

**ASSESSMENT ON IMPACT OF MICROFINANCE INSTITUTION ON
GROWTH OF MEDIUM AND SMALL SCALE ENTREPRENEUR IN
TANZANIA. A CASE OF EFC**

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**A Research Dissertation Submitted In Fulfillment of the Requirements for Award of
Degree of Master of Business Administration (MBA) of Mzumbe University**

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CERTIFICATION

We, the undersigned, certify that we have read and hereby recommend for acceptance by the Mzumbe University, a research report entitled: **“Assessment on impact of Microfinance institution on growth of medium and small scale entrepreneur in Tanzania. A case of EFC”** in Partial/fulfilment of the requirements for the Degree of Master of business Administration of Mzumbe University.

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My sincere thanks also go to my supervisor Ms Nora for guidance, constructive and enlightening criticism which paved a way to clear direction of this study.

Genuine thanks to all respondents from EFC employee and management for the assistance they gave me while collecting data for this research.

I wish to state here that all deficiency and errors that may be contained in this document are absolutely my sole responsibility.

DEDICATION

To my lovely husband Hans Kweka, my beloved parents Mr and Mrs Bakalemwa for my up bringing, moral support and encouragement up to this point in life.

ABSTRACT

The aim of this study was to assess the contribution of MFI services on the growth of MSEs in Tanzania. Specifically to identify the benefits of MFI on medium and small scale enterprises growth, to assess the impact of MFI loans on livelihood of Medium & Small Entrepreneurs, to assess the costs that medium and small enterprises incur when accessing the microfinance services.

The researcher used both random and purposive sampling to select subject of 120 Purposive sampling was used to 5 administrative staff and random was used to 30 respondents who were operations department staff and 90 customers who were MSE . The collected data through (both primary and secondary) were coded and analyzed by using a special program known as Statistical Package for Social Science (SPSS) and Microsoft Excel 2007.

Most of the SMEs get business capital for their business loans from banks and MFI where by security is required for certain kinds of credits. Most of the business has turned into medium enterprises because of the extended support of these micro-finance institutions and among the appreciated services delivered by MFI, Microfinance enables the poor and excluded section of people in the society who do not have an access to formal banking to build assets There is some challenges facing SMEs in acquired loans from MFI like limited capital, Limited Capital, Poor Market strategies Innovation was a big challenge that Tanzanian SMEs faced.

It is recommended that there is a need to help enhance an accelerated and sustained growth in the SME sector and also provide recommendations to help in the improvement of the services of MFIs. The MFIs may be quick to measure their success rate by considering factors like high repayment, outreach and financial sustainability, but these may not be success if their activities do not reflect in the growth of SMEs. The growth of SMEs does not only rely on access to credits but also the creation of favourable and formidable business environment. The MFIs have a great responsibility of ensuring the proper use of credit which is an important facility in business acceleration. To achieve this, credits should client-oriented and not product- oriented. Proper and extensive monitoring activities should be provided for clients who are granted loans

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LIST OF ABBREVIATION

EFC	Entrepreneur Financial Centre
GDP	Gross Domestic Product
MFB	Integrated Microfinance Bank
MFI	Microfinance institution
NGOs	Non Governmental Organization
NMB	Micro Finance Bank
OECD	Organisation for Economic Cooperation and Development
SIDO	Development Organisation
SMMEs	small, micro and medium-sized enterprises
SPSS	Statistical package for Social science
VETA	Vocational Education Training Authority
WBCSD	World Business Council for Sustainable Development

CHAPTER ONE

INTRODUCTION

1.1 Introduction

This chapter presents a brief introduction and historical background of the study, statement of the problem, research objectives, significance of the study, scope and limitation of the study, and definition of the key operational terms.

1.2 Background of the Study

Micro finance services have become significantly important globally and more preferably at national levels in developing countries. A Microfinance institution (MFI) is an organization that provides financial services in terms of loans, funds at a given interest rates. For example the modern microfinance movement started in the 1970s when pilot programs in Bangladesh, Bolivia, and other countries began to provide small loans to groups of vulnerable women to invest in economic activities.

Ledger wood (2002) microfinance refers to the provision of financial services to low income client including self-employed. Integrated Microfinance Bank (IMFB 2007) was of the opinion that microfinance is the supply of loans, savings and other basic financial services to the poor. Everyone needs a diverse range of financial instruments to run their business, build asset, stabilize consumption and shield themselves against risks. Financial services needed by the poor include working capital loans, consumer credit, savings pension insurance and money transfer services.

Jamil (2008) microfinance is the entire flexible structures and processes by which financial services are delivered to micro entrepreneurs as well as the poor and low income population on a sustainable basis. Africa remains one of the least developed, and the most under-banked continent. This is not a coincidence, and reflects the importance of banking as an engine for economic development. Interest in microfinance has soared in the recent decade and the instrument is now seen as one of the most promising tools to tackle poverty in the developing

The fascination with microfinance derives from the fact that the provision of financial services can contribute to poverty reduction and pass the test of sustainability at the same time. For donors, microfinance is especially attractive as it can be delivered in an institutional and financially sustainable manner that permits them to withdraw after making relatively modest investments. However, microfinance has sometimes disappointed its supporters.

