt and Khandker (1998) reasoned that given the small loan size and the type of activities undertaken by micro-entrepreneurs, it is unlikely that capital intensity has increased. Given that the labor and the capital intensity of rural non-farm production are unchanged, increased microfinance implies that employment can be expected to rise. However, if increased income as a result of microfinance programs results in a decrease in labor supply (income effect), it can negatively affect labor supply of particular type, for example male labor supply. As a result employment may decline, given the demand for labor. Therefore, the net impact cannot be determined a priori. Microcredit programs seem to reduce wage-employment and income, but raise self-employment and corresponding income for program participating households. One might expect that a reduction of employment in the wage market might increase wages, but this may not happen because the wage-employment gap may be filled by previously unemployed or underemployed wage workers.

### **(iii) Study Done in China**

On the study of Nichols (2004), he revealed that, over the past 25 years, China has made huge strides in its battle against poverty as it has transformed into one of the most dynamic economies in the world. China's poverty rate today is probably slightly lower than the average for the world as a whole. In 1980 the incidence of

poverty in China was one of the highest in the world. What might many developing countries that have been less successful against poverty learn from China's experience? And what can China learn for its continuing efforts against poverty? Based on survey data spanning 1980–2001, they analyzed China's record against poverty over the two decades since Chinese leader Deng Xiaoping introduced his pro-market reforms in 1978. Their study shows that, while the incidence of poverty in China fell dramatically, progress was uneven. Rural areas accounted for the bulk of the gains to the poor, although migration to urban areas helped. However, for China to make more progress against poverty, it will have to confront the problem of rising inequality.

The Author used a case study approach to investigate the impact of microfinance upon the lives of the poor in the rural China and found that the participation of poor in MFI program had led to positive impact in their life. Their income have increased, spending on educational and health have increased hence improved their standard of living and also women have benefited out of this program. There were visible sign of higher wealth level within the village.

#### **2.4.2 Review of the Studies Done in Tanzania**

In Tanzania several studies has been done on microfinance institutions service, there are over 50 registered MFIs in Tanzania but their overall performance has been poor. In her study Chijoriga evaluated the performance and financial sustainability of MFIs in Tanzania, in terms of the overall institutional and organisational strength, client outreach, and operational and financial performance. In the study, 28 MFIs and 194

MSEs were randomly selected and visited in Dar es Salaam, Arusha, Morogoro, Mbeya and Zanzibar regions.

The findings revealed that, the overall performance of MFIs in Tanzania is poor and only few of them have clear objectives, or a strong organisational structure. It was further observed that MFIs in Tanzania lack participatory ownership and many are donor driven. Although client outreach is increasing, with branches opening in almost all regions of the Tanzanian mainland, still MFIs activities remain in and around urban areas. Their operational performance demonstrates low loan repayment rates and their capital structures are dependant on donor or government funding.

In conclusion, the author pointed to low population density, poor infrastructures and low house hold income levels as constraints to the MFIs' performance. Many of these MFIs have no clear mission and objectives. Also their employees lack capacity in credit management and business skills. Among the questions which arise out of these research findings is whether these MFIs whose performance is questionable will have any impact on poverty alleviation.

Other studies on microfinance services, in Tanzania were carried out by Kuzilwa (2002) and Rweyemamu et al, (2003). Kuzilwa examines the role of credit in generating entrepreneurial activities. He used qualitative case studies with a sample survey of businesses that gained access to credit from a Tanzanian government financial source. The findings revealed that the output of enterprises increased following the access to the credit. It was further observed that the enterprises whose

owners received business training and advice, performed better than those who did not receive training. He recommended that an environment should be created where informal and quasi-informal financial institutions can continue to be easily accessed by micro and small businesses.

Rweyemamu *et al*, (2003) evaluated the performance and constraints facing, semi-formal microfinance institutions currently providing credit in the Mbeya and Mwanza regions. The primary data, which were supplemented, by secondary data, were collected through a formal survey of 222 farmers participating in the Agricultural Development Programme in Mbozi and the Mwanza Women Development Association in Ukerewe. The analysis of this study revealed that the interest rates were a significant barrier to the borrowing decision. Borrowers also cited problems with lengthy credit procurement procedures and the amount disbursed being inadequate. On the side of institutions, the study observed that both credit programmes experienced poor repayment rates, especially in the early years of operation, with farmers citing poor crop yields, low producer prices and untimely acquisition of loans as reasons for non-payment.

It was further revealed that poor infrastructure of the MFIs led to high transportation costs, which increased the transaction costs in credit procurement, and disbursement and this ultimately hindered the effectiveness of the credit programmes. This happened because most of borrowers lived in rural areas, far from credit offices. The coverage by Kuzilwa was on the National Entrepreneurship Development Fund only, while Rweyemamu *et al*'s study was on assessing the micro-finance services for the agricultural sector only.

From the above evidence the researchers found that there was a strong need to study the schemes existing in Tanzania and see to what extent their operations contribute to poverty reduction in the country. Recommendations were made to policy makers so as to find alternatives through which financial services could be offered to the low income earning population or rather restructure the existing schemes for poverty reduction.

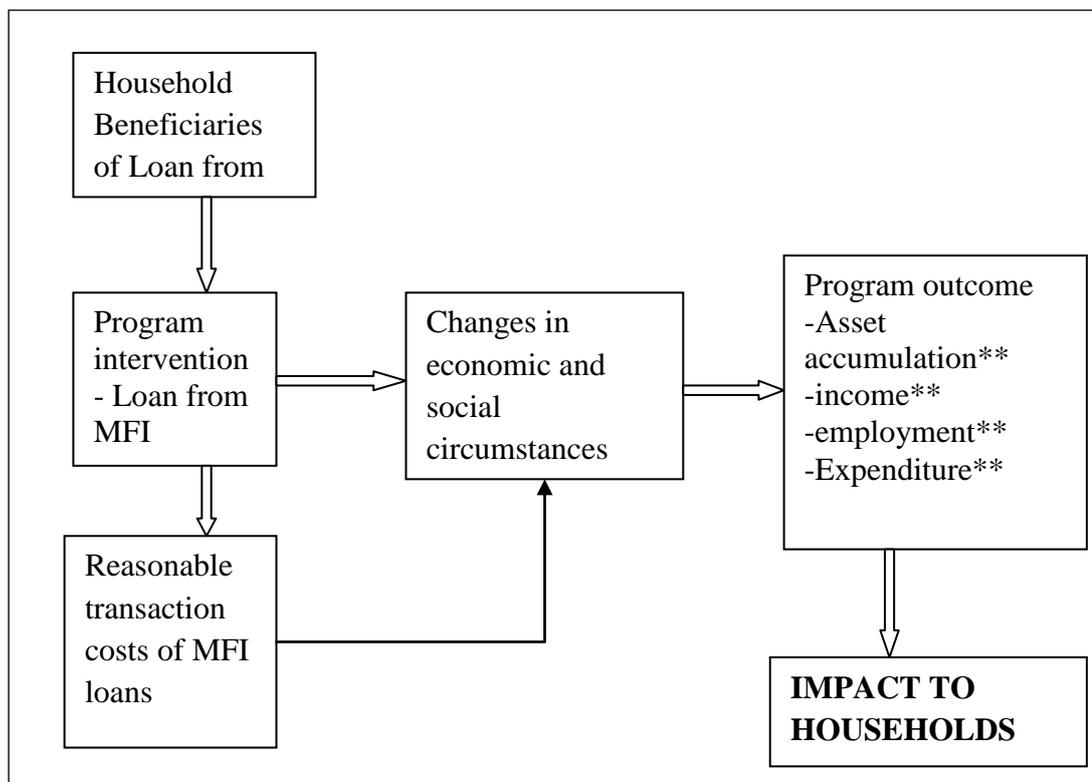
In a study conducted by Kessy & Urrio (2006) on contribution of MFI on poverty reduction in Tanzania, the researchers covered four regions of Tanzania which are Dar es salaam, Zanzibar, Arusha and Mwanza. Both primary and secondary data were collected; primary data were collected from 352 MSE's through questionnaires, interviews were also conducted. PRIDE which is a microfinance institutions were used as a case study so as to get the insight of MFI operations. The study findings pointed out that to large extent MFI operations in Tanzania has brought positive changes in the standard of living of people who access their services, clients of MFI complained about high interest rate charged, the weekly meeting was pointed out as barrier as the time spent in weekly meeting could be used to other productive activities. The study recommended MFI to lower its interest rate, increase grace period and provide proper training to MSEs.

## **2.5 Research Gap Identified**

There are a number of studies have been done in the area about MFIs. Most of them concentrate in success and failure factors both internal and external. To the researcher's effort, there is none of the study done concentrate on the contribution of

Microfinance Institutions in the light of poverty alleviation in rural area especially South District of Zanzibar from 2002 where microfinance policy made. Zanzibar's microfinance policy aims at raising the income of both households and enterprises, by facilitating savings, payments and insurance and credit services (Mkuza, 2007).

