Micro Finance Institutions (MFIs) Practices and Poverty Alleviation in Tanzania

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Abstract: Tanzanian's Poverty Reduction Strategy (PRS) focuses among other efforts at reducing income poverty, improving human capabilities, survival and social well-being and containing extreme vulnerability among the poor. In this context access of households and firms to physical and financial resources is etremely crucial. For the majority of Tanzanians who are poor, without access to formal financial institutions, access to micro finance services is a viable alternative in an attempt to reduce poverty. Micro finance institutions (MFIs) offer the poor, the possibility of managing scarce resources more efficiently and taking advantage of investment opportunities for economic returns. Access to finance services may contribute to increased income generation and thus achievement of higher standards of living at household levels while at enterprise levels it can facilitate the pursuit of income and firms growth. The operations of MFIs need therefore to have greater outreach particularly where the poor are concentrated, i.e. in the rural settings. At the same time services ought to be sustainable in order to have impact on poverty alleviation.

INTRODUCTION

Poverty is a multi-dimensional concept that includes income and non-income human development features such as access to education, health, nutrition, safe water and social welfare services. Strategies to combat poverty are several, one among them being raising returns on the poor's assets and encouraging non-farm employment. This paper focuses on the postulate that increasing poor access to micro finance will contribute towards poverty alleviation.

The contribution of MFIs to poverty alleviation in various dimensions in a country like Tanzania is influenced by a number of factors. These include the types of the institutions, objectives and the MFI practices. The practices have been identified as selection procedures, repayment enforcement, savings forms, lending conditions, outreach including location and sustainability strategies. The practices and the donors/owners' objectives have bearing on the poverty alleviation orientation of the MFIs.

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Most of the MFIs provide small loans to clientele in urban and peri-urban areas. Women form the majority of their borrowers. Most of them have records of high repayment rates. However the outreach is very limited covering only about 0.0075 percent of the country's population of about 34.5 million people. The micro finance industry is therefore at subsistence level in the country with the impact on poverty alleviation being minimal especially because the rural areas have not been reached. Best practices to deliver MFI services to the rural poor need to be developed.

Micro-finance NGOs adopt credit delivery modalities that are based on group solidarity. These procedures lower transactions costs of borrowers screening and loan losses. However other poor without social capital and character reference (unemployed youths/graduates) to join the groups are excluded from practices. At the same time loan sizes are uniform to all borrowers regardless of differences in financial needs and business cycles. This serves more the interest of lenders than borrowers and less the positive effects on poverty reduction. More flexibility in micro lending practice is required in order to broaden and depeen financial intermediation for the poor.

It has been shown that the poor do save in this country. The MFIs especially savings and credit cooperative societies (SACCOs) and MFIs have raised substantial savings from the poor. This avails an opportunity that can be made use of by the conventional financial system to enhance linkages between formal financial institutions (FFIs) and MFIs, which at the moment is not being exploited. This will in the long run lower the dependency on eternal funding of NGOs, contribute to financial deepening and eventually reduce the poverty level as more people get access to financial capital base.

Substantial money and energy worldwide has been invested with the good intention of poverty alleviation in poverty stricken countries like Tanzania. Much of the support services have gone to micro and small enterprises as they are thought to play a key role in poverty alleviation. For example the World Bank alone lent over US $ 3 billion between 1973 and 1989 to foster a healthy growth of the MSE sector (Sarder, 1997). At the same time a number of outstanding micro-finance institutions (MFIs) have been established as a way of cutting the known vicious circle of poverty. Micro finance addresses the financial needs of the major sectors in population. They are primarily facilitators than creators of the underlying economic activities that lead to widespread economic prosperity. Micro finance services are financial in nature and differ from other safety-net arrangement such as food handouts, cash transfer, etc. In Tanzania, it has been broadly acknowledged that micro finance contributes to poverty reduction (URT (a) 2000).

The established MFIs enable the poor and especially poor households and micro and small enterprises (MSE) to have access to credit. This is because the poor and MSE lack access the formal financial institutions (FFIs). A number of constraints faced by the poor and MSE operators looking for credit in FFIs include lack of collateral, high interest rates, too high indirect cost of borrowing (bribes and follow-up costs) and preparation of project write-ups (Shayo- Temu, 1998). Other problems are liquidity shortages (business cycles not matching with terms of loans), corruption and personality clash with lending officials (VPO and UNDP, 2000).

On the other hand FFIs associate lending to the MSE with too high transaction costs to process and monitor the small volumes of credit normally demanded, lack of track records upon which the credit rating can be based and high risk customers. Moreover, most of the FFIs lack the innovative ability to design and offer appropriate products to the MSE and poor households (Shayo & Temu, 1998).

Non governmental organizations innovated modalities for offering financial services to poor households and MSE. They started to operate at small scale in delivery of credit (with savings elements) by utilizing the strengths of the poor while at the same time working upon against their weaknesses. The delivery procedures include the self-selection and screening of the borrowers, group lending and use of group solidarity/pressure for timely and full repayment, close monitoring and well established management information system, swift transactions (very short time between application, approval and eventual receipt of the loan). Savings in different forms such as insurance against loan, fund raising etc. has been mandatory component of the schemes. It is now widely recognized that even the very poor can save. MSE and poor households regardless of poverty level are treated as clients and not beneficiaries of the NGOs. The handling of clients/borrowers is therefore with business mindset backed by social welfare enhancement motive. This has been referred to as social-market approach to financial services delivery to the MSE (Shayo&Temu, 1998a). The NGOs that concentrated their services in the credit and savings services for the poor households and MSEs are in this paper referred to as MFI-NGOs. Other institutions offering micro finance services to the poor include specific departments of FFIs, government's schemes either operating autonomously or under designated ministries. In Tanzania, these include Small Industries Development Organization (SIDO), Akiba Commercial Bank to mention but only a few.

The most outstanding MFI-NGOs at global level have been the Grameen Bank of Bangladesh (Hashemi, 1997), BancoSol of Bolivia (Glosser, 1994), Bank Rakyat Unit Desa System of Indonesia (Boomgard and Angell, 1994). In Africa and particularly in East Africa, Juhudi Credit Scheme of K-REP Kenya is one of the most successful MFI-NGOs in terms of providing micro financial services to poor entrepreneurs (Mutua, 1994).