The important contribution made by small, micro and medium-sized enterprises (SMMEs) across nations has been widely acknowledged, with a lot of empirical research suggesting that SMMEs play a crucial role towards achieving industrial and economic development objectives of a country. European Commission (2007), SMMEs are viewed as an engine of growth for the European economy as they are an essential source of job creation, entrepreneur spirit and innovation, and in that regard, seen as crucial for fostering competitiveness and growth. The World Business Council for Sustainable Development (WBCSD, 2004:2) reports that in the Organisation for Economic Cooperation and Development (OECD) economies, SMMEs account for over 95 percent of firms, 60 to 70 percent of employment, 55 percent of Gross Domestic Product (GDP) and further generate the lion's share of new jobs. In addition, WBCSD (2004:2) reports that for developing countries, more than 90 percent of all firms outside the agricultural sector are SMMEs, generating a significant portion of GDP.

The relative importance of small and medium scale enterprise in advanced and developing countries has led and would continue to lead to a reconsideration of the role of Small and Medium Scale Enterprises in the economy of nations. The development of many countries is often measured by such indices as the level of industrialization, modernization, urbanization, gainful and meaningful employment for all those who are able and willing to work, income per capital, equitable distribution of income, and the welfare and quality of life enjoyed by the citizenry.

Considering their documented socio-economic importance across nations, SMEs still face daunting challenges and in order for them to survive and grow, there is a need for a

favourable environment that allows them to prosper and expand. New small businesses are usually considered to be vulnerable especially in the immediate post start-up period and many will fail to develop into prospering and thriving ventures. As already highlighted, the SMME sector is seen as an alternative avenue to contribute to a country's sustainable economic growth, through employment creation and poverty alleviation.

Despite the role played by Microfinance Institution in poverty reduction, there are serious constraints limiting their growth and thus their contribution to poverty reduction. The most important constraints the MSEs sector growth have always been non-conducive, non-transparent and complicated legal and regulatory frameworks coupled with bureaucracy. Although these constraints are also faced by large firms, they affect MSEs more. Another constraint MSEs are facing is inadequate markets due to unstable market value chains and reliance on small and localised markets. Purchasing power is low, transport infrastructure poor, and most MSEs have no knowledge of markets beyond their immediate locality. Productivity (including quality) is low, due to a variety of reasons, which include inadequate and outdated technology, low levels of technical and vocational skills, and weak business management capabilities.

Competitiveness is therefore low, especially when comparing products imported from neighboring countries and beyond. Most enterprises lack access to capital that would allow them to address some of these weaknesses. It is known that most of these constraints could be eased through effective MSEs institutional frameworks. A number of studies have indicated that the business institutional framework for MSEs crucial for sustainable and rapid growth of MSEs. The institutional framework is critical in view of the strong waves of globalization and against the background that Tanzania's MSEs function in an environment that is not conducive. A great need for transformation is needed in the MSEs sector to protect the poor entrepreneurs from the frequent losses arising from inadequate business management styles.

Currently there are many MSE support institutions providing backing to MSEs. Despite their existence, MSEs in the country continue to weaken, raising questions as to whether

the institutions have adequate capacity to support the MSEs. By itself, however, an inadequate institutional framework does not constitute a research problem. The major issue is that previous studies had focused on the identification of the institutional constraints facing MSEs without assessing the capacity of the support institutions and requirements and delivery systems of their services. Studies like one by Wangwe (1999), Lund et al. (2005), and Kimuyu (2002) have investigated the role of the institutions in promoting MSEs, but do not explain why the institutional framework for the promotion of MSEs is poorly integrated, or what constraints the MSE support institutions themselves face.

The quality of the institutional framework depends on the capacity of the players within it. It turns out therefore to be important to conduct a critical assessment of the capacity of the existing MSE support institutions so as to understand the factors underlying the dismal performance of the institutional framework for MSEs development. Though the study focuses on the assessment of the MSE institutional framework, some of the causes of the dismal performance of the MSE support institutions could also be found in the demand side. Accordingly, the study was extended to include issues related to MSEs' service needs, awareness and utilization.

1.3 Statement of the Problem

The financial institution should review their operation taking full account of the new environmental in which they are operating in. The environment in which development finance are operating has changed substantially. Future developments of financial institutions are required to be efficient and effective. Unlike the parastatals private sector firms cannot expect draw resources from the treasury.

Although liberalization has resulted into increasing in number of financial institutions operating in Tanzania, financial deepening has not occurred. The financial system is still shallow in performing the intermediate role of receiving deposits from those with surplus to save and to lend to those who are in need of funds to finance their business including Small and Medium Enterprises (SME). While SMEs have suffered from severe shortage of finance, a bank has grappled with problem of excess liquidity (Wangwe, 1999).

Most formal financial institutions regard low income households as poor to save, and are not personally known to them, they do not keep written accounts or business plans and they usually borrow small and uneconomical sum. They therefore perceive that they are exposed to high risk and cost every time they lend to this group. This situation which is market failure has force people to look for alternative financing. Establishment of MFIs was one of the initiatives of the government, non-governmental organization (NGOs) and private companies to fill the financing gap resulted from the market failure. Other motives of establishing MFIs were poverty alleviation and improving standard of living, women empowerment, development of small business and creation of employment opportunities MSEs in Tanzania are finding it difficult to access financial services due to lack of stable Micro-Finance Institution (MFIs) in the country.

1.4 Objectives of the Study

The objectives from this study is divided in to two general objective and specific objectives

1.4.1 General Objective

The main objective of this study was to assess the contribution of MFI services on the growth of MSEs in Tanzania.

1.4.2 Specific Objectives

- i. To identify the benefits of MFI on medium and small scale enterprises growth
- ii. To assess the impact of MFI loans on livelihood of Medium & Small Entrepreneurs
- iii. To assess the costs that medium and small enterprises incur when accessing the microfinance services.

1.5 Research Question

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

- i. What are the benefits of MFI on medium and small scale enterprises growth?