## 2.6 Conceptual Framework



**Figure 2.1: The Link Between MFI Loans and Household Level**

\*\* Variables to be analyzed

**Source: Author' construction**

## 2.7 Theoretical Framework

The theoretical framework developed from conceptual framework's structure sheds the light for the methodology of this study. The conceptual framework developed to reflect the outcome of MSEs growth at household level, this is due to the assumption

that increase on growth, result into an increase of MSEs owner's wealth and overall standard of living since the profit obtain from SMEs activities enable the SMEs owners to meet his/her living expenditure, hence create a possibility of trickledown effect.

Coase (1960) pointed out that financial intermediation involves transaction costs and according to Chijoriga and Cassimon (1999) transaction costs comprises cost involved in finding a lender, mismatch costs and risk premium, all these transactions increase the gross cost of credit for the borrower. The conceptual framework reflects the effect of transaction cost on SMEs when accessing and servicing MFI services.

## **CHAPTER THREE**

### **3.0 RESEARCH METHODOLOGY**

#### **3.1 Introduction**

This section describes the research procedure in terms of research approach and research design, operational design, statistical design and data analytic strategy (handling of intervening and extraneous factors, sampling procedures, data sources, quality and data collection methods, and data processing procedures to be adopted), ethical consideration, and data validity and reliability.

#### **3.2 Research Design**

The study involved both primary and secondary source, the data gathered is crucial to make a reasonable arguments. This imply that data from primary sources including practionners, academicians, entrepreneurs, policy makers and any stakeholders are crucial in complementing the data from secondary sources such as theories, library research, previous literatures, books, the internet, journal articles, reports and so on.

In addition the research also conducted structured and unstructured interview and observation within sampled population. This mainly focused to get the insight data that could not be gathered throughout questionnaires that influence/hinder borrowers, lenders and policy makers.

The study is characterised by mixed methods approach; it combines the quantitative and qualitative ways in collecting and analysing data in a single study. Reasons for

combination of both techniques are based on complementarily and triangulation (Berger, 2000). Basically, social science based on “objectivity” of quantitative methods is complemented with the quality of things; the what, how, when and where of social issues (essence and ambience of things); meanings, concepts, definitions, characteristics, symbols and descriptions of things.

### **3.3 Area of Study**

This study was conducted at South District of Zanzibar, one of the six districts in Unguja Island, namely: Town District, West District, North District, Centre District and South District. The area was among the areas in which Microfinance Institutions have concentrated their efforts and it was among those areas where the people in need of Microfinance Institutions, and since researcher lives in this area, it was found convenient for data access.

### **3.4 Survey Population**

The study involved two groups of respondents. The first group was the staff working in Microfinance Institution and the other group was the members registered in the Institution.

### **3.5 Sampling Design and Procedures**

The researcher used non-probability sampling. A core characteristic of non-probability sampling techniques is that samples are selected based on the subjective convenience of the researcher, rather than random selection (i.e., probabilistic methods), (Grande, 1984). Non-probability sampling is divided into three types; namely, judgment, convenience and quota sampling.

**Judgment:** Sometimes it is hard to get a sample that accurately represents the subjects. So judgment sampling occurs when the researcher creates the sample themselves, looking for what the researcher believes is the best representation of the population. The greatest problem with judgment sampling is that researchers tend to disagree with what constitutes an accurate sample, leading to differing opinions about which research findings are “more correct” – an argument that is invalid in probability sampling.

**Convenience:** Convenience samples are the most well-known type of non-probability sampling. Convenience sampling is simply sampling those around you, or those that you know you can reach. Polling a group of people that happen to be in a room would be a form of convenience sampling. The main issue with this style of sampling is that it ignores everyone not in proximity.

**Quota:** Quota sampling has some similarities to judgment sampling, in that the researcher decides on the quota that “best represents the population.” Quota sampling takes the population’s known statistics, chooses what portion of the population is a large enough sample, and then creates a proportionate sample for their research. The greatest problem with quota sampling is not necessarily the quota itself, but the method used to choose those that enter the sample. They also may not account for unknown aspects of the demographic.

Non-probability sampling is often used because the procedures used to select units for inclusion in a sample are much easier, quicker and cheaper when compared with probability sampling (Ayyagari, 2003). This is especially the case for convenience

sampling. For students doing dissertations at the undergraduate and master's level, such practicalities often lead to the use of non-probability sampling techniques.

For this study, convenience sampling was used because the BRAC's registered members in South District of Zanzibar were not large which lead to be much easier, quicker and cheaper. The sample size of the BRAC's members in South District is the same as the all registered members occupied by BRAC Institution. There were only 45 registered members, so all members were questioned and in addition of 5 operational staffs of the BRAC Institution were interviewed to make sample of 50 respondents.

### **3.6 Nature and Type of Data**

Both primary and secondary data were collected. All primary data were collected through interviews, questionnaires and observation. While secondary data were obtained from the Institutions documents such as Audit report, operational manual registers etc. Therefore asking for such documents from the management and in-charge concerned helped the researcher to source and obtain more information.

### **3.7 Data Collection Tools**

Data collection techniques are the approaches, or methods that enable researcher to gather the required data. Therefore primary data were collected through, questionnaires, interview and observation, while secondary data were obtained through documentation. All instruments were introduced to respondents so as to enable them to know the objectives of the study.

**Observation:** Direct observation is used to gather various information by using five sense organs (Chen, 1997). During data collection and compilation, researcher used “participant observation approach” to get reliable information focusing on the problem. This was important for a researcher because it helped to note other information that was relevant while collecting information on the activities which were going on. The researcher participated in daily operations, observing and recording information that were not be given by respondents when answering.

**Interview:** This is the direct contact between researcher and respondents. The interviewer (researcher) and respondent (interviewee) engaged in oral questioning or discussion. The interviews was conducted by the researcher to managers and lower level management. Unstructured interview was used to secure data,the researcher conducted a semi structured interview in Kiswahili. Likewise, unstructured interview were used by the researcher to supplement some questions depending on responses from interviewees. This helped in creating rapport by the researcher and in collecting some data, which were confidential or not easily disclosed.

**Questionnaires:** A questionnaire consists of a number of questions in a definite order; this method is used for gathering data which require the researcher to prepare questions for specific strata of the population (Kothari, 2004). Questionnaires contained self-explanatory and self-administered instructionsthis helped and enabled respondents to answer questions clearly and at their convenience time. There are two types of questinnaires: Structured and Semi-Structure questinnaires.

**Structured Questionnaires:** These were used to collect information from households. Questionnaires were developed to obtain survey data that allowed an

understanding of the impact of micro financing services on the growth of micro and small entrepreneurs. They consisted of open and close ended questions with enough flexibility to allow new issues to be raised and filled in. The section on demographic data of the participants included age, marital status, educational level, employment and residence. These questions were included to obtain general views of the participants' social characteristics and be able to make triangulation analysis based on those characteristics. The major section of the individual questionnaire contained closed ended questions on how they are benefited from their Microfinance Institution. Based on the objectives of the study, questions were reformulated in simple, easy-to-understand language and were administered in the preferred language of the study participants, i.e. Kiswahili.

Questionnaires were designed to match the objectives of the study and focused to bridge the gap found in the Literature Review as discussed earlier. The questionnaires were distributed to target respondents since the number of sample size chosen were the same as number of the whole members registered in the MFI of the South District in Zanzibar. The aim of questionnaires is to gather the information that will assist to assess the ability of MFIs to provide service to rural farmers. Also to understand and suggest the best workable strategies on eradicating poverty through business.

**Semi-Structured Questionnaires:** These were used to guide dialogue with a range of stakeholders from microfinance institutions and officials who are involved in outreach missions of spreading microfinance services especially in rural areas and informed people in the areas of study.

**Documentary source:** This involved collecting information and data from existing surveys, reports and documents. Documentary sources concerned with the examination of document were available at Financial Institutions in Zanzibar. Those documents enabled the researcher to source required data and information. Documentary sources were obtained from institutions files and other records. The documents include manuals and reports kept by the departments of the concerned Institution.

### **3.8 Data Validity and Reliability**

Validity is the degree to which an instrument measures what it is intended to (Denise, *et al*, 2001). The instruments for this study were pre-tested. Components that were assessed during the pretest included; economic growth among the members. Pre-testing was done to determine whether the questions were clear, unambiguous and could be understood by the study participants. Some adjustments to the questions in terms of language used, content and flow were made.

Ondeng (2000) refers reliability to the question of whether a measuring instrument or process can produce the same result if successively employed by different researchers. In the language of measurement equation, it refers to persistence of systematic error in the measurement process. It is a measure of how consistent the results from a test and it involves the accuracy of the research methods and techniques.

For the case of this research concerning an assessing the contribution of microfinance on poverty reduction, collected information were reliable and valid

because the researcher was careful in collecting, analysing and processing data from the respondents, the researcher was explicit, unambiguous and less complicated when formulating a questionnaire. The use of both primary and secondary sources of data by using different types of data collection instruments such as Questionnaire, interview, observation and documentary sources were designed to measure the same thing in order to check reliability. Also the use of purposeful sampling allowed the researcher to select the respondents based on the knowledge of the population its elements and research objectives. The researcher asked questions that were relevant to the study.