Juhudi has been reckoned for being able to provide credit to the poor on commercial basis. K- REP through the Juhudi scheme has recently become a bank.

The Grameen Bank (GB) of Bangladesh (started by Professor Yunus at University of Chitaggong on an experiment basis in 1976) has won a reputation of Bank of the Poor. GB has great outreach covering almost 50% percent of the villages in the country in 1995. It has extended credit to over 3 million poor women in Bangladesh and the repayment rate has been 100%. It has been reported by many that most of the GB clientele have been empowered not only economically but also socially and their health status has improved.

Most of the success has been attributed to the modalities of credit delivery and follow up. Credit delivery model has been mainly group lending in GB although in other MFIs like the BancoSol and Bank Rakyat individual lending has being dominant. Committed and innovative management, motivated and dedicated staff to poverty alleviation, long term and continuos donor support, government political will to eradicate poverty are among other factors that have immensely contributed to the success and also sustenance of the services of the MFI over a long period. Whether similar evidence on the relationship between MFIs and Poverty alleviation in Tanzania could be found is a subject of this study.

STATEMENT OF THE PROBLEM

The Tanzanian government recognizes the need for micro financial services to the poor as one of the ways towards poverty alleviation. As stated in the National Poverty Eradication Strategy (1998), the long-term objective of the government is to reduce abject poverty by 50 % by the year 2010 and eradicate poverty by the year 2025. In order to realize this goal there is need for developing financial system that can reach the majority of the poor in the rural areas. The system has to be able to mobilize savings and at the same time deliver credit services to the poor. It is for this reason that the government has been seriously supporting micro finance programs and schemes that are in pursuit of this objective.

The growth of MFIs in Tanzania, particularly the non-governmental ones gained momentum from early 90's. There are about 100 MFIs in the country at the moment. Most of the MFIs are donor-funded although local members solely own some. Some of the MFIs in the country lack the capacity to deliver the expected services. Only a few of these MFI are not branches of international NGOs. They therefore have practices that have to be tailored to the needs and objectives of the parent NGOs. Those that are owned by private individuals have the objective of ensuring that their activities and thus existence are sustained, thus the profit generation motive is implicit in their operations. The MFIs that are member owned are guided by regulations that have been agreed upon by all the members. Due to these differences there are differences in their services delivery practices.

Elsewhere in the literature, it has been asserted that the modalities of the operations in Tanzania are similar. They all except a few use the group lending approach in the delivery of credit services

(VPO and UNDP, 2000). Our contention is that there are differences in the credit practices of the various MFI depending on the objectives of the financiers, the ownership and experience gathered and possessed by the various MFIs. Most of the documented practices of the MFI concentrate on the evaluation of the MFIs, in particular financial sustainability (Chijoriga, 1999). Other important elements such as client selection criterion, repayment enforcement, approaches to savings mobilization strategies to expand outreach and measures towards sustainability remain un-researched and thus undocumented. The exploration of the linkage between MFIs practices and poverty alleviation in the country remain unquestioned. Therefore the objective of this study was to identify the different MFIs' practices and examine how they contribute towards poverty alleviation.

THE STUDY METHODOLOGY

Most of the findings reported in this paper come from a study carried out in four regions, namely Dar es Salaam, Mbeya, Arusha and Mtwara. The study aimed at investigating how MFIs practices in the mentioned regions bear upon poverty alleviation particularly on women borrowers.

Two questionnaires were used in gathering the data. One questionnaire was sent and answered by the MFIs' staff. The senior/program credit officers who are most conversant with the MFIs practices and strategic objectives were requested to provide the information. A total of 13 MFIs were studied and all of them gave useful data. The second questionnaire was served to the clients who provided data to substantiate the institutional information of MFIs. Women borrowers in groups provided answers in the form of focus group discussions guided by the researcher. In total 87 MFI borrowers were interviewed. In brief the questions to the borrowers were aimed at finding out the effects of the borrowed funds on their enterprises in terms of reduced poverty level (increase of disposable income), creation of additional income generating activities and improvement in welfare i.e. increased expenditure on health, education and housing. In addition, a number of reports and studies on MFIs were reviewed.

REVIEW OF LITERATURE

The Status of Poverty in Tanzania

Poverty is a multi-dimensional concept. It is difficult to define it uniquely. In Tanzania poverty measures include both income and non-income human development features (PRSP 2000). The most common definition of poverty addresses the income dimension of poverty. In such definition poverty is defined as the inability to attain a minimum standard of living. Thus poverty would be measured by income (expenditure) level that can sustain a bare minimum standard of living. Based on the 1991/92 Household Budget Survey, around 27 % of the Tanzanian people were in households with total expenditure that was insufficient to obtain enough food to meet nutritional requirements. At the same time, about 48 percent of the households were unable to meet their food and non- food basic requirements. The various estimates for the year 2000 show that poverty levels are over 50 percent in Mainland Tanzania (URT,2000).

Column 3 in Table 1 shows the level of poverty in Tanzania using the Headcount Index (HI). The HI shows the proportion of the population defined as being poor i.e. those whose measured standard of living is less than the poverty line. It is obtained by dividing the number of poor by the total population in the area. Using the HI, majority of Tanzanians (about 51%) are living below the poverty line.

As correctly argued by Likwelile (2000), it is insufficient to conceptualize poverty in terms of income and expenditure. Health, life expectancy, access to clean water, gender balance, ones position in society etc. are other central dimensions of human welfare. That is poverty has to do with the general quality of human life. Thus issues of command over resources, utility and capability (avoiding hunger, illiteracy etc.) are all important in conceptualizing peoples' welfare. In this context, attention neeqs not only be directed at income and employment generation but education, health care, access to clean and safe water, housing and food security.

Progress in human development is measured through a measure of socio-economic progress called HDI (Human Development Index). HDI integrates life expectancy (longevity), literacy rate (knowledge) and income. It is an approximation for capturing the many dimensions of human progress i.e. how well resources are used in the advancement of human development. The lower the index, the lower the quality or efforts at enhancing human development. Column 2 of Table 1 gives the HDI estimates for various regions in Tanzania.