- ii. What are the impacts of MFI loans on livelihood of Medium & Small Entrepreneurs?
- iii. To what extent do small and medium enterprises incurred when accessing the microfinance services.

1.6 Significance of the Study

First, the study would contribute to the body of knowledge on the impact of microfinance on the growth of medium and small entrepreneurs taking into consideration the true cost incurred by MSEs apart from interest cost.

Second, this study would shed light on the relationship between microfinance services and growth of medium and small enterprise particularly with the focus on their livelihoods for both planners and policy makers in government, agencies and NGOs. This would help them to come out with substantive possible alternative policy interventions which might help to address problems and challenges which medium and small enterprises face.

Third, this study would show the impact of microfinance services on the growth of micro and small enterprises for use in short term and long term interventions especially in the fight against poverty. A study of this nature is equally very important because it is going to enlighten the government and the public on the role of MFI in the SMEs sector.

1.7 Scope and Limitation of the Study

To cover all the regions in the entire country was impossible because of the limited time frame and amount of funds for this research. For this reason, the research will cover only Dar-es-salaam region because it has large number of MSEs and high concentration of MFIs and also the region is well distributed therefore this region provided good source of data for the study. The impact of microfinance to the growth of SMEs in this area was analyzed, looking at its contributions, and in what form, and of course the response of MSEs to the contributions of this institution to them.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter provides literature review that comprises both theoretical literature review and empirical literature review. The chapter also provides the conceptual framework for the research study and finally research gap will be identified

2.2. Theoretical Literature

2.2.1 Definition of Concepts

Microfinance

URT (2000) defines Microfinance as the provision of financial services to the low income households, small holder farmers, and small and micro- enterprises in rural areas as well as in the urban areas to people who have poor access to financial services from formal financial Institutions. Under this definitions a range of financial services are covered, which include savings, credits, payments, and other services. Hence, clients use these services to support their enterprises and economic activities as well as their household financial management and consumption needs.

The World Bank (2007) defines microfinance as the provision of very small loans to low income clients for self employment, often with the simultaneous collection of small amounts of savings. The financial services are for people who lack access to the traditional banking services. The World Bank (2007) also identified and enumerated nine traditional features associated with “microfinance”. These include small transactions and minimum balances (whether loans, savings or insurance), loans for entrepreneurial activity, collateral free loans, group lending, target poor clients, target female clients, simple application processes, provision of services in underserved communities and market level interest rates.

Microfinance is the provision of appropriate financial services to significant numbers of low income and economically active people in order to improve their condition and local

economies. Financial services can include one or any combination of the following: lending, savings, insurance, pension/ retirement and payment services. (Kosiura 2001)

Microfinance services has been and increasingly become a popular intervention against women empowerment in developing countries, generally targeting poor women. It has been considered an effective vehicle for women's empowerment (Leach & Sitaram, 2002).

The argument behind Microfinance Institutions (MFIs) targeting women is that, women are good credit risk, are less likely to misuse the loan, and are more likely to share the benefits with others in their household, especially their children (Garikipati, 2008; Swain & Wallentin, 2009). Furthermore, it is argued that women's increasing role in the household economy will lead to their empowerment (Hunt & Kasynathan, 2002). Empowerment of women is one of the most important issues in Tanzania and beyond. It is viewed as a process in which women challenging the existing institutions to effectively improve their well-being and of their children.

2.2.2 Overview of SMEs in Tanzania

There is no consensus of SME definition as various countries had different definition depending on the phase of economic development and their prevailing social conditions. In this, various indexes are used by member economies to define the term such as number of employees, invested capital, total amount of assets, sales volume (turnover) and production capability.

Pass et al (2000: 194), define Small and Medium Size Enterprises (SMEs) as companies that have annual turnover of less than £ 11.2 million; Have gross assets of under £ 5.6 million; and Not more than 250 employees.

The criteria above especially cannot be adequately used to define SMEs in Tanzania. In the Tanzanian context SME definition can be borrowed from Wangwe (1999) and Massawe (2003). Wangwe argues that the definition of Micro and Small Enterprises (MSE) is slippery and has not been universally agreed upon. He defines micro enterprises

as those engaging 1-5 persons and small enterprises as those which engage 6-20 persons. MSE therefore are all those enterprises which engage between 1 and 20 persons. Masawe (*ibid*) defines Small and Micro Enterprises as those employing up to 4 persons; Small Scale Enterprises as those is employing 5-49 persons and Medium Size Enterprises as those employing 50-99 persons. Generally, therefore, one can take a working definition of SMEs as those employing between 6 and 99 persons.

An *enterprise* is another name for a business but it includes the idea of being bold, adventurous and taking risks. A person who sets up an enterprise is not afraid to try something new and is often referred to as an *entrepreneur*. It is useful to think of an entrepreneur as someone who creates jobs and employs other people. This sets the entrepreneur apart from someone who merely operates an existing business or who seeks employment. Enterprises range in size from very small to very large. Below are the four categories of enterprises that the Government of Tanzania recognizes.

- Micro enterprises: Employ from one (1) to four (4) person, and have a capital of up to five (5) million Tanzanian Shillings (Tshs). (1 USD was approximately equal to 1600 Tanzanian Shillings in January 2014.).
- Small enterprises: Employ from five (5) to 49 persons and have a capital of between six (6) and 200 million Tshs.
- Medium enterprises: Employ from 50 to 99 persons and have a capita of between 201 and 800 million Tshs.
- Large enterprises: Employ from 100 and above and have a capital of more than 800 million Tshs.