### **3.9 Data Processing and Analysis**

The data were entered into Statistical Package for Social Science (SPSS) software version 20.0 and processed, the results were analysed using a simple descriptive statistics such as mean and standard deviation, the frequency and cross tabulation were also employed on some variable. Microsoft Spread sheet was also used to generate the bar charts and pie charts.

### **3.10 Ethical Consideration**

Ethics are norms for conduct distinguish between acceptable and unacceptable behaviour. Research ethics refers to the application of fundamental ethical principles to a variety of topics in scientific research (Kothari, 2004). These include the design and implementation of research involving:

Various aspects of academic scandal and so forth. The confidentiality of those involved in the observation must be carried out, keeping their autonomy and privacy secure.

Also since research involved a great deal of cooperation and coordinating among many different people in different disciplines and institutions, ethical standards promote the values that are essential to collaborative work such as trust, accountability, mutual respect and fairness.

Therefore, this study considered all these measures to secure the actual permission, and interests of all those who involved in the study and information provided by each individual or entity remained confidential throughout the study. Ethical issues such as guideline for authorship, copyright and patenting policies, data sharing policies and confidential rules in peer review were taken into consideration.

## **CHAPTER FOUR**

### **4.0 DATA ANALYSIS AND INTERPRETATIONS**

#### **4.1 Introduction**

This chapter consists of data collection, analysis and interpretation of the study. The main objective is to find out the extent to which Microfinance Institutions (MFIs) contribute to poverty reduction at South District in Zanzibar so as to come up with possible measure and strategies to be taken by the MFIs, policy makers and government in the overall process of empowering, promoting and modernizing business activities. During data gathering, questionnaire and interview were used as means of collecting first hand primary data and journals, books, newspaper, extra used to gather secondary data.

Only BRAC was chosen for collecting data since it is considered to be among the MFIs with the best practices for administering microfinance services in Zanzibar. Questionnaires were distributed to 45 BRAC's clients. In addition, BRAC branch manager as well as 4 employees to make the total of 5 staffs were oral interviewed to gain more insights on how it had assisted rural farmers to raise their income and expand their business activities.

#### **4.2 Demographic Characteristics**

##### **4.2.1 Clients Coverage by BRAC**

Clients coverage by BRAC in South District of Zanzibar, depends on various factors like availability of other financial institutions in the particular Village, nature of services provided by BRAC, etc. During study, it was found that, though the BRAC's

office is centered at Makunduchi whose sub villages are Kajengwa, Kijini, Kiongoni, Mzuri and Tasani, Mtende region has high coverage, which is 33.3% compare to the other regions since there was no other financial institution in the Village and people have to rely mainly on BRAC to fulfill their financial needs. Jambiani village includes Kibigija and Kikadini while Mtende and Muyuni villages have the same names with their shehias as appear in the table below:

**Table 4.1: Clients Coverage by BRAC**

<b>Shehia</b>	<b>Respondents</b>	<b>Percent</b>
Kajengwa	2	4.4
Kibigija	4	8.9
Kijini	3	6.7
Kikadini	5	11.1
Kiongoni	4	8.9
Mtende	15	33.3
Muyuni	4	8.9
Mzuri	3	6.7
Tasani	5	11.1
<b>Total</b>	<b>45</b>	<b>100.0</b>

**Source: Field Data**

#### **4.2.2 Age Composition of the Study Participants**

Table 4.2 below illustrates that, all 45 respondents were of the age group between 20- 50 years group. This shows that most of the people engaging in the credits from MFIs were not so young and not so elders. The standard deviation shows how much variation or dispersion exists from the average (mean), or expected value. A low standard deviation indicates that the data points tend to be very close to the mean; high standard deviation indicates that the data points are spread out over a large range of values. The surveyed area shows that on average the age of the clients was

37 years and the magnitude that deviate from the mean was 7.9, this result implies that the age of clients are close to the average and distributed normal as revealed in the value of Skewness and Kurtosis statistic which lie within -1 and +1.

**Table 4.2: Age of Clients**

	N	Minimum	Maximum	Mean	Std. Deviation	Skewness		Kurtosis	
						Statistic	Error	Statistic	Error
<b>AGE</b>	45	20	50	37.31	7.962	-.152	.354	-.810	.695

**Source: Field Data**

#### 4.2.3 Education Levels of Study Participants

In South District, people who have essential and sounding knowledge (University or College education), skills on entrepreneurship, financing, marketing, project management, risk management, and so on, they don't normally engage on self-employment instead they look well on government employment. The study has observed that, in BRAC, the people with Secondary Ordinary Level of Education managed and operated more than the other level. They dominated 53.3% of the all 45 members registered. As shown in the Table 4.3 below:

**Table 4.3: Education Level of Clients**

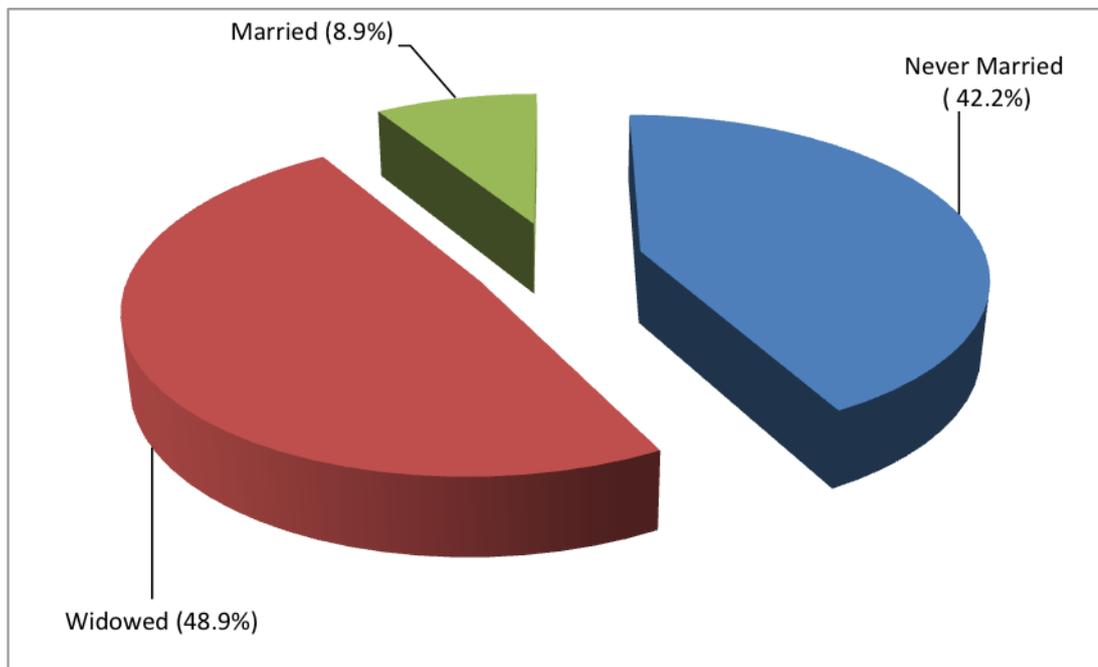
Education Level	Respondents	Percent
Primary	15	33.3
Secondary (O'Level)	24	53.3
Secondary (A'Level)	6	13.3
<b>Total</b>	<b>45</b>	<b>100.0</b>

**Source: Field Data**

#### 4.2.4 Marital Status

BRAC provides its service only for women. It has been recognized by the BRAC's staffs that women are more responsible managers of household finances and are disciplined borrowers. They make proper use of loans and make timely payment of interest. Women are more responsible managers of household finances and are disciplined borrowers. They make proper use of loans and make timely repayment. There fore, they are more reliable credit clients and better co-operators than males.

The findings revealed that 48.9% of 45 women members are widow, 42.2% of married followed by only 8.9% never married. This indicates that, women who have no husbands were more engaged in taking loan. Since they had no other alternative income source compare with women belong husbands.