Table 1: *HDI and Headcount Index-for Tanzania*

Region	HDI index	(Headcount index)
Dar es salaam	0.658	20.5
Kilimanjaro	0.536	30.9
Arusha	0.533	47.2
Tanga	0.429	51.4
Iringa	0.425	56.6
Mwanza	0.420	46.9
Morogoro	0.41 I	55.8
Mbeya	0.405	42.2
Dodoma	0.399	66.2
Mara	0.388	51.2
Shinyanga	0.375	56.6
Ruvuma	0.358	42.5
Coast	0.348	38.5
Singida	0.347	72.0
Tabora	0.344	40.6
Kagera	0.370	41.5
Mtwara	0.319	66.3
Rukwa	0.288	79.6
Kigoma	0.265	83.5
Lindi	0.236	60.5
Tanzania	0.395	50.8

Source: Tanzania Human Development Report (1997), Semboja *et al.*, (2000)

From Table 1 it is apparent that the level of poverty measured by the two indices differs across regions in the country. Implications are that poverty alleviation measures with the target of increasing equal distribution of income and resources across the whole society must take into account the poverty differentials at regional levels and also individuals.

Studies on profiling of poverty have come with five categories of poverty with different distinctive features. These are the poorest, the poor, the quite poor, the OK and the wealthy individuals. Examples of each category are given in Table 2.

One notes form Table 2 that poverty denotes the condition of people who are unable to meet the minimum basic standards of human well-being as perceived in different societies around the world. Poverty involves a range of inadequacies in economic, social and human security capabilities. Indeed, some recent definitions have gone further to include issues of dignity (people's freedom), autonomy (ability to choose self-fulfilling and rewarding life styles). Thus poverty is more than physical deprivation. UNDP has defined human poverty as deprivation in essential capabilities like longevity, knowledge, provisioning and community participation (Likwelile, 2000). In a nutshell the concept of poverty goes beyond objectivity to what individuals consider to be poor or deprived.

Strategies for Poverty Alleviation

Any suggested package for poverty alleviation has to recognize the fact that poverty is a multidimensional problem. As such in order for one to be able to properly design, implement and assess programs intended to reduce poverty, an approach that reflects the complexity of the problem of poverty must be used. In the case of Tanzania such poverty alleviation programs must, as a minimum, aim at:

- Emphasizing shared growth to widen economic opportunities;

Table 2: *Characteristics of different poverty levels in society*

Poorest • Single parent unemployed or two parents both unemployed • Many children • No means of provision except by begging • Widows with lots of children • Orphans • Inability to educate children • Almost never buy clothes • No assets • Insufficient poor quality food, sometimes have to beg for food • No proper place to sleep poor quality housing	**Poor** • Temporary jobs • Have some food, but struggle • Pensioners with many children • Lots of children • No pension • having some sort of house not good made of mud **Quite poor** • Earns enough to cope daily, mostly temporary work/self-employed • Few children to look after • Have sleeping place • Children attend school irregularly • Able to buy enough food • Payouts from old jobs **OK** • Pensioners without dependants • Good supply of food • Few children	○ At least one parent has a permanent job • Children attend school regularly • Good house • More than enough food **Wealthy** • Professionals and business owners • Good money to adequately supply family • Children attend school regularly • Electricity in the house • Owning a television • Smaller families • Owning a car/gun • Eating bread with margarine • Children attending tertiary education • Company pensions • Food in abundance • Excellent housing

- Promoting individual initiative i.e. private sector development;
- Enhancing qua'ity of life i.e. human development or meeting basic needs;
- Working to reduce gender inequalities to create ajust society;
- Addressing the rural question to bring the majority along;
- Investing in (modern) agriculture to ensure food security and stable incomes; and
- Institutionalizing participation and good governance to imbue a sense of accountability (Likwelile, 2000).

In Tanzania proposed strategies for poverty alleviation are multidimensional. They embrace:

- Raising the return on assets;
- Increasing the non-farm employment;
- Designing and implementing policies that accelerate economic growth i.e. ensuring that the poor acquire own capital base;
- Involving the poor in the poverty alleviation process, because they are the agents that need be changed;
- Instituting property rights taking into account gender inequities; and
- Continuing to study and documenting the forms, nature, changes and distribution of poverty in order come up with policies measures that can correctly redress the situation. (URT 2000).

Since most of the MFIs aim at increasing access to financial services to the poor, the above listed ingredients for any poverty alleviation program do apply. The extent to which MFI have contributed to poverty alleviation in Tanzania will be examined with the above ingredients in mind.

MFIs Achievements and Poverty Alleviation

Knowledge about the achievement of MFIs in relation to firms' performance but specifically on poverty alleviation remains partial and contested. At one extreme are studies arguing that MFIs have beneficial economic and social impact (Hossain 1998; Holcombe, 1995; Otero and Rhyne, 1994). In this context it has been argued that micro-finance might indeed make substantial impact on the incomes and welfare of most disadvantaged groups, even in a country without any financial infrastructure (ILO, 1997). MFIs elsewhere in Africa have records having impacts on jobs creation, income and welfare. As argued by the ILO Director (1997), poverty eradication is the main objective in the operation of the MFIs. The Director argues that MFIs give the poor the means to save and protect themselves against risks. Access to micro finance to MSEs facilitates investments that create or sustain jobs. A study by the World Bank using data on consumption, savings, assets ownership and net worth shows that micro credit not only reduces poverty and improves welfare of participating households but it also enhances the households' capacity to sustain their gain over time (Khandiker and Chowdhury 1995).

At the other extreme are those studies cautioning against such optimism and pointing to the negative impacts that MFIs can have (Montgomery, 1996; Rogaly, 1996; Adams and Von Pischke, 1992). It is held by the pessimists that MFI services are not sustainable as most MFIs depend on external funding. Many borrowers find themselves in the spiral of borrowing as the credits they received are too small for them to spin off the poverty circle.

In the middle are the works that identify beneficial impact but argue that micro-finance does not assist the poorest as is often claimed (Hulme and Mosley 1999, 1998, 1996). This position is mainly associated with the shift towards "better offs" in MFIs programs over time because of the pressure toward financial sustainability by the institutions themselves (Mayoux, 1999). Hulme (19990 argues that different strategies are needed to reach and effectively assist the poorest households. Direct assistance in terms of food handouts or other direct safety nets such as cash transfers could be more appropriate than would micro finance services. These contested views are important in assessing the impact of MFIs on poverty alleviation in a country like Tanzania.