2.2.3 Importance of Small and Medium Enterprises

It is estimated that about a third of the GDP originates from the SME sector. According to the Informal Sector Survey of 1991, micro enterprises operating in the informal sector alone consisted of more than 1.7 million businesses engaging about 3 million persons that was, about 20% of the Tanzanian labour force. Though data on the SME sector are rather sketchy and unreliable, it is reflected already in the above data that SME sector plays a crucial role in the economy. Since SMEs tend to be labour-intensive, they create

employment at relatively low levels of investment per job created. At present, unemployment is a significant problem that Tanzania has to deal with. Estimates show that there are about 700,000 new entrants into the labour force every year. About 500,000 of these are school leavers with few marketable skills. The public sector employs only about 40,000 of the new entrants into the labour market, leaving about 660,000 to join the unemployed or the underemployed reserve. Most of these persons end up in the SME sector, and especially in the informal sector. Given that situation and the fact that Tanzania is characterised by low rate of capital formation, SMEs are the best option to address this problem.

SMEs tend to be more effective in the utilisation of local resources using simple and affordable technology. SMEs play a fundamental role in utilising and adding value to local resources. In addition, development of SMEs facilitates distribution of economic activities within the economy and thus fosters equitable income distribution. Furthermore, SME technologies are easier to acquire, transfer and adopt. Also, SMEs are better positioned to satisfy limited demands brought about by small and localised markets due to their lower overheads and fixed costs. Moreover, SME owners tend to show greater resilience in the face of recessions by holding on to their businesses, as they are prepared to temporarily accept lower compensation. (URT, 2012)

Through business linkages, partnerships and subcontracting relationships, SMEs have great potential to complement large industries requirements. A strong and productive industrial structure can only be achieved where SMEs and large enterprises not only coexist but also function in a symbiotic relationship. However, the linkages between SMEs and large enterprises are very weak in Tanzania. SME development Policy, therefore, creates the potential for enhancing linkages within the economy. In addition, SMEs serve as a training ground for entrepreneurship and managerial development and enable motivated individuals to find new avenues for investment and expanding their operations.

There are also opportunities indicating a bright future for SME sector development in Tanzania. This includes the various on-going reforms that are oriented towards private

sector development and, thus, lay the ground for SMEs development. In addition, the recognition of SME sector that it has higher potential for employment generation per capital invested attracts key actors to support SME development programmes. Since SME development does contribute significantly to poverty alleviation, resources earmarked for poverty alleviation will also be availed to the SME sector. Various initiatives towards improving the infrastructures and especially roads do provide an added opportunity for SME development. Furthermore, there are several ongoing schemes aimed at strengthening SME service providers such as Small Industries Development Organisation (SIDO), Vocational Education Training Authority (VETA), Micro Finance Bank (NMB) and various Industrial Support Organisations. These interventions do provide opportunities for growth of the SME sector. (URT, 2012)

Given the fact that Tanzania is endowed with abundant natural resources, the creation of enabling business environment will facilitate exploitation of these resources through SMEs. This is again an opportunity for SMEs development.

2.2.4 Financial Services and MSE

According to pecking order theory the firms prioritize their sources of funding starting from internal finance, debt and then equity. That is to say there is a tendency of the firms to go to loan option after they have exploited own internal savings or have none. Myers and Majluf (1984) argued that this is due to the fact that there exists information asymmetry between managers of the firms or enterprises (insiders) and investors (outsiders). Studies (World Bank, 2000; ILO, 2001) have shown that many MSEs lack access to finance for starting, operating and expanding their businesses. The estimated demand for MSE credit in Tanzania is 2.5 million borrowers, compared to about 50,000 borrowers being served currently (SIDO, 2002). The largest demand for credit is in the range of Tshs 50,000 to 500,000. Small and short-term loans (typically rising in stages 19

2.2.5 Small and medium enterprises and access to finance

A major barrier to rapid development of the SME sector is a shortage of both debt and equity financing. Accessing finance has been identified as a key element for SMEs to

succeed in their drive to build productive capacity, to compete, to create jobs and to contribute to poverty alleviation in developing countries. Small business especially in Africa can rarely meet the conditions set by financial institutions, which see SMEs as a risk because of poor guarantees and lack of information about their ability to repay loans. Without finance, SMEs cannot acquire or absorb new technologies nor can they expand to compete in global markets or even strike business linkages with larger firms (UNCTAD, 2002). Many factors are believed to be responsible for the refusal of loans and equity fund to SMEs by formal banks.

According to Cork and Nisxon (2000), poor management and accounting practices are hampering the ability of smaller enterprises to raise finance. This is coupled with the fact that small businesses are mostly owned by individuals whose personal lifestyle may have far reaching effects on the operations and sustainability of such businesses. As a consequence of the ownership structure, some of these businesses are unstable and may not guarantee returns in the long run.

According to Kauffmann (2005), access to formal finance is poor because of the high risk of default among SMEs and due to inadequate financial facilities. However, Cressy and Olofsson (1997) sum up constraints facing SMEs into two; these include demand-based (SMEs) and supply-based (formal banks) financial constraints. The duo define a supply-side finance constraint as a capital market imperfection that leads to a socially incorrect supply of funds to projects, or the incorrect interest rate charged on funds. They further define a demand-side financial constraint as a capital market imperfection in which performance of a firm is adversely affected by a factor internal to the firm. Thus for example, if the firm's owners would like to grow the firm faster, but the only way they can do this is to relinquish equity, and they refuse to do so, it may be said that the firm's demand for funds is demand-constrained. These deficiencies shall lead us to exploring other alternative financial sources for SMEs.