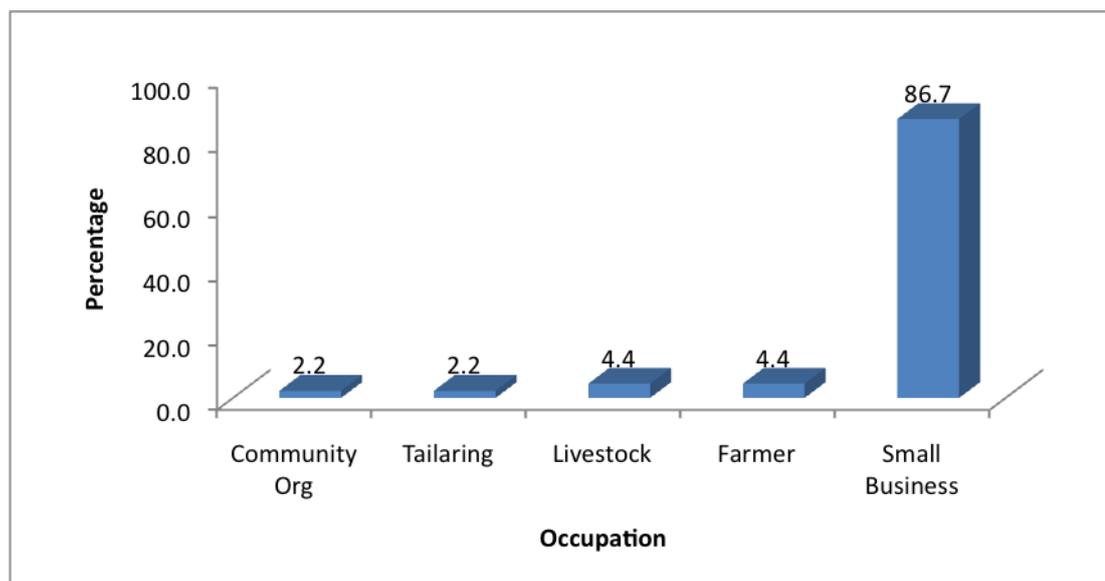


**Figure 4.1: Marital Status of the Clients**

**Source: Field Data**

### 4.3 Source of Livelihoods for Clients

Credit is provided for different purposes related to production, marketing, personal effects and other income/employment generating activities. To develop the saving habit among small farmers, group savings and their mobilization are also being undertaken as an integral component in which every member is required to deposit a certain amount (as per a decision made by the group) in a group savings fund. As a complementary input to credit and savings services the target groups of the program are also trained in different areas such as group management and functioning, savings mobilization, income generating activities, etc.



**Figure 4.2: Source of Livelihood of Clients**

**Source: Field Data**

The sources of livelihoods for clients are various. 86.7% of 45 clients depended on small business, 4.4% on farmers (agriculture), 4.4% were live stocks, 2.2% involved in tailoring and again 2.2% were involving in different community organizations. Thus, it can be concluded that the biggest source of livelihood for the Clients is

Small Business which percentage to 86.7 of the total sources of livelihoods. The following figure summarizes the reality of the sources of livelihoods of the Clients.

#### **4.4 Findings Related to the First Objective**

The first objective concerns with the general achievements of rural farmers after being the members of the MFIs

##### **4.4.1 Micro and Small Enterprises Achievements**

To a large extent MFIs operating in Zanzibar have brought about positive changes in the standards of life of the clients who received MFI services. 80% of 45 the surveyed MSEs revealed that their profit had increased after receiving the loan and they were in the age group of 25 to 40 years. With regard to the level of education, the majority of respondents who had achieved a positive change in their profit after the loan had attained a secondary level of education.

##### **4.4.2 Goal of Loan**

Loan is taken for productive activities but in some cases people use it as per their need (personal effects) like house construction/repaying, marriage, buying goods for household consumption etc. In some cases there arises a difficulty to repay back the loan if farmers do not have enough income sources. Forexample, members in Muyuni reported that the investment of money is quite higher than its output. Since majority of the farmers depend only upon agriculture, they do not have other income sources and sometimes the agricultural production will not be as desired by farmers. However for those who run small business said that they were partially benefited

from the loan, these people occupied 91.1%. This situation also noted in study done in UK by Fatchamps and concluded that, without financial assistance, rural farmers cannot cope with temporary cash flow problems. Table 4.4 shows different goal of loans according to their Client's purposes.

**Figure 4.3: Goal of Loan**

<b>Purposes of the loan</b>	<b>Respondents</b>	<b>Percent</b>
Buying Shamba	1	2.2
Personal Effects	1	2.2
Repaying House	2	4.4
Running for Small Business	41	91.1
<b>Total</b>	<b>45</b>	<b>100.0</b>

**Source: Field Data**

#### **4.4.3 Income Increment and Business Expansion**

All 45 clients declared that loans have increased their income in many different ways. BRAC provides working capital loans, and by using these loans, they were able to invest in their businesses, make profit and expand/open new businesses.

Explaining the advantage of the loan available, one BRAC's client said:

*“The money I got from BRAC has assisted me to expand the chickens husbandry. I am now returning the loan of 1,000,000/= Tshs and I believe I will keep on expanding”*

Generally, production has increased. Clients stated that the loans have assisted them in increasing production which in turn increased their income and led to the expansion of businesses. Nichols in his study from China realised the same thing that, participation of poor in MFIs program had led to positive impact in the life.

Those who engaged in this program, their income have increased, spending on educational and health have increased hence improved their standard of living.

#### **4.4.4 Employment**

An increase in income is not automatically related to an increase in the number of employees. Clients explained that an increase in the number of employees depends on many factors and not income only. Most clients still have retained the same number of employees as when they started accessing MFI's services. Explaining why there is no an increment in the number of employees, one respondent said that:

*“I run this business as a family business, my children are enough in assisting me in the business and so there is no need of increasing employees. I will think of doing that may be when I am in a stage of getting 3,000,000/= Tshs, but not now. And by then I will have to open another business.”*

Although this client had not employed someone outside of the family, the observation that some of the family members assist is an indication of employment creation.

### **4.5 Findings Related to the Second Objective**

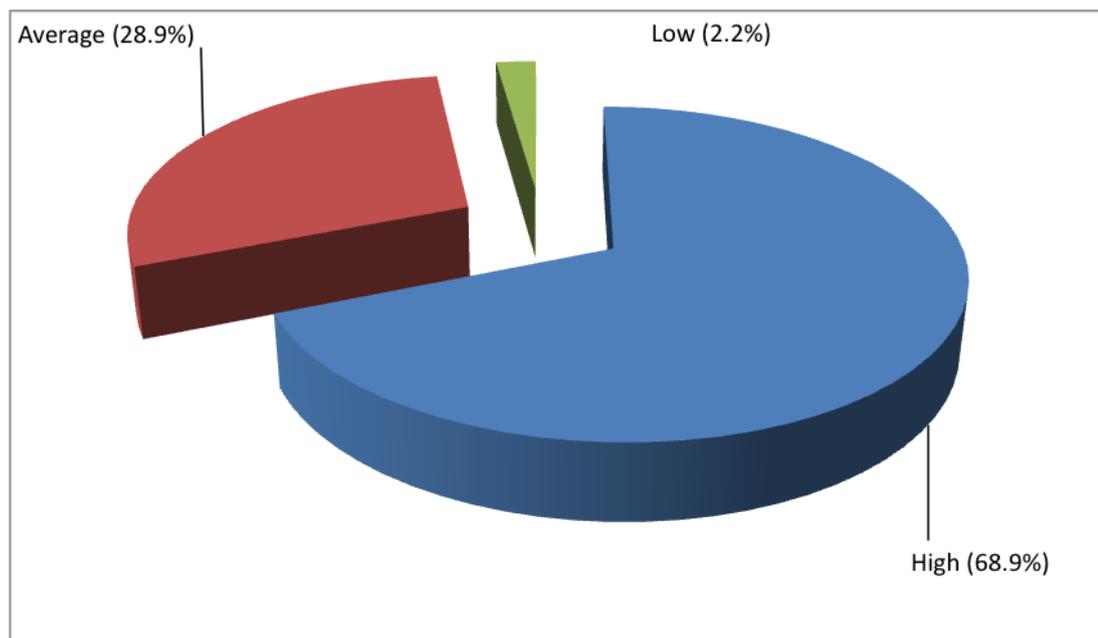
The second objective is about the conditions set by MFIs for credits if they favour the rural farmers

#### **4.5.1 Loan Interest**

It is recognised that BRAC has only two interest loan cycles on weekly basis. So there are two types of loans payment rates with different weekly periods. For those loans which are supposed to be paid within 20 weeks are imposed 13% weekly and those loans which supposed to be paid within 40 weeks are imposed 25% weekly.

Again all staff questionnaires say that Loans offered by BRAC are mainly in the form of short-term working capital. 10% of loan amount is deducted as loan security. After full repayment of loan, member can withdraw her loan security deposit. Again 1% of loan amount is deducted as loan appraisal fee so it is not refundable.

68.9% of 45 clients indicated that, getting loan is very expensive since the interest rate that the borrower has to pay the lender is very high. There are other direct and indirect costs incurred by the clients on loan. These costs include admission fees, loan appraisal fee and the loan security. All these add to the cost of obtaining the loan. In a study conducted by Kessy & Urio, they revealed this bad situation, they noted that, clients of MFI complained about high interest rate charged, the weekly meeting was pointed out as barrier as the time spent in weekly meeting could be used to other productive activities. The study recommended MFI to lower its interest rate, increase grace period and provide proper training to MSEs. Figure 4.3 illustrates.