MFIs in Tanzania

The existence of MFIs has no long history in Tanzania as in other countries in the region such as neighbouring Kenya. In Kenya one MFI-NGO has graduated into a bank, i.e. the K-Rep Bank. In general NGOs in Tanzania were deliberately depressed during the socialist era because they were perceived as not playing a significant role in development process. However after the country's plunge into the economic crisis in the late 1970's and 80's, NGOs were recognized as one way of attracting foreign resources into the country. At the same time the structural adjustment programs together with other economic and social reform measures recognized the important role that non-governmental institutions play in the development process. Indeed, NGOs are now regarded as complementing the government efforts in the development process and not a threat.

By 2000 more than 1,800 NGOs had been registered countrywide (Assad, 2000). Out of these 100 NGOs are operating as micro-finance institutions. The estimated number of the clientele level is just about 240,000 (Dinwiddy, 2000). The MFIs coverage is still very low at about 0.0075%

of the country's total population of about 34.5 million people out of whom 80% live in the rural areas where the level of poverty is very high. In the following section study findings of the MFIs are presented.

FINDINGS OF THE STUDY

The study findings include the categories of the MFIs studied, practices of the MFIs and contribution to poverty alleviation.

Categories of MFI Studied

From the study results we could categorize MFIs in the country into five groups. These are: (a) Government funded MFIs, comprising the central or local government schemes that have been formed with a specific objective of delivering financial services mainly credit to specific groups of population normally, specifically to small industrialists and resources-disadvantaged ones like women, youth, disabled. The schemes include the Small Industries Development Organization (SIDO), Women Development Fund of the Ministry of Community Development, Women Affairs and Children and Dar es Salaam City Commission; The second category is that of the financial NGOs (MFI-NGOs). These include international branches of NGOs and locally founded and based NGOs that are dealing with the delivery of micro-finance services to the poor. Those included in our study were Swiss Aid, PRIDE, MEDA, SEDA, SERa, Poverty Africa, FEDA, Presidential Trust Fund for Self reliance (PTF).

Savings and credit co-operatives (SACCOs) are the third category. These are members' organizations mostly workers from the same organization (e.g. local government workers at municipal level) or professionals (e.g. teachers). In the fourth category we count the private firms/ religious organizations that are delivering financial services with one of their objectives being poverty reduction. In our survey these included Caritas and the Tanzania Finance Women Company. Micro financial services from the FFIs such as the Akiba Commercial Bank fall in the fifth category.

MFIs Practices and Poverty Alleviation

In this section we shall discuss the practices of MFIs. The practices have been examined under seven different aspects namely: (i) slients selection procedures (ii) repayment enforcement (iii) savings mobilization (iv) lending conditions (v) outreach including areas of operations (vi) sustainability strategies in place

Future Outlook

Differences between the various categories of MFIs will be described if found to be substantial.

Clients Selection Criteria and Existing Procedures

Almost all the categories of the MFIs described above except small-scale ones are targeting existing micro and small enterprises. Generaly for all MFIs, no loans are given to a client with an outstanding debt. Most the MFI-NGOs are targeting adult individuals in groups. SME borrowers may also be business starters, they must however produce good and viable business plans to qualify for the loans.

But the credit department of FFIs like Akiba Commercial Bank, has a different clientele selection system, that of searching for a guarantor for the individual borrowers and not group of other borrowers. For government supported schemes, borrowers have to organize themselves in groups before they can apply for a loan from the schemes. The composition of the group is not specified. Group members that are interested to borrow from the schemes do select themselves. Similar procedures apply to the selection of clients of MFIs-NGOs. Self-selection process is quite strict in MFI-NGOs as members visit each other's business premises to assess the viability before accepting a member into group. They also take interest to exchange information about their families before accepting a new member into a group. As a result clients for MFI-NGOs are closely related some are family members or friends. This is the true, for example, with PRIDE, PTF.

Most of the clients undergo a pre-loan training as part of loan application process. The length of the training ranges from a minimum of one week to one month (PRIDE and PTF). Local government schemes take longer period (Dar es Salaam City Commission Scheme was operational in 1999).

The training takes a form of meeting in which the participants are informed about the rules and procedures of the MFI in question. The same opportunity is taken to sensitize the clients on some of the basic skills of business and credit management. The training attendance is also used by MFIs like PRIDE and Poverty Africa to assess the seriousness and commitment of the potential borrowers in their groups. In the case of PRIDE, it is only those potential borrowers who the pre-loan training without missing even a single day that qualify as clients.

Gender of the borrower is one the most influential factor that is considered in the selection process. This is particularly so in the MFI-NGOs. Almost all the financial NGOs have set aproportion of women to be reached in their services. For instance Poverty Africa clientele is 80% women, the same with PRIDE and SERa. In others like MEDA 60 % of the clients are women.

Other MFIs programs of FFIs have not pre-specified but definitely serve women as well. SMA and SACCOs offer their services regardless of the sex. However our study revealed that 46% of the SMA borrowers were women entrepreneurs.

Specific selection conditions apply for SACCOs. The selection of borrowers is predetermined by the nature of the institutions themselves. A borrower must be a member and the size of loan has to be consistent with the rules namely a maximum of three times the value of savings. Capacity to pay is determined by the level of salary. Thus a higher salary attracts a higher loan than a lower salary.

Enterprises Targeted

Many of the micro enterprises being supported are in trade sector and less in processing industries. Exceptions here are SMAs and SACCOs. The former is by history actively engaged in the manufacturing sector. SACCOs extend credit to the needy members engaged in agriculture (provision of loans to make bulky purchase in the post harvest periods or inputs for farms), education, health or personal houses construction.

Weaknesses Observed

What can be discerned from the above selection criteria is that many of the poor people wishing to start micro businesses as a way of disentangling themselves from poverty cannot easily be accommodated in above criteria. These include the youth who lack social networks as they cannot easily be trusted to join groups. The same applies to "the new poor" groups of unemployed fresh graduates with knowledge but without practical entrepreneurial skills, salaries and capital base. Such individuals are effectively crowded out of the MFIs portfolio and in particular out of SACCOs which workers associations per se tend to gravitate to.

The kind of businesses that are being supported is also questionable. Very little support is going into the processing /manufacturing sector, most of credit goes into petty trading and services sector. It is widely known that manufacturing sector adds higher value in the economy compared to others. It is therefore doubtful as to whether the contribution to poverty alleviation can be realized to the maximum by supporting mostly the micro trade sector and less the industrial sector.