Amin et al (2003) used a unique panel dataset from northern Bangladesh with monthly consumption and income data for 229 households before they received loans. They find

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, are 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 (1999), 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 labor amongst poor people.

Mosley and Hulme (1998) 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.

Fatchamps (1997) 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 contends 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 labour 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 programmes results in a decrease in labour supply (income effect), it can negatively affect labour supply of particular type, for example male labour supply. As a result employment may decline, given the demand for labour. Therefore, the net impact cannot be determined a priori. Microcredit programmes seem to reduce wage-employment and income, but raise self-employment and corresponding income for programme- 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.

2.2.6 Micro-finance Services offered by Micro-Finance Institutions

Auren and Krassowska, (2004) indicated that “the provision of micro-finance services can be facilitated by business development services. These services can help build financial and business management capacity of rural households, improve their technical skills, provide local support services for enterprises with emphasis on marketing, and establish linkages between forest communities and micro-finance services. Business development services should grow with the development of small-scale enterprises and cater to their evolving needs”. Examples of useful business development services for improving access to micro-finance are: training of rural households in funds management, loan application, bookkeeping and accounting; preliminary loan appraisal of small-scale enterprise financial planning; consolidation of small individual proposals into a bankable portfolio of forest-based enterprise plans; and support to micro-finance institutions for monitoring and supervising the implementation of small-scale enterprise activities. Business development services can also help micro-finance institutions to assess risks related to small-scale

enterprises. Embedded services such as training to producers and quality control, provided by buyers of commodities, can also positively improve access to micro-finance services by increasing micro-entrepreneurs' skills and the marketability of their products. Customer Savings Service:

Worldwide micro-finance experience has shown, access to safe and flexible savings services can play a critical role in poor people's strategies for minimizing risks, mitigating income fluctuations, facing unexpected expenditures and emergencies, and building a small asset base over time. In particular, the very poor living in rural areas, who may lack investment opportunities and safe ways of keeping their savings, greatly value access to safe savings services. Most poor families do save and often in a non-financial form, for example, small gold items or stockpiling goods, because they frequently lack access to good formal savings facilities. In-kind savings are suboptimal options, because they are subject to fluctuations in commodity prices, and destruction by pests, fire and theft. While micro-finance institutions offer both good loan services and good voluntary savings services, worldwide experience shows that there is usually more demand for savings than for loans. Better availability of safe savings facilities increases self-financing capacity and thus reduces the need to borrow, with its inherent risks. When a poor household needs a relatively large amount of money for an investment purpose, saving is a less risky way to obtain it than taking on a debt with a fixed repayment obligation. Traditionally, micro-finance mobilization of savings has taken place in the form of compulsory savings under group or individual lending methodologies.

Often a percentage of the loan amount is required as mandatory savings and is meant to guarantee group loan repayment. Compulsory savings were also seen as a way to instill savings habits in poorer households. Experience has shown, however, that compulsory saving is not conducive to encouraging clients' saving habits, but rather is considered as one of the requirements for accessing loans. It is the mobilization of voluntary savings, ensuring safety, flexibility and accessibility, which can have the strongest impact on poor people's lives. With the right products and incentives, micro-finance institutions can rapidly mobilize very significant resources. Ensuring the existence of safe and accessible

savings services for forest-based small-scale enterprises should be a priority for any microfinance development programme. Possible ways for microfinance institutions to make the service available at lower costs include mobile banking, microfinance officers visiting rural communities on market days, and facilitating groups in collecting and depositing individual voluntary savings.

Krassowska, (2004), indicates that mobilizing the savings of small-scale enterprises implies risk, however, and microfinance institutions allowed to do so should clearly show their capacity to mobilize savings safely. Accordingly, they should demonstrate strong governance and professional management, strength and reliability, adequate internal controls, financial management and information systems, the guarantee that deposits and savings are not used to cover their operating expenses and records of strong loan portfolio quality management. In most countries, mobilization of public savings is restricted to banks, where regulations should be in place for effective supervision. Credit cooperatives are also a very important instrument for mobilizing savings, although generally limited to cooperative members. It is important that sound provisions regulating and supervising cooperatives' operations are in place to prevent governance weaknesses that would ultimately damage depositing members. Micro- Credit Service:

According to Thomas *et al.*, (2003) explained that “Micro-credit consists of small loans provided to poor households or micro-enterprises. Micro-credit is normally characterized by standardized loan products with short maturities, limited amounts, fixed repayment schedules and high interest rates. Most micro-finance institutions require potential borrowers to save before applying for a loan in order to demonstrate their intention to develop a long-term banking relationship. When the amount saved reaches a specific level, the lender will consider granting a certain amount as a loan. Although forced savings might be effective in helping to control moral hazard risks, they increase the effective interest rate and restrict potential borrowing. Small-scale enterprises, especially when engaged in wood forest production, may need financing for larger investments that have prolonged amortization periods”. Due to the gestation period, there is normally a significant time lag between the initial expenditures and the time when investment creates

a positive cash flow and the enterprise can repay the loan. While presenting the advantage of reducing transaction costs and credit risks, the traditional standardized micro-credit and group lending may not match their cash flow, and may not suit their investment requirements. Small-scale enterprises with intensive capital needs to finance fixed-term investments and that are engaged in higher risk activities are likely to face difficulties in accessing micro-credit that matches their demand, given its shorter maturities, limited amounts and fixed repayment schedules.