**Figure 4.4: Classification of Loan Interest to Clients**

**Source: Field Data**

#### 4.5.2 Grace Loan Period

Again 51.1% of 45 clients wrote that the grace period is very low. It is a one week later after loan disbursement. This was indicated by MSEs as a short period especially for those who are supposed to pay within six months. Also the weekly repayment of interest and part of the principle of the loan usually limits many MSEs from growth. Table 4.4 shows details.

**Table 4.4: Grace Loans Period**

<b>Satisfaction Ranks</b>	<b>Respondents</b>	<b>Percent</b>
Low	23	51.1
Average	16	35.6
High	6	13.3
<b>Total</b>	<b>45</b>	<b>100.0</b>

**Source: Field Data (2013)**

#### 4.5.3 Loan Size

The BRAC's loan sizes ranges from Tshs 175,000 to Tshs 5,000,000. Table 4.6 shows that, 31.1% of 45 Clients lie on 175,000 to 300,000 Tshs. This range is kept for new borrowers. Clients of this range declared that the starting amount of loans of 175,000 Tshs for new borrower is so small; this amount was set in 2006 when BRAC started its operation in Zanzibar. The value of Tshs 175,000/= in 2006 is not the same today. 46.7% were in between 300,000 to 600,000 Tshs. And the remaining of 22.2% are in the range of 600,000 to 1,000,000 Tshs. No one was above this range.

**Table 4.5: Amount of Loans Taken**

Amount in Tshs	Respondents	Percent
175,000 - 300,000	14	31.1
300,001 - 600,000	21	46.7
600,001 - 1,000,000	10	22.2
<b>Total</b>	<b>45</b>	<b>100.0</b>

**Source: Field Data**

The findings revealed that the process of application for loans starts with small amount and after repayment the client can apply for next higher amount. This process was observed to be a limiting factor for those customers who needed a large amount right from the beginning. Most of the visited MSEs indicated that source of funds is a big problem and when asked why, as there are institutions offering loans, one client responded that:

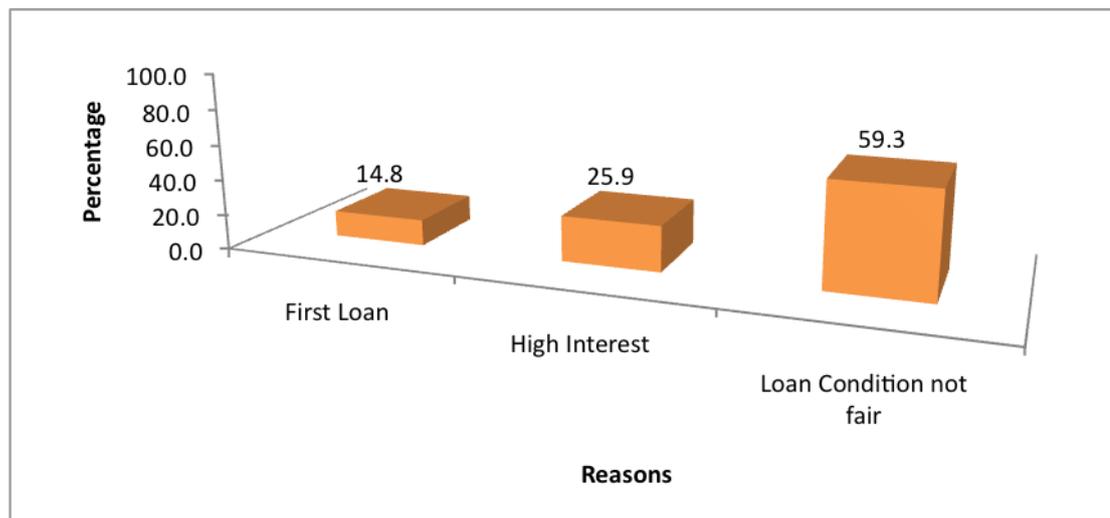
*“When I joined BRAC I thought I will be able to get any amount I needed, but that was not the case, as a new member has to start from the stage of 175,000/= and keep graduating until the level of 5,000,000/=. This takes so long to get enough funds for big loan seekers.”*

This is true because it takes an unnecessarily long time for those seeking a large loan to obtain enough funds to meet their needs. In addition to the time taken to receive large loans, the clients also raised concerns about the time frame from the receipt of the loan to the time of starting repayment, which is just one week after the disbursement of funds in most cases.

#### **4.5.4 Loans Conditions**

All Clients responded that some conditions of borrowing more loans are not satisfactory. 14.8% of 45 Clients said that, they unsatisfied because of first loan's

block, while 25.9% unsatisfied because of high interest rate and 59.3% because of loan conditions of MFI were not fair. This was also observed by Chijoriga, in her study, she revealed that, MFIs in Tanzania have lack of participatory ownership and many are donor driven. Figure 4.5 shows the reasons of unsatisfaction for loans conditions.



**Figure 4.5: Reasons of Unsatisfaction for Loans Conditions**

**Source: Field Data**

#### **4.6 Findings Related to Third Objective**

The third objective is about the impacts of MFIs in delivering service in rural society

##### **4.6.1 Saving for Clients**

It was seen that there has been an increase in income of cooperative members since they joined in a BRAC. The BRAC has contributed significantly on the income level of rural farmers. Principally it functions mainly as a rural development bank by providing different credit to its member groups. From the findings it can be said that the contribution of BRAC is significantly high to increase in income. Table 4.6 shows Clients before and after the loan. Before the loan, some Clients were not able

to save any amount where only 25 members were able, however, those who were able they managed to save 20,000/= minimum and 50,000/ max. But after the loan all 45 Clients are able to save.

The value of Standard deviation shows how much variation or dispersion exists from the average (mean). Saving before Loans the value was 8103.5 and saving after loans the value was 10471.2 this indicates that the data points tend to be very close to the mean which implies the amount of saving between the client was almost on the same distribution.

**Table 4.6: Saving for Clients**

<b>Saving</b>	<b>N</b>	<b>Minimum</b>	<b>Maximum</b>	<b>Mean</b>	<b>Std. Deviation</b>
Saving Before Loans	25	20,000	50,000	36,400	8103.5
Saving After Loans	45	30,000	60,000	40,111	10471.2

**Source: Field Data**

#### **4.7 Findings Related to the Fourth Objective**

The fourth objective concerns with constraints faced by the MFIs in the delivery of credits to the rural farmers

##### **4.7.1 Constraints and Future Prospects of BRAC**

It was explained by all 5 staffs that: The poor state of the infrastructures, especially rural roads, was pointed out as the main reason why BRAC fail to operate efficiently and effectively in rural areas. This constraint was also revealed by Kuzilwa and

Rweyemamu's study, they pointed out that, poor infrastructure of the MFIs led to high transportation costs, which increased the transaction costs in credit procurement, and disbursement and this ultimately hindered the effectiveness of the credit programmes. This happened because most of borrowers lived in rural areas, far from credit offices. Also it was answered that there are some clients fail to repay the loans according to agreed instalments, when this situation happens other members of their groups concerned are responsible for repaying the instalment.

All 5 staffs further concluded with different ideas, one staff, the BRAC's manager indicated that: According to the 2012 report given by Consultative Group to Assist the Poorest (CGAP) for BRAC, there was a slight decrease in the repayment rate from 100% in year 2006 to 99% in year 2012. As shown in table 4.7 below:

**Table 4. 7: Repayment Rates of BRAC**

Year	2006	2007	2008	2009	2010	2011	2012
RR <sup>1</sup> (%)	100	100	100	99.8	98.9	99.8	99

**Source: BRAC's Report, 2012**

The decline was identified as being due to problems such as socio-economic and harassment from local government authorities (the majority of MSE owners operate in undesignated premises and often have their businesses demolished by these authorities). The manager concluded by advising that; the Zanzibar Government to monitor these bad impacts so as to increase the business activities within the country.

---

<sup>1</sup>RR repayment rate

Other 4 staffs answered that, the Zanzibar Government should improve infrastructures and to introduce trade exhibition to their micro and small businesses in order to expand the MSE's market coverage.

About their BRACs future prospects, they all indicated that, after a time they want to see Zanzibar and Tanzania in particular are free from exploitation and discrimination where everyone has the opportunity to realise their potential. This future will be obtained through empowering people and communities in situations of poverty, illiteracy, disease and social injustice.

#### **4.8 Constraints and Future Prospects of Clients**

Regarding future prospects, 90% of 45 Clients indicated the plans to expand their business in the future, and mentioned MFIs to be their prospective source of capital. Despite the achievements, MFIs' clients urged MFIs to make improvements like improving the training/technical advice, increasing time for repayment and grace period, and reducing interest rates. It was further observed that these clients who wished to expand their business in the future were in the age group of 25 to 40 years and had completed a secondary level of education. With regard to the constraints in running a business, but all 45 Clients pointed out lack of continued business support and training as the major constraint. Even with the training provided by MFIs in some cases, it did not meet expectations of recipients. As the case of BRAC.

Generally, all clients felt that some regulations, including interest rate set by MFIs, did not favour low-income earners. The interest rates were claimed to be too high up

to 25% per year, there were other non-refundable fees to pay before securing the loan such as admission fee and loan appraised fee. They concluded that the interest rate and loan amount were constraints to their businesses. All these constraints made it difficult for them to generate enough profit for rapid growth.