Using the group formation and lending approach in the government MFI schemes has in some regions suffered from political intervention (VPO-UNDP, 2000). Politicians have used the schemes as their campaign instruments. The danger here is that the business philosophy in the delivery of the credit services suffers which ultimately lowers the willingness to repay and the ability of the scheme itself to become financially sustainable and to increase outreach.

Group modality has also been shown to exclude the very poor of the poor as these may either exclude themselves from joining or be deliberately excluded by "the better-offs" from the groups.

Repayment Enforcement Mechanism

Loan repayment enforcement mechanisms are designed to suit the circumstances of the parties involved. They are usually a creation of the lender. For government schemes like SMA borrowers enter into a contract with the lender in which the grace period and other terms of the loan are specified. Normally a borrower is required to contribute a fixed percentage to the value of the project being financed before loan approval. At the same time if the loan is given in form of an asset the ownership does not pass to the borrower until after the payment of the final balance (Use of Hire Purchase system).

Group pressure and credit officer follow-ups were used to a less extent in the central and local central governments' schemes. Success rate with these measures was very minimal as compliance to rules was not in place. The repayment rates were at most 10% (Women Development Fund). Enforcing loan repayments from the MFI-NGOs (PRIDE, Poverty Africa, SERa, SEDA, PFT etc.) involved a blend of measures which all contributed to very high repayment rates. Repayment enforcement practices in the financial NGOs are given below.

Loan Enforcement Repayment Practices of MFI-NGOs

a) Members of groups guarantee each other, there is no real asset as a collateral such that if repayment is due and a member cannot pay the other group members pay on her/his behalf;
b) Starting with small sized loans that can be easily be repaid if business performs well.
c) Very short and frequent repayment intervals (weekly basis for PRIDE) with virtually no grace period;
d) Imposition of penalty against the groups which fail to pay on time;
e) Frequent (most frequent are weekly) meetings to pressurize loan repayment;
f) Very short grace period (e.g. one week) from loan receipt to repayment;
g) Very frequent repayment intervals (shortest one week) so that to lessen the risk of sales revenue diversion into other uses.
h) Very close loan monitoring by the credit officer. Indeed, like the case of Poverty Africa and PTF the credit officers are always on their toes following up their clients and at times offering assistance where it is needed.
i) Detailed and effective management information systems have been instituted. Management and staff in general are on top of the day knowing always what is going on in their loan portfolio;
j) Use of incentives to repay effected though increasing the loan sizes for good repeat borrowers that may need larger loans to finance their growing businesses does this;
k) Social exclusion of members from groups if one is proved to have deliberately defaulted; and
l) In extreme cases personal property (household items) have been confiscated and auctioned to recover the loans.

These measures facilitate early detection of possible defaulters before it is too late. At the same time the penetration of non-needy clients can be minimized.

Strengths of the enforcement practices are many.

- Certainty of very high (almost 100%) loan repayment rate. This has a positive impact on poverty alleviation measures, as the funds repaid can be re-lent and circulated to other needy clients and thus facilitates the expansion of economic activities and thus possibly reduces poverty in additional households or MSE;

- Low risk on the part of the lenders arising from very low loan l.osses. At the same time the self-selection procedures lowers the transactions costs for credit rating tremendously. This was acknowledged by all MFI-NGOs;
- Monitoring of the performance of borrowers if accompanied with some advisory services helps clients to improve performance. However this is done at a low scale and practiced by PTF credit officers mainly;
- Enhanced sustainability chances of the MFI as an institution due to low transaction costs and virtually nil loan losses;
- An increased outreach in terms of increased number of borrowers resulting from the fact that the loaned money (plus interest) flows quickly back to the lender who again can re-lend the money to even increased number of other borrowers.

Weaknesses of repayment enforcement practices are:

- High transaction costs on the side of the lender in particular the monitoring of loans, which is almost on a daily basis. This will limit the ability of the institutions to become financially sustainable. At the same time other strategic actions such as capacity building will not be realized due to lack of funds;
- High opportunity costs on the side of borrowers arising indirectl): from the time spent on meetings (weekly meetings) for pre-loan training and repayment;
- If borrowers fail to repay they suffer the sociological effects of social exclusion from the groups they have been associating with. This is in deed a loss of social capital which many Africans make use in many incidences of their lives (Mayoux, 1997);
- The borrowers self-selection practice may lead to discrimination, where the group's formation excludes the most disadvantaged individuals. The discrimination may also be combined with self-exclusion from programs by the poorest themselves when "better-off" (though still poor) people are involved. This has been reported in Small enterprise Foundation in South Africa (Mayoux 1999).

Savings Mobilization

Savings is the beginning of all financial intermediation. Savings services are among the most beneficial service for the poor. Nearly all households need to save to protect themselves against periods of low income or cover for emergencies like health expenditure. Enterprises need to make savings from profits for re-investment. Credit delivery should ordinarily be accompanied by savings mobilisation.

Deposits-taking institutions in Tanzania are subject to the central regulatory and supervisory authority, the Bank of Tanzania (BOT). Thus unless authorized and licensed by BOT no institutions in Tanzania can legally take deposits as a financial institution. All MFI-NGOs are subject to this regulation. They are legally disallowed to operate as deposit taking institutions. According to MFI policy the non-deposit taking institutions will not be subject to regulation and supervision. Limited supervision will applied to the MFIs that are organized cooperatively among people who know each protection (URT, 2000a:13)

Our study revealed that NGO-MFIs and SACCOs mobilize some money "savings" from borrowers. An exception is for those MFIs like sma which are by their law of establishment explicitly prohibited to mobilize savings from borrowers.

The MFI-NGO's mobilise "savings" in guise of members registration fees, loan insurance funds, groups funds. The savings are both compulsory and voluntary. They do not categirze themselves as deposit taker although they truly compel their borrowers to save with them.

The compulsory savings are in form of loan insurance Funds (LIF) i.e borrowers contribute a part of the loan (5% to 10%) of the borrowed amount into the LIF of the lender before receiving the loan. This amount is normally deducted and retained by the lender in the institutional account. The voluntary savings are made by members in the group's accounts or paid into the borrower's bank accounts, which then save as an indicator of seriousness to credit demand. In MFIs like PRIDE members do contribute deposit the money by the institution, while for organizations like TWFC, the borrowers have to provide bankers (FFI-linkage) evidence of the existence of the money in an account. The loan insurance fund serves as a collective collateral for the loans. It can be quite substantial, like the case of PRIDE where the loan insurance had grown to Tshs. 6.5 billion by March 1999 (VPO and UNDP, 2000).