Wenner D (1995) argued that “Micro-credit is most often extended without traditional collateral”. If physical collateral were a requirement for borrowing, most MFI clientele would be unable to participate due to their extreme poverty level. Because borrowers do not have physical capital, MFIs focus on using social collateral, via group lending. Group lending encompasses a variety of methodologies, but all are based on the principal of joint liability. In essence, the group takes over the underwriting, monitoring, and enforcement of loan contracts from the lending institution

Auren & Krassowska, (2004) further indicates that “for small-scale enterprises in Uganda (within and outside the forest sector), finances and financial management represent one of the greatest constraints to effective operations”. Few financial products are available to Ugandans other than bank loans. There are many problems accessing finance in Uganda, due to its relatively underdeveloped financial sector, and this particularly affects sustained investment in long-term ventures such as forestry. For many small-scale enterprises it is extremely difficult to get a loan, since it involves undertaking effective budgeting and cash flow projections, preparing business plans, maintaining solvency and liquidity, providing collateral, managing accounts and providing accurate financial records for external investors or tax authorities. Furthermore, many of these enterprises operate as one of many parallel business ventures, and their finances tend to flow between them, sometimes causing problems of cash flow and liquidity. Small-scale enterprises that cannot get a loan must resort to informal lending at very high interest rates or rely on personal connections.

Biryabarema, E. (1998), reports that Microfinance institutions typically provide short-term loans for small amounts of capital, while small-scale enterprises often need longer-term and larger loans. There is often a lack of cooperation between banks and forest sector. A better appreciation of the specific and long-term nature of forestry investment is necessary for banks to understand operating requirements for small-scale enterprises. While there may be interest in investing in tree planting, for example, there is generally insufficient widespread ability to invest in a sector that yields only long-term benefits. A saw log production fund is being established, overcoming the problem of access to long-term finance for small- to medium-scale plantation development.

The fund will be operated as an independent entity through a management agent or bank, and will provide a mix of grants and credits targeting small to medium-sized private investors and organized groups. In a modern financial sector there are products such as asset leasing and venture capital. In Uganda, no such services yet exist, and government regulations do not allow or recognize the modern concept of leasing. If leasing were clarified and made more available, it would provide opportunities for small-scale enterprises to commence or expand operations. However, a Financial Institutions Bill (2003) is being discussed that further clarifies taxation and obligations of all parties under leasing agreements. Equity facilities provide much-needed finance to small- and medium-scale enterprises worldwide. In Uganda, equity financing is limited, largely due to the loss of social capital stemming from years of civil unrest, which has resulted in general mistrust between lenders and receivers of credit beyond close family ties. Krassowska (2004). MFIs provide similar products and services to their customers as formal sector financial institutions. The scale and method of delivery differ, but the fundamental services of savings, loans, and insurance are the same. Notwithstanding, to date most efforts to formalize micro-finance have focused on enterprise lending (loans for enterprise formation and development) which remain by far today the dominant product offered by MFIs (Nourse (2001).

Woller (2002) remarked that “Increasingly today, MFIs have begun to offer additional products, such as savings, consumption or emergency loans, insurance, and business

education”. But Nourse (2001) reviews the context and rise of micro-finance products and argues there is a need for savings and insurance services for the poor and not just credit products. He goes on to argue that MFIs need to provide tailored lending services for the poor instead of rigid loan products. Supporting this latter assertion of Nourse (2001), Eyiah (2001) develops a model of small construction management contractors and MFIs in developing countries that provides a tailored lending structure for micro enterprise contractors. Similarly, Woller (2002a), Cohen (2002), and Dunn (2002) argue that MFIs need to be more client-focused, including offering a mix of financial products tailored to the varied needs and wants of poor consumers.

2.2.7 Role of the Entrepreneurs in Business formation and Growth

These theories considered differences in attitudes and abilities among individuals as critical issues in determining why some small firms grow and others do not. Two schools of thought, the Austrian School and the Classical Economist were the first to acknowledge the role of the entrepreneur in small business development; they recognize the entrepreneur as an individual with special characteristics. Knight (1921) described an entrepreneur as someone that has the willingness and superior ability to make decisions, raise capital and assume the risk of failure. In the same vein, Schumpeter (1939) added among other things, the fact that an entrepreneur has the superior ability to perceive new market opportunities. He sees the entrepreneur as an innovator.

According to the Austrian school, people have certain characteristics that are associated with the productivity for entrepreneurship. Individuals who have more of these characteristics are more likely to become entrepreneurs than those who have fewer. An individual chooses to create a new business so as to maximize his expected utility. This utility is a function of entrepreneurial activity or wage income, and of attitudes that affect the utility that the person derives from entrepreneurial activity, such as one's taste toward work effort, risk, independence, working close to customers, etc. Income, in turn, depends on the individual's ability to generate profit, such as managerial abilities to raise capital, and abilities to perceive new market opportunities and to innovate (Papadaki and Chami, 2002).

The classical school, have extended analysis of the decision to start a business to that of the decision to grow the business. According to Davidson (1989, 1991), firm growth is an indication of continued entrepreneurship. Davidson notes that economic theories take the willingness to grow a business for granted, by assuming profit maximization. However, empirical evidence suggests that small business owners are reluctant to grow even if there is room for profitable expansion and that profitable firms of different sizes co-exist within industries.

According to Papadaki and Chami (2002), theories on small business growth and development view business growth from an organizational life cycle perspective, which sees growth as a natural phenomenon in the evolution of the firm, other perspective sees growth as a consequence of strategic choice. It is obvious that attributes of the business owner, organizational resources and environmental opportunities are crucial in expanding the firm and in overcoming the barriers to the evolution of the firm from one stage to the next. Sexton and Smilor (1997), and Carland et al., (1984) distinguished between a business owner and an entrepreneur. According to them, an entrepreneur is committed to the growth of the business. Growth is the very essence of entrepreneurship," and commitment to growth is what primarily distinguishes small business owners and entrepreneurs.