#### **4.9 Performance of BRAC**

BRAC is playing a significant role in fighting poverty. BRAC has moved from donor dependency to an institution that is able to meet all its operational costs using its own internally generated resources over the past three years. Clients visited have proved that they are benefiting from the services offered by the institutions and that is why they are still BRAC's clients. Sometimes clients quit and then come back to BRAC.

When asked why they do that, one client responded that:

*“Sometimes I just get tired of the weekly meetings and compulsory savings, or I am in need of money and I know I have my savings, so I quit and get my savings back. After sometimes I re-join the group and start afresh”*

BRAC have brought positive change in women's participation and found greater potentialities of leadership development and increase in decision-making capability. Participation of women in such programs has been helpful to lessen household financial strain and have been a tool to empower rural women in decision making as regards to their financial matters. Therefore, it is very important to make sure women are involved in mainstream development activities. However it is also very important to make sure their workload does not get increased.

Despite of BRAC's performance on fighting to poverty, it has some limitations, all 45 Clients declared that the interest rates have been observed to be a serious problem,

they advised to the Zanzibar Government to form Regulatory Authority aiming to foresee and regulate credits offering and interest rates charged as cost of capital for loans funds sources from finance institutions. Again, they advised that BRAC would be flexible by raising the minimum base to reflect changes in the value of money over time. Also BRAC should increase the grace period and reducing the frequency of repayment so as to give them enough time of making profit before repayment. And BRAC should organise regular business training for them so as to gain business skills in their business activities.

## **CHAPTER FIVE**

### **5.0 SUMMARY, CONCLUSION AND RECOMMENDATIONS**

#### **5.1 Introduction**

This chapter draws a conclusion and recommendations of the study. The conclusions are based on the findings of each chapter, while the recommendations are the actions to be taken to improve the performance of Microfinance Institutions toward poverty reduction.

#### **5.2 Summary of the Main Findings**

Generally it has been observed that, MFIs have changed the life of poor people in a positive way. MFIs' clients have increased their incomes, increased the capital invested and therefore expanded their businesses. These are the indicators of achievements in their business activities. To a large extent MFIs operation in Zanzibar has brought about positive changes in the standard of living of people who access their services. Although some of the clients have not benefited, most MFIs clients have benefited positively. Despite the achievements of MFIs clients, most of them complained that, the interest rates charged by MFIs were very high.

The surveyed MFIs conducted a pre-lending training programme, but it was further observed that, the training was provided by loan officers who were not experts or practitioners in the area of small business. The training concentrated more on familiarising the clients with loan terms and conditions rather than providing small business skills. This practice may build up the spirit of loan repayment but does not

influence business growth. From the study done by Kuzilwa and Rweyemamu, they observed that, the enterprises whose owners received business training and advice, performed better than those who did not receive training. Clients also mentioned that, the required weekly reporting to the MFIs office was very high (one day in every week where they spend almost the whole day). This consumed a lot of productive time and hence reduced the time they could concentrate on other productive activities.

### **5.3 Implications of the Findings**

It was revealed from the study, the interest rates that MFIs charge make loans more expensive. When interest rates are high, that means fewer people and businesses can afford to borrow. This lowers the amount of credit available to fund purchases, slowing consumer demand. At the same time, it encourages more people to save (if they can) because they receive more on their savings rate. Higher interest rates also reduce the capital required to expand businesses, strangling supply. This reduction in liquidity usually slows the economy down. Also the grace period had a larger impact on clients with higher discount rates. Delayed repayment encourages more profitable, though it is riskier investment. It was revealed that the number of grace period clients still have not repaid more than a year after the loan disbursement date. The top three causes of poverty to any country of the world are lack of education, unemployment and the high cost of health insurance.

### **5.4 Conclusion**

By comparing with the general research objective of this study with the findings, it was revealed that, there is very slightly MFI's contributions to poverty reduction in

South District of Zanzibar though only one MFI was chosen because of limit of resources such as money and time. Although client outreach is increasing, with sub-branches opening in almost all regions of the Zanzibar, most of MFIs activities remain in and around urban areas.

It was observed that the MSEs whose owners received business training and advice from MFIs, performed better than those who did not receive training. The study show the same results as the Kuzilwa's study done in 2002. This surveyed MFI (BRAC) does not provide business skills. It was further revealed that poor infrastructure of the MFIs led to high transportation costs, which increased the transaction costs in credit procurement, and disbursement and this ultimately hindered the effectiveness of the credit programmes. This happened because most of borrowers lived in rural areas, far from credit offices. As indicated by all questioned staffs of surveyed MFI. This result matches with Rweyemamu's study done in 2003.

From the above evidence, it was found that there was a strong need for MFIs to study the existing situation of poverty in Zanzibar and see to what extent their operations will contribute to poverty reduction in the country. From this study, recommendations were made to policy makers so as to find further alternatives through which private financial services could be offered to the low income earning population or rather restructure the existing conditions for reducing poverty.

## **5.5 Recommendations**

The following recommendations are put forward in order to improve operations of MFIs.

1. Up to now there is no regulatory authority to foresee and regulate credits offering and interest rates charged as cost of capital for loans funds sources from finance institutions. The regulatory authority will be responsible to safe guard the interest of all borrowers and lenders that build strong independent economy and development sustainably.
2. MFIs should restructure the existing conditions for reducing poverty by considering the possibility of increasing the grace period and reducing the frequency of repayment so as to provide for clients with long term loans turn to businesses such as farming.
3. The poor state of the infrastructure, especially rural roads, was pointed out as the main reason why MFIs fail to operate in rural areas. In addition to improvement of infrastructure the Government of Zanzibar, in collaboration with MFIs, should introduce trade exhibitions to their micro and small businesses in order to expand the MSEs' market coverage.
4. MFIs should restructure their training contents to include improving their clients' business skills. They should organise regular business training for their clients and qualified training institutions should conduct this.
5. Regarding the issue of small base loans, the MFIs should be flexible by raising the minimum base to reflect changes in the value of money over time.
6. In order to have MFIs as the tools for participatory development processes, there is need that it becomes a permanent agenda for people to discuss on how to improve MSE's activities for their livelihood promotion.

7. Along with the saving and credit facility other employment oriented training programs should also be introduced to the rural farmers in order to boost up their economic productive ability. Special emphasis should be given on agricultural training since majority of the people are dependent on agriculture.

## **5.6 Limitations of the Study**

The process of collecting data was not be smooth, some of the problems happened which will be beyond the control of the researcher. The following limitations were encountered:

- (i) **Access to data:** Almost all the respondents visited were reluctant to provide all the information's requested by the researcher as they treated some of the information as confidential.
- (ii) **Reliability, Availability and Quality of data:** Researcher faced some problems concerning reliability, availability and quality of data because storage and accuracy of data was questionable due to contradicting reports and information. Some of informations were inaccurate and unreliable.
- (iii) **Financial Resources:** Another limitation of the study was the financial resources, due to the limited financial resources the researcher had, it was difficult to cover all Microfinance institutions operated in Zanzibar as the result the researcher opted for the BRAC only.

## **5.7 Delimitation of the Study**

This study was confined to the Contributions of MFIs in reduction of poverty at South District in Zanzibar, thus data was controlled by the researcher when they

were collected. Both primary and secondary sources of data as well as different instruments of data collection including questionnaire, interview, observation, and documentary were consulted to balance validity and reliability of data. And assurances were given to respondents on confidentiality of information required by the researcher. These motivated respondents to provide the information required in the study and enable the researcher to collect valid and reliable data on time. For those data which were not easy to be accessible at all, researcher tried to minimise their use as much as possible in connection with the research.

### **5.8 Areas for Further Research**

1. As the interest rates have been observed to be a serious problem, there is a need to conduct a study to determine rates that would favour for the operating expenses of MFIs and at the same time facilitate the growth of their clients' business.
2. There is a need to conduct a comparative study between member based MFIs Savings and Credit Cooperative Societies (SACCOS) in rural areas. This would indicate to the Government on which institution to empower more than the other.
3. Further research is required to investigate on how the government has been empowering MFIs and as the results MFIs empower community in participatory development processes in rural and urban areas.