All SACCOs are by definition thrift organizations among groups of workers in one organisation or in related organizations or professions. They are thus actively engaged in savings mobilization, which is the core activity. Members in SACCOs do not necessarily join with the motive for borrowing like in the MFI-NGOs. The number of members in SACCOs ranges between 100 and 1000 persons. The SACCOs included in our survey was the Mikindani Teachers SACCO of Mtwara, in which the members were borrowing according to the repayment conditions set by their co-operative. Most of the savings are used for emergency/ precautionary motives.

Strengths of the Savings Component

- Savings services are among the most beneficial services for the poor. It has been proved that even the poor in Tanzania can save. This creates an opportunity that can be innovatively used by the commercial financial institutions to broaden and deepen financial intermediation in the country. Intermediation can take different forms from use of wealthy guarantors to poor or MSE to credit facilities to the MFIs for on-ward lending to the poor household and the MSE.
- Nearly all households need to save to protect themselves against periods of low income or cover for emergencies like health expenditure. Enterprises need to make savings from profits for re-investment. However this is again dependent on the ease and flexibility of withdrawal of the savings made to the depositors.

Weaknesses Observed

- The major concern here is the security of the members' savings. As noted above the recent Micro finance policy has clearly spelt out that a flexible framework for regulation and supervision with respect to depositors protection and prudential financial principles is in the making (URT 2000a:12-14).
- The members forego other benefits that they would get from their money by saving with the MFIs. This opportunity cost ought to flow back to them in terms of interest. Collection of savings from the poor without return is further dis-empowering rather than empowering them financially. Most MFI-NGOs have not specified the rate on interest on savings. Clients cannot withdraw their savings as and when they want to. They must first quit from the MFI. This is an aspect where the MFI policy implementation mechanisms need to re-examine and design ways that to serve the interests of both parties involved in the MFI business.

Lending Conditions

Lending conditions are imposed upon the MFI clients to comply with. They include interest rates charged, loan sizes, minimum savings prior to loan application, references or collateral. Loans are extended to adults of 18 years of age or above. For those loans lent to rural areas, the village government or ward officers act as a guarantor for the loans disbursed to groups. This applied to WDF, SEDA.

Lending conditions for most MFIl-NGOs include:

- Most MFI-NGO's do lend as a rule and general practice to borrowers who have viable/ profitable projects. Many of these projects have been on-going;
- All loans made carry interest rates. Interest rates for the MFI-NGOs range between 17 percent to 40 percent per annum. Specific interest rates for MFI- NGOs are given in the appendix.
- Interest rates for SACCOs have been observed as being relatively low ranging from 1.5% to 29%;
- Pre loan savings either in group fund (Poverty Africa) or in bank account (TWFC) ranges from Tshs. 1000 to 10,000/= per person (in year 1999); and
- Pre-loan training attendance on the side of borrowers is another condition for the borrowers. The length of training ranges from a total of one week to one month. The borrowers are required by some MFIs (PRIDE and City Commission borrowers) to pay for the training cost.

Loan sizes vary from 40,000/= to Tshs. 2.5 million. The a verage loan for starting borrowers is however around Tshs 50,000 and the repeaters get higher amounts depending on the repayment speed.

MFIs such as MEDA demand positive recommendation or character reference from the influential parties such as market/ward leaders. MEDA does not use the group lending approach but takes household or personal property as security (bicycles, radio, etc.).

Lending Conditions and Poverty Alleviation

As already pointed out above the clientele of MFIs are mainly existing businesses and matured adults. These practices omit the younger generation and starters from their portfolio. Unfortunately the young generation in Tanzania lacks the social capital that is demanded by the MFIs. They also lack the character references that being demanded by some MFIs. To which source of capital will this group of population resorts to? Mayoux (1999) correctly pointed out that the focus on existing (women) entrepreneurs with proven business track record means a neglect of others who might indeed need the assistance but lack businesses. This is in deed a shift to the "better offs" individuals which works against reduction of poverty. It in a way tallies with the position held by others that MFIs may not reach the poorest of the population.

Furthermore credit delivery to existing business leaves other important aspects of poverty alleviation such as support to education and health expenditures. Loans directed to these other human development aspects will bring about lasting contribution to poverty reduction.

Interest rates have not been explicitly been mentioned as one of the limitations by the borrowers. What most of the small borrowers are interested in is more of the liquidity, to get the credit as quick as possible so that they can tackle immediate orders or finance their current operations. They do not therefore think intensively about the magnitude of the interest. In deed only a few borrowers (about 15 percent of the 87 respondents cared about interest levels).

However, a substantial percentage of the borrowers (36 %) complained against the size of loans. The start up loans ranging from 40,000/= to 50,000/= (Poverty Africa, PRIDE, SEDA) are too low to start any meaningful business. The application of the minimum loan to laterallx to all borrowers mav therefore be serving the interest of the lenders more than the borrowers. It puts all the borrowers in the same bandwagon regardless of the differences in financial needs. In fact some borrowers (women in Arusha) admitted that they borrow the money keep and repay as per schedule, repeat the same procedure until they qualify for the higher amounts that they need for their business activities. This is certainly not the objective of the MFls. It really delays the potential large borrowers from realizing the business activity they have in mind, and implicitly it also means delayed contribution to poverty reduction at aggregate level.

This is an area that needs further innovation as far micro finance indus!ry is concerned. Actually the challenge is how to design a variety of products to different kinds of clients. This calls for product differentiation in the delivery of micro finance services. Bank Raykat Indonesia with its Unit Desa System and BancoSol of Bolivia have been serving both poor MSE as well as clients in need of relatively large amounts. It is high time that MFls draw lessons from these successful MFls that follow best practices in delivering their services to the poor.