2.2.8 SMEs and Growth

It is evident from literature that not all small businesses are growth oriented and for certain firms" growth is a voluntary choice (Masurel and Montfort, 2006). An empirical study of SMEs growth pattern by Kolvereid and Bullvag (1996) concluded that growth intentions may be used to predict actual growth, that past intentions are related to later intentions, and that change in growth intentions are associated with changes in growth patterns. Arbaugh and Sexton (1996) provided empirical evidence that most new firms do not grow into large ones and that there is no relationship between the age of a firm and its size. Chaston and Mangles (1997) opined that there is no single strategy to firm growth. Hence, the probability of achieving growth is increased by avoiding excessive emphasis on single-strategy transformation initiatives, and by giving different capabilities priority

depending upon the development stage of the firm. They identified three factors that could limit the growth of small business to include ability, need and opportunity. Kolveired (1992) concluded that small business entrepreneurs who wanted their firms to grow started their business in order to achieve just that. The process of mutual adjustment between proprietors and their employees was identified by Goffee and Scase (1995) as a major constraint limiting factor to small business growth.

2.2.9. Organization of Microfinance Institutions

2.2.9.1 Cooperative financial institution

This is a financial institution that can be termed semiformal. It constitutes credit unions, savings and loan cooperatives and other financial cooperatives. They are generally identified as credit unions or savings and loan cooperatives and provide savings and credit services to its members. There are no external shareholders and run the same as a cooperative and implementing all its principles. Members who are at the same time customers make the policy of the cooperative. They are either elected or work on voluntary bases. They are not often subjected to banking regulations but have their own regulations and are under the supervision of the ministry of finance of the country.

Individual financial cooperatives in a country are often govern by a league that coordinate activities of these credit unions, trains and assist its affiliates, act as a place where the deposit and provide inter lending facilities and act as a link between external donors and the cooperative system (Schmidt, 1997) .They raise capital through savings but to receive loans is not easy. Loans are delivered following the minimalist approach where the requirements for loans are not often difficult to meet by customers; little collateral, character and co-signing for loans between members. These loans are usually loans within the savings of the member (Schmidt, 1997).

2.2.9.2 Group Lending

This method of providing small credits to the poor is most use by microfinance that provides loans without collateral. The interest charge is around not much different from that of commercial banks but far lower than interest charge by individual by money

lenders (Natarajan, 2004). The Grameen bank is a typical example of microfinance institution using this method. The repayment rate is very high since each member is liable for the debt of a group member (Stiglitz, 1990). Group formation is made by members who know themselves very well or have some social ties. Loans are not granted to individuals on their own but to individuals belonging to a group; and the group acts as a collateral which is term social collateral. This is to avoid the problems of adverse selection and also to reduce costs of monitoring loans to the members who must make sure the loan is paid or they become liable for it (Armendariz, 1994).

2.2.9.3 Individual Lending

This is the lending of loans to individuals with collateral. Besley and Coate (1995), say despite the advantages of lending to groups, some members of the group may fail to repay their loan. Montgomery (1996) stresses that this method of lending avoids the social costs of repayment pressure that is exerted to some group members. Stiglitz (1990) highlights that members in group lending bear high risk because they are not only liable for their loans but to that of twenty-two group members. Navajas et al. (2003) and Zeitinger (1996) recommend the importance of routine visits to the clients to make sure the loan is use for the project intended for. These monitoring is vital but at the same time increases the cost of the microfinance institution.

2.2.9.4 Self-help groups (SHG)

This is common among women in the rural areas who are involved in one income generating activity or another (Ajai, 2005). Making credit available to women through SHGs is a means to empower them. This group is an institution that helps its members sustainably with the necessary inputs to foster their lives. SHG provides its members with not only the financial intermediation services like the creating of awareness of health hazards, environmental problems, educating them etc. These SHGs are provided with support both financial, technical and other wise to enable them engage in income generating activities such as; tailoring, bee keeping, hairdressing, weaving etc. It has a bureaucratic approach of management and are unregistered group of about 10 – 20 members who have as main priority savings and credit in mind (Ajai, 2005). The members

in the SHG have set dates where they contribute a constant and equal sum as savings. These savings are then given out as loans to members in need for a fixed interest rate (Bowman, 1995).

2.2.9.5 Village Banking

This is a method of lending to individual members to have constant access to money for their Micro-enterprise daily transactions (Mk Nelly and Stock, 1998). Borrowers are uplifted using this method because they own SME that earn money sustainably. This enables them to acquire a larger loan sum which gives them higher profit when introduced into the business and of course the interest with this high sum is high making the bank financial sustainable. Village banking as of the 90s has gained grounds and certain adjustments are made to suit partner institutions (Nelson et al; 1996). Hatch and Hatch (1998) Village banking loan and savings growth rate increases as the bank continue to exist.