## REFERENCES

- Adongo, J. & Stork, C. (2005a). The microfinance gap: *Selected Issues for Namibia. Research Report 38*. Namibia: NEPRU.
- Amin (2003). “Does microcredit reach the poor and vulnerable?” Evidence from northern Bangladesh, *Journal of Development Economics*, Vol. 70 (1).
- Ayyagari, M., Beck, T., and A. Demirgüç-Kunt, (2003). “*Small and Medium Enterprises Across the Globe*” World Bank Working Paper WPS2127.
- Bamberger, M. ed, (2000). *Integrating Quantitative and Qualitative Research in Development Projects*, Washington D.C; The World
- Beck.T, Demirguc-Kunt. A and Levine R.(2005). SMEs, Growth, and Poverty: Cross- Country evidence. *Journal of Economic Growth*, Vol 10:3 197-227.
- Bhatt and Shui-Yan, (1998). The Problem of Transaction cost on group-based micro lending: an institutional perspective. *World Development*, vol.32.4, pp. 623-637.
- Buller, H. and Wright, S. (1990). “Intoduction: Concepts and policies of rural development”, in *Rural Development: Problems and Practices* (Edited by Buller).
- Chen, A.N. (1997), *Assessing the Impact of Microenterprise Servicee at the Individual Level*, USAID-AIMS Brief. No. 16
- Chijoriga, M. M. (2000) “The Performance and Sustainability of Micro Finance Institution in Tanzania” *Working Paper*.
- Chijoriga, M.M. and Cassimon (1997) “Micro Enterprise Financing: Is there a Best model?” in Rutashobya and Olomi (eds). *African Entrepreneurship and Small Business Management*, DUP Dar es Salaam.

- Chijoriga, M.M. and Cassimon (1999) “Micro Enterprise Financing: Is there a Best model?” in Rutashobya and Olomi (eds). *African Entrepreneurship and Small Business Management*, DUP Dar es Salaam.
- Coase, Ronald (1960) “The problem of Social cost” *Journal of Law and Economics* 3, p.1-44.
- Coleman, B.E. (1999), “The impact of group lending in Northeast Thailand”, *Journal of Development Economics*, Vol. 60 (1).
- Cook, P & Nixson, F (2000). “Finance and Small and Medium-Sized Enterprise Development”. *Journal of Developmental Entrepreneurs Inp*, Vol. 6 (I) April.
- Denise, F. Cheryl, B. & Hungler, B. (eds). (2001). *Essentials of Nursing Research Methods, Appraisal and Utilization*. New York: Baltimore.
- Fabozzi & P.P.Peterson (2006). “*Key Findings of the FinScope Survey in Namibia*”, Financial Management & Analysis, 2nd Edition.
- Fatchamp, M. (1997), “Trade Credit in Zimbabwean Manufacturing”, *World Development*, 22 Vol. 25, No. 5.
- Grande, O. T, (1984). “The role of Rural Credit Projects in Reaching the Poor: IFADs experience” In ILO (ed) *Group Based Savings and Credit of the Rural Poor*, Geneva.
- Harper, V.L. et al (1999). “Measuring Transformation assessing and improving the impact of Micro credit” *Paper Presented at Micro credit Summit meeting of Councils in Abidjan Cote de’Ivoire*, June.
- Hashemi, S., Schuler S. R. and Riley A. P. (1996). “Rural Credit Programs and Women Empowerment in Bangladesh” *World Development*, Vol. 24, No.4, pp635- 653.

- Hassan, K. M. and L. Renteria-Guerrero (1997) “The experience of the Grameen Bank of Bangladesh in community development” *International Journal of Social Economics*, Vol. 24 No. 12 pp. 1488-1523.
- Hirway, I. (2003) *Identification of BPL households for poverty Alleviation Programmes*, Economic and Political Weekly pp.4803-4808 in *Development Strategies and The poor ISS Readings (4202)*, The Netherlands.
- Household Budget Survey (HBS) 2009/10, Final Report of May, 2012.
- Hulme, D. and Mosley P. (1997). “Finance Against Poverty”, Volume 1. London and New York: Routledge. International Finance Corporation. (1994) “*Emerging Stock Markets*” Fact Book, Washington DC.
- International Finance Corporation (1994) “*Emerging Stock Markets*” *Fact Book*, Washington Dc.
- Johnson, S. and B, Rogaly (1997) *Microfinance and Poverty Reduction*, Oxfam (UK and Ireland).
- Kessy, S.A and Urio, F (2006). *The Contribution of Microfinance Institutions to Poverty Reduction in Tanzania*, Research Report No. 06.3 – REPOA, Mkuki na Nyota Publishers, Dar es Salaam.
- Kimenyi, Mwangi, S, Robert C.Wieland and J.D.Von Pischke (1998) “Strategic Issues in Microfinance”. *Contemporary Perspectives on Development Societies*, Ashgate Publishing Limited.
- Khandker (1998). “The Impact of Group-Based Credit Programs on Poor Households in Bangladesh: Does the Gender of Participants Matter”, *Journal of Political Economy*, 106 (5).
- Kothari, C.R. (2004) “Research Methodology” *Methods and Techniques*. H.S. Poplai, 2nd Edition.

- Kuzilwa, J. A. (2002) "The Role of Credit for Small Business Success: A Study of the National Entrepreneurship Development Fund in Tanzania" *A Paper Presented at the 6th Annual International Conference on Entrepreneurship and Small Business Development (ICAESB)*, White Sand Hotel, Dar es Salaam.
- Ledgewood, J. (1998), "An institutional and financial perspective: Sustainable banking With the poor", *Micro finance hand book, the World Bank, Washington D.C Ministry Of Finance (2000)*, "National Micro Finance policy", United Republic of Tanzania, Government Printers, Dar es Salaam.
- Lont, H and O, Hospes (2004) *Livelihood and Microfinance: Anthropological and sociological perspectives on savings and Debt*, Eburon Delft.
- Maanen, G.V (2004) *Microcredit: Sound Business or Development Instrument*, Voorburg, the Netherlands.
- Ministry of industry and trade of Zanzibar: *Small and medium enterprises development policy 2002*.
- Montgomery and J. Weiss, (2005) *Great Expectations: Microfinance and Poverty Reduction in Asia and Latin America*, ADB Institute Research Series No.63.
- Mosley, P (2001) "Microfinance and Poverty in Bolivia" *Journal of Development Studies*, Vol. 37, No. 4, pp. 101-132(32), April.
- Nalunkuuma, J. (2006) *Microfinance and Outreach: A case study of Soroti Catholic Diocese Integrated Development Organisation*, The Hague: ISS.
- Nichols (2004), Nichols, S., *A Case Study Analysis of the Impacts of Microfinance Upon the Lives of the Poor in Rural China*, RMIT University, Melbourne, 2000.
- Olomi, D and Chijoriga M (2001). Survey of SMEs in Tanzania Pitt, M. and S.

- Ondeng, P. (2000) "Handout for: International Workshop expanding the Frontier of Rural Finance" International Agricultural Centre.
- Pilipinas, B. S., (2002) "Notes on Microfinance" [http://www.bsp.gov.ph/archive/Regulations\\_2002/Circulars/notes.htm](http://www.bsp.gov.ph/archive/Regulations_2002/Circulars/notes.htm)
- Pitt, M. and S. Khandker (1998), "The Impact of Group-Based Credit Programs on Poor Households in Bangladesh: Does the Gender of Participants Matter", *Journal of Political Economy*, 106 (5).
- Qorinilwan (2005) Microfinance and Poverty Alleviation: *Achievements and Innovation of Grameen Bank (Banglades)*.
- Rahman, A, (1991). Micro-Credit Initiatives for Equitable and Sustainable Development: Who pays? *World Development*, Vol. 27, No.1, pp67-82.
- Roglay, B (1996) Microfinance Evangelism 'Destitute Women' and the Hard Selling of a New Antipoverty Formula, *Development in practice*, vol.6 (2):100-112.
- Rubambey, G. (2001) "Tanzania National Micro Finance Policy", *A Paper Presented at the 5th Annual International Conference on entrepreneurship and Small Business Development (ICAESB)*, White Sand Hotel, Dar es Salaam.
- Rweyemamu D.C; Kimaro M.P. and Urassa O. M. (2003) "Assessing Micro-Finance Services in Agricultural Sector Development:A Case Study of Semi-Formal Financial Institutions in Tanzania" *Economic and Social Research Foundation*.
- URT (1999), *National Poverty Eradication Strategy*, Vice-President's Office, Dar es Salaam.
- URT (2000), *National Micro Finance Policy*, Dar es Salaam.
- URT (2003), *Small and Medium Enterprise Development Policy*, Dar es Salaam.

Wangwe, S. and Semboja H. (1997) “Establishing Micro and Small Enterprise (MSEs) Research Programme”, *A paper presented to the workshop on Micro and Small Enterprise Research*, November, Dar es Salaam.

Wright and H. , S. (1990), Aldershot: Avebury Gower Publishing Company Limited.

Yunus, M. (1984) “Group based Savings and credit of the Rural Poor: The Grameen Bank in Bangladesh”, In ILO (ed) *Group based Savings and credit of the Rural Poor*, Genev.

Zanzibar Strategy For Growth And Reduction Of Poverty (Mkuza), July, 2007,Zanzibar.