Location of Borrowers

Our findings show that most of the MFIs studied except SACCOs, SMES and religious organization like Caritas are urban and peri-urban based. This is consistent with all the studies of MFls (K-rep, 1997; Shayo and Temu, 1998; VPO-UNDP, 2000). This is definitely a good attempt to poverty alleviation in urban and peri-urban areas. However the major shortcoming is the exclusion of rural areas, where the level of poverty and infact abject poverty is prevalent. MFls like PRIDE, SEDA and MEDA justify their confinement to urban areas by high cost of operation in rural areas. It is also argued that the group lending model like the one followed by PRIDE which demands frequent meetings of the borrowers cannot be easily applied in rural areas where the population is more scattered.

In fact the major question is whether the current operating modalities can work in rural areas? What innovations need be made? Rural peasants are not salaried workers who can contribute to SACCOs from which they can later on borrow. What other alternative sources of income or civil organizations can be used to organize them so as to get access to micro finance services? The speed at which community banks are being opened (currently only two are functioning; namely Mufindi in Iringa region and Mwanga Community banks in Kilimajaro region) does not yet answer these questions.

Sustainability Strategies in Place

The first strategy towards financial sustainability is the reduction of dependency ratio (Hashemi, 1997). The dependency ratio shows the extent to which the MFls loan portfolio are funded by the capital injections from either donors or government coffers. The question of dependency ration applies to MFI-NGOs or government schemes that are basically dependent on external financing.

The strategies in place to raise further funds for MFI-NGOs include the search for other donors implying further dependency on external funding and using interest income on savings to finance operations. Further dependency on donors especially the external donors will in the long run work against the financial sustainability of the MFIs. This is because of the growing competition on the donor funds from all over the world especially after the end of the cold war.

The fact that MFI-NGOs are able to mobilize "savings" in guise of "loan insurance funds" or others shows that the poor can save. They only fail to save in their formal financial sector due to several reasons such as fear of intimidation by the formal procedures at commercial banks and the reluctance of such institutions to handle small sums in rural or peri-urban areas. This avails an opportunity that can be made use of by the FFIs and enhance linkages between FFIs and MFIs, which at the moment not being exploited.

Indeed, our findings show that no single MFI has approached the doors for financial sustainability in terms of trying to forge the macro-micro financial linkages. Efforts towards this direction would show that the MFIs are operating profitably and have viable business that can are acceptable by the financial institutions on prudent business reasons. It would also mean that the MFIs have reached a business level in which lending from financial institutions for onward lending is profitable. This is for in instance a practice with BancoSol Bolivia and Grameen Bank of Bangladesh (Glosser, 1994; Hashemi, 1997).

It should however be acknowledged that micro-macro linkages require proper and functioning financial policies to be in place at both macro and micro levels. It is hoped that with the Micro Finance Policy in place the macro-micro linkages will be facilitated.

Future Outlook

The study by the VPO and UNDP (2000) has established a number of constraints faced the poor and MSE operators looking for access to credit. These include lack of collateral, high interest rates, too high indirect costs of borrowing, (bribes and follow-up costs) and preparation of project write-ups. Others problems include liquidity shortages in the sense that business cycles do not match with terms of loans, personality clash with the lending officials, corruption/nepotism. These problems have been observed in relation to FFIs. We did not observe such problems and malpractices in our study. This does not however means that the MFI-NGOs are immune to such ills. TIle way forward is to ensure that such tendencies do not encroach them.

According to our study and others (Limbu, 1998), there is little networking and coordination among MFIs. This has given a room to duplication of micro-credit services in such regions as Arusha and Dar es Salaam (Shayo-Temu, 1998). Moreover, the NGO-MFIs services are not properly aligned with that of government and public sector institutions financing MSEs. The recent efforts that led to the formation of the Tanzania Association of Micro Finance Institutions (TAMFI was officially launched in 1999) is a great milestone and big step towards the co-ordination of the work of MFI and within different categories of MFIs covered by the survey. It is expected that networking and co-ordination will result into increased outreach and greater impact on poverty alleviation.

CONCLUSIONS

The existing records show that MFI borrowers in Tanzania do not exceed 250,000 in total. Many of the existing MFIs provide small loans and successfully target women who operate in urban and peri-urban areas and, as a result the urban bias of the MFIs has become very apparent. The level of outreach is very small compared to the level of abject poverty in the country particular in rural areas (over 50% of Mainland Tanzanian are living below poverty line). One can in fact conclude that MFIs in this country have not yet managed to reduce poverty to a notable level (e.g. a million borrowers). MFIs in this country have not yet gone beyond the "subsistence dimensions" (Mosley, 1999). The arguments that existing MFIs in their present models find it expensive to operate in rural areas might not be tenable as experience elsewhere has shown that micro finance can work in rural areas.

The un-answered questions still remain what are the appropriate and less expensive modalities that can be applied in the delivery of micro finance services to the rural poor? This calls for further innovations and refinement of the existing modalities. There is need to expand the MFI industry and more so this builds a case for strongly supporting the existing institutions, in terms of macro policies and financial backing where possible. Services by MFIs are mainly provided to existing women micro-entrepreneurs. Implicit rationale for targeting women is the recorded repayment rates form women and thus directly contributing to financial sustainability of the institutions. The targeting is correct but it is not free of problems especially taking the extent of poverty in Tanzania. The targeting leaves out the unemployed youth without any track record on entrepreneurial ability. More specific "the new poor," these being unemployed graduates from various training institutions have not being thought of in the current MFIs practices.

Most of the MFIs currently operating in the country are small and/or new. They lack well trained and competent staff to conduct the micro finance business which is different in philosophy and practice to the commercial banking business. To be able to contribute effectively to poverty alleviation, they need to have well-trained and equipped staff in Micro finance. A great deal of capacity building is required to bring them to the level at which they can operate with large outreach, quality services and profitable operations. Thus capacity building should be a continuous exercise. Much of the capacity building can take place in-house through training of staff, development of management and organizational structures and building of management and governance capabilities.

External professional training in financial management and management information systems tailored to the needs of MFIs is equally important. In the training focus has to be on good standards and best practices for increased outreach and sustainability of operations of MFIs. Most MFIs with the exception of SACCOs are far from sustainability that is they are solely donor dependent.

They still need a lot support particularly in strategic/long term orientation of creating ways and means of achieving financial sustainability.

Appropriate technical support is much needed particularly is support the training programs of most of the MFIs. Donor support should be directed towards capacity building because this is decisive in sustainability of the MFIs.