## APPENDICES

### APPENDIX A: Conditions and Regulations of BRAC

Page 17

#### Regulation:

##### **Member Admission, termination, resignation:**

1. Admission to groups for female only whose land (including household) is not more than 3 acres, works for others enterprises, sale manual labor 100 days a year, have small business etc.
2. A member will be aged between 20 - 50 years.
3. Anybody who wants to be a member of a group has to be a permanent resident of that village / hamlet and her house has to be located within the fixed unit of the group. Regarding urban area a person has to be a resident of the area at least three years.
4. A new group can be formed with 15 members and subsequently will be increased up to 30 members. Each member in a group will select two names as proposed group leaders. They individually write two names and can include their own names along with another. After counting the names the most common name will be the group leader. The second common one will be the cashier of the group. Group leader and cashier will be changed every one year using same process.
5. Members must bring certificate from local street/hamlet / village leader and their photo must be attested by the street / hamlet / village leader in the admission time
6. Admission fee to the group is 1500 Tsh. and each year member has to renew her membership with a renew fee of 1000 Tsh.
7. After becoming a member, a passbook will be given. First passbook will be given with out any charge and for subsequent pass book the member has to pay 500 Tsh.
8. After admission all members will have to receive four weeks orientation course about the regulation of the group as well as the credit regulation. The orientation course will take place in the group – meeting place for first four weekly meetings.
9. In case of old age, physical disability, physical deformation, migration, and for special regions a member can withdraw her membership at any time.
10. If any member conducts any activities against the rules and regulations of group will be terminated from the group.

##### **Loan**

1. Member can apply for loan at least four weeks of regular attendance of weekly meeting. Attendance will be mandatory every week after disbursement.
2. For any kind loan, permission is required from the group. After resolution loan applications will be sent to branch office. The office has all rights to approve or reject the loan application. Under no circumstances member will claim loan as their entitlement

3. Loan and its service charge will be realized in equal weekly installments during weekly meeting from the next meeting day of loan disbursement.
4. Loan service charges will 22% flat for 1 year loan and 12% flat for six months loan.
5. 1% of loan amount will be deducted during sanctioned amount will be charged as loan appraisal fee.
6. 10% of loan amount will be deducted during disbursement as loan security deposit (Refundable. During loan period member will not be allowed to withdraw this money. After full repayment of loan member's can withdraw their loan security deposit, it is to be noted that there is no interest provision of this security
7. On time repayment is a must for retaining membership and obtaining further loans.
8. The borrower must use the loan amount only for business and generating purpose and can not be used other than the business/project which was mentioned in the loan application form
9. There will be no relationship between profit and loss of project where borrowed money is used and with the loan repayment. Member must pay her loan installments on time without showing any cause.
10. In case of any installment missed by any member, other members of her small group will be responsible for repaying the installment.
11. The members who have loans from BRAC can not take loan from other organizations / institutions in the period.
12. All the loans will be approved by Area Manager
13. To receive the sanctioned loan, members will come to the respective branch office with their National ID card and take loan from office by signing the loan disbursement sheet.
14. The borrower must pay the whole loan amount with interest by installments within the specified time. If for any reason the loan is not paid back in the fixed time, it will automatically be transferred to delayed loan and the service charge of the due loan will again be applied.
15. If a member does not pay the loan within contracted period the loan is transferred to delay loan, the membership to the member will be canceled and other regulation will be followed to retrieve the amount.

**Source: BRAC's Conditions**

## APPENDIX B: ENGLISH HOUSEHOLD QUESTIONNAIRE

Dear Respondent,

My name is Yussuf Haji Haji. I am doing a Master of Business Administration at Open University of Tanzania. I am currently doing a research on THE CONTRIBUTION OF MICRO FINANCE INSTITUTIONS TO POVERTY REDUCTION as partial fulfillment of my Master course. I humbly request you to fill this Questionnaire so that I can get reliable data that will make my assignment successful. I promise that the data that you are going to fill in will be confidential as the report will provide information in its aggregate and we will both benefit from this research.

### A: GENERAL INFORMATION

A1	Date interview	
A2	Place of interview	
A3	Name of the respondent (option)	
A4	Shehia	

### B: DEMOGRAPHIC INFORMATION

Sex	Marital Status	Education Level	Age	Occupation

**Sex:** 1=Male; 2=Female

**Marital Status:** 1=Married, 2=Widowed, 3=Separated, 4= Single (Never married)

**Education Level:** 1= none, 2= Primary, 3=Secondary (O'Level), 4= Secondary (A'Level)

**C: RESEARCH INFORMATION**

1. Have you ever taken the loan?

Yes ( )

No ( )

2. If Yes, How much loan have you taken?

➤ Tshs. 175,000 to Tshs.300,000 ( )

➤ Tshs. 300,001 to Tshs. 600,000 ( )

➤ Tshs. 600,001 to Tshs. 1,000,000 ( )

➤ Above Tshs. 1,000,000 ( )

3. Have you satisfied with amount of loan you get?

Yes ( )

No ( )

4. If no, give reasons: .....

.....

5. Does the rate of interest of your loan is

High ( )

Average ( )

Low ( )

6. Does the grace period is

Low ( )

Average ( )

High ( )

7. What did you do with the loan you have taken?.....

.....

8. Have you found any changes from your level of economy after taking the loan?

Yes ( )

No ( )

9. If yes, what kind of changes did you find?

Specify:.....

.....

10. Are you satisfied from the achievements you get?

Yes ( )

No ( )

11. If No, why? .....

.....

12. How much amount of money did you save per month before getting loan?

.....

13. What suggestion do you recommend for the effective operation of your Institution?

.....

.....

**THANK YOU FOR YOUR THOUGHTFUL RESPONSE.**

**SWAHILI QUESTIONNAIRES****DODOSO KWA WANACHAMA**

Mpendwa mdodoswaji,

Mimi ni Yussuf Haji Haji nasomea shahada ya pili katika fani ya Biashara, katika Chuo Kikuu Huria cha Tanzania. Nafanya utafiti juu ya **MASHIRIKA YA MIKOPO YANAVYOSAIDIA KUPUNGUZA UMASIKINI** ili kuweza kumaliza masomo yangu. Kwa heshima zote naomba ujaze dodoso hili ili nipate maelezo muhimu kwa ajili ya kukamilisha kazi hii. Naahidi kwamba maelezo utakayotoa yatakua siri baina ya mimi na wewe kwani maelezo nitayaandika kwa ujumla wake na sio kwa mtu mmojammoja na nawahakikishia kwamba sote tutafaidika na utafiti huu.

Tarehe: .....

**A MAELEZO YA JUMLA**

- 1) Jina la Wilaya.....
- 2) Wadi ya .....
- 3) Jina la Shehia .....
- 4) Hali ya kindoa: uko na ndoa ( ) huko na ndoa ( )

**B MAELEZO BINAFSI**

- 1) Jina(si lazima): .....
- 2) Miaka: .....
- 3) Pahala unapoishi: .....

4) Jinsia: Mume ( ) Mke ( )

5) Kazi: .....

6) Kiwango cha elimu: .....

### **C MAELEZO KUHUSU UTAFITI**

1) Wewe umeshachukua mkopo?

Ndio ( ) Hapana ( )

2) Kama ndio kiasi gani cha mkopo?

- Kutoka Tshs. 175,000 mpaka Tshs.300,000 ( )
- Kutoka Tshs. 300,000 mpaka Tshs. 600,000 ( )
- Kutoka Tshs. 600,000 mpaka Tshs. 1000,000 ( )
- Zaidi ya Tshs. 1000,000 ( )

3) Mkopo ulochukua ndicho kiwango ulichokitaka?

Ndio ( ) Hapana ( )

4) Kama hapana ni kwa nini? Elezea

.....  
 .....

5) Je riba ya mkopo uliochukua ni

- Kubwa ( )
- Kiasi ( )
- Ndogo ( )

6) Muda wa kuanza kurejesha mkopo ni

- Mdogo ( )
- Kiasi ( )

➤ Mkubwa ( )

7) Umeufanyia nini mkopo wako?

.....  
.....  
.....

8) Je umebadilika kiuchumi baada ya kuchukua mkopo?

Ndio ( ) Hapana ( )

9) Kama ndio, mabadiliko gani?

.....  
.....

10) Je unaridhika na mafanikio unayoyapata?

Ndio ( ) Hapana ( )

11) Kama hapana ni kwanini?

.....  
.....

12) Ni kiwango gani cha fedha unaweka hakiba kwa kila mwezi?

.....

13) Una ushauri gani kwa ushirika hususan katika masharti waliyoweka kwenye mikopo?

.....  
.....  
.....

**ASANTE KWA KWA KUWAJIBIKA**

**INTERVIEW QUESTIONS FOR INSTITUTION'S STAFFS**

1. What kind of services are provided by your Institutions?
2. How many loan members are there in your Institution?
3. Who are more favorable?
4. Why, Explain
5. What are the conditions for taking loan?
6. What is your loans interest rate?
7. Is there any other cost for taking the loan?
8. After taking the loan, what time for starting repayment?
9. What are the constraints faced by your Institution at the time of delivering credits?
10. What is the provision for the one who is not in a position to pay back loan?
11. What suggestion do you recommend for the effective operation of your  
Institution especially in the granting credits to rural farmers?

**THANK YOU FOR YOUR THOUGHTFUL RESPONSE**