The savings-first institutions i.e. SACCOS tend to be financially sustainable as they are member based and funded, without any donor support. In the long run, this is important for continued outreach and impact. They provide loans to ongoing business, for working consumption, and education and health expenditures, which is equally essential for poverty eradication, as it contributes to improvement of human capabilities. More generally, increasing access to savings facilities to the poor is an important objective in itself.

One possibility is that Government funds could supplement the capital base of savings- first institutions such as SACCOs so as to expand the outreach.

Using the existing MFIs services delivery practices to different target groups, or for different activities in rural locations, may still be preferable to creating new institutions but a lot needs to be done in terms of adaptation and design of new products. This is in deed a challenge to academia, researchers and practitioners.

Further lessons need to be drawn and adapted from successful models such Grameen Bank that has managed to serve over 3 million clients and covered over 50% of the villages of Bangladesh. The size of the loans from form most of MFIs are not flexible and do not take into account the business cycles of the clients. The application of the minimum loan sizes to all borrowers serves better the interest of the lenders than the borrowers. It puts all the borrowers in the same bandwagon regardless of the differences in financial needs. This practice delays the potential large borrowers (though still poor) from financing their activities and directly delays contribution to poverty reduction at aggregate level. This is an area that needs further innovation as far micro finance industry is concerned.

Actually the challenge is how to design a variety of products to different kinds of clients. This calls for product differentiation in the delivery of micro finance services. Bank Raykat Indonesia with its Unit Desa System and BancoSol of Bolivia have been serving both poor MSE as well as clients in need of relatively large amounts. It is therefore timely that MFIs draw lessons from the established best practices in delivering their services to the poor and MSE.

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Appendix: *Brief MFIs Profiles*

Dar es Salaam City Council Fund

This fund was formed in order to curb the shortage of credit funds to the city micro entrepreneurs. It was started as an effort to complement the funds that were being provided by the Women Development Fund and the Youth Development Fund. Seems to have been able to contribute out of revenue to support the WDF and YDF. Moreover, unlike other town councils, the DCC operates a credit shop in addition to the two funds. Credit is provided to individuals and individuals organized in groups. Moreover, unlike other councils, the DCC has 6 staff specially recruited for the delivery of micro-credit services and offers other services-project write-up and assists clients in project management. The DCC also envisages starting a community development bank.

FFIs : Formal Financial Institutions

MEDA: Mennonite Economic Development Associates

MEDA started operating in Tanzania in 1987 with a start-up capital ofOS$300,000 from Canada and was licensed as an MFI-NGO 1993. It has two branches, one in Mbeya and another in Dar es salaam. The size of loan range from Tshs. 50,000 to Tshs. 150,000. The lending rate is 48 percent and charges for technical services offered to client by MEDA is 12 percent but falls to 6 percent and zero percent for the second and third round of borrowing. MEDA does not mobilize savings. Loans are provided both to individuals directly and to individuals organized in groups. Either of the targeted client must have an ongoing business; and, the loans are supplied on the basis of character trust assessment. Loans are screened first and clients must contribute 20 percent of the loan value in advance as loan insurance (i.e. collateral)

NGOs: Non-Government Organizations

PRIDE: Promotion of Rural Initiatives and Development Enterprise Tanzania

PRIDE started in 1994 with the aim of testing the applicability of the Grameen Bank micro-lending model in Tanzania. PRIDE operates only in urban and peri-urban environments (the population must exceed 100,000 people). It currently operates a network of 22 branches in all regions in Tanzania except Mtwara, Lindi, Bukoba and Rukwa.

SACCOs: Saving Associations and Credit Cooperative Societies

The main source of capital of the SACCOS is share holdings and deposits of members to whom it provided credit.' The use of the loan is at the members discretion. For example, the use of the loans has included finance of businesses, household construction, education fees. There is only limited screening of loan applications, seemingly because of peer pressure associated with SACCOS. The loan sizes depend on a member's share holdings and these shares provide collateral for the loans. The interest rates are variable, they range from 1.55 to as high as 24%.

In SACCOS, loan repayment is enhanced by the fact that deductions are automatically made from the lender's salary.

SEDA: Small Enterprises Development Agency

SEDA was initially started as a department of World Vision in 1993 with a capital injection of US$50,000 and subsequent capital injection from Ford Foundation and USAID. In 1996 SEDA was registered as a micro-finance NGO-MFI with its headquarters in Arusha. By May 1999 SEDA had branch offices in Arusha, Moshi and Mwanza. Two field offices started in Babati and Shinyanga in 1999. Loans are available for ongoing businesses with a minimum loan size of Tshs. 50,000. More than 77 percent of loans are made to women. The lending rate is 24 percent (down from 30 percent). In addition, 13 percent of the loan value is charged as cost of processing the loan and training the beneficiaries. SEDA only lends to individuals who must first form an upatu (ROSCA) group of not less than 10 members and contribute 20 percent of the loan amount in advance as collateral.

SIDO: Small industries Development Organization

SIDO is a government-owned MFI that commenced operations in 1974. It has received capital injections of Tshs. 1,960 million with approximately three-quarters from the government and one- quarter from foreign donors and NGOs. It does not mobilize its own savings from the clients serviced with both start-up and working capital loans of between Tshs. 50,000 and Tshs. 6.5 million. In 1998, approximately 46 percent of total loans were disbursed to women, mostly in the urban areas. SIOO supports value adding projects in the areas of manufacturing such as metal fabrication, furniture and wood work industries, food canning and processing etc.

The lending rate charged is 30 percent per annum. SIOO, whose mission is to eradicate poverty, also provides complementary business services to clients that include training of clients, project write-up, and advocacy. SIOO retains as collateral ownership of the asset purchased by the loan until repayment is complete.

WDF: Women Development Fund

WDF is under the Ministry of Community Development, Women Affairs and Children, respectively. The fund was instituted in 1993/94 fiscal year and is administered to the targeted groups by the office of the District Community Development Office under the District Council.

The WDF started with Tshs. 1.5 billion and the targeted group was women who are formers organized in groups and live in villages. The lending rate for the WDF was set at 24 percent but was revised downwards to about 10% in 1999. Beneficiaries are expected to undergo training before credit delivery.

WDF is distributed to each region and each district where the district councils administer it. However, the volume of funds has been small relative to the population women in the country. There has been a record of low repayment rates that can be accounted for by lack of staff trained in micro-finance services and institutional framework for credit delivery and enforcement of loan repayment at the level of the district council.