2.2.10. The Factors that Affect SME's Access to Credit

The type of population to be served and the activities that the target market is active in and also the level or stage in development of the business to be financed is determined by the MFIs. SMEs differ in the level in which they are and the products and services offered to them by the MFIs are towards meeting the demands of the market. SMEs are financed differently and the financing is determined by whether the firm is in the start-up phase or existing one and also whether it is stable, unstable, or growing. The type of activities that the business is involve in is also determined and this can be; production, commercial or services activities (Ledgerwood, 1999).

a) Start-up or existing SMEs

In identifying the market, MFIs consider whether to focus on already existing entrepreneurs or on potential entrepreneurs seeking for funds to start up a business venture. Working capital is the main hindrance in the development of already existing SMEs and to meet up, the borrow finance mostly from informal financial services such as; families, friends, suppliers or moneylenders. The finances got from these informal financial services have high interest rates and services offered by the formal sector or not

offered by these informal financial services. MFIs see it less risky to work with existing microenterprises because they have a history of success (Ledgerwood, 1999).

Businesses that are financed by MFIs from scratch consider that they will create an impact in the society by alleviating poverty by increasing their level of income. An integrated approach lay down the foundation for start-up businesses to pick up since financial services alone will not help them. They need other services such as skills training and to equip them with all the necessary tools that can hinder them from obtaining loans. Existing businesses with part of their capital being equity is preferred by most MFIs to work with since the level of involvement is high and consequently lower risk (Ledgerwood, 1999).

b) Levels of SME development

MFIs provide their products and services based on the level of development of the businesses. SMEs can be grouped into three main levels of business development that profit from access to financial services.

- i) Unstable survivors** are groups that are considered not credit worthy for financial services to be provided in a sustainable way. Their enterprise are unstable and it is believe they will survive only for a limited time and when MFIs focus on time to revert the situation by providing them other extra services, it is noticed that costs increases and time is also wasted.

- ii) Stable survivors** are those who benefit in having access to the financial services provided by MFIs to meet up with their production and consumption needs. Stable survivors are mainly women who engage in some sort of business activities to provide basic needs such as food, child health, water, cooking for the household, etc. These types of microenterprises rarely grow due to low profit margins which inhibit them to reinvest and an unstable environment due to seasonal changes which makes them to consume rather than to invest in the business.

- iii) **Growth enterprises** are SMEs with high possibility to grow. MFIs focusing on these types of microenterprise are those that have as objective to create jobs, and to move micro entrepreneurs from an informal sector to a formal sector. MFIs prefer to provide products and services to meet the needs of this group since they are more reliable and posing them the least risk (Ledgerwood, 1999).

2.2.11 Small and medium enterprises and access to finance

A major barrier to rapid development of the SME sector is a shortage of both debt and equity financing. Accessing finance has been identified as a key element for SMEs to succeed in their drive to build productive capacity, to compete, to create jobs and to contribute to poverty alleviation in developing countries. Small business especially in Africa can rarely meet the conditions set by financial institutions, which see SMEs as a risk because of poor guarantees and lack of information about their ability to repay loans. Without finance, SMEs cannot acquire or absorb new technologies nor can they expand to compete in global markets or even strike business linkages with larger firms (UNCTAD, 2002). Many factors are believed to be responsible for the refusal of loans and equity fund to SMEs by formal banks. According to Cork and Nixson (2000), poor management and accounting practices are hampering the ability of smaller enterprises to raise finance. This is coupled with the fact that small businesses are mostly owned by individuals whose personal lifestyle may have far reaching effects on the operations and sustainability of such businesses. As a consequence of the ownership structure, some of these businesses are unstable and may not guarantee returns in the long run. According to Kauffmann (2005), access to formal finance is poor because of the high risk of default among SMEs and due to inadequate financial facilities. However, Cressy and Olofsson (1997) sum up constraints facing SMEs into two; these include demand-based (SMEs) and supply-based (formal banks) financial constraints.

The duo define a supply-side finance constraint as a capital market imperfection that leads to a socially incorrect supply of funds to projects, or the incorrect interest rate charged on

funds. They further define a demand-side financial constraint as a capital market imperfection in which performance of a firm is adversely affected by a factor internal to the firm. Thus for example, if the firm's owners would like to grow the firm faster, but the only way they can do this is to relinquish equity, and they refuse to do so, it may be said that the firm's demand for funds is demand-

2.2.12 Relationship between Micro-finance Services and Small, Medium Enterprises

Various scholars explain significant relation between the availability of micro-finance alongside the growth of the small scale and medium enterprises worldwide. From several studies carried out while analyzing four programs in Bolivia, Mosley (2001) shows that assets and income increased commensurate with initial poverty levels, but also that MFI services may increase vulnerability if borrowers over-leverage. Bolnick and Nelson (1990) find that MFI participation had a positive impact on enterprises that were typically small, labor intensive and growing, although the impact was far from uniform across sectors and target variables. Copestake et al. (2001), find that borrowers who were able to obtain two loans experienced high growth in profits and household income compared to a control sample, but borrowers who never qualified for the second loan were actually worse off due to MFI collection mechanisms.

Wydick (1999a) finds that upward class structure mobility increases significantly with access to credit. Using the same Guatemala data set in a subsequent study (2002), Wydick also finds that rapid gains in job creation after initial credit access were followed by prolonged periods of stagnant job creation. Dunn (2001) finds that program clients' enterprises performed better than non-client enterprises in terms of profits, fixed assets, and employment. Edgcomb (2002), Cook et al. (2001), and Dumas (2001) each use case methodology to analyze MFIs offering integrated business development training. They conclude that business development training significantly improves micro-enterprise performance and micro-entrepreneur empowerment. A final issue meriting mention is provision of equity in lieu of credit for enterprise formation and start-up capital. Pretes and Seibel (2002) discuss several cases of this practice in East Africa. They refer to this service as providing enterprise equity; however, in finance vernacular, this service would most likely be considered a grant.

2.4 Empirical Literature View

SME remains one of the most reviewed topics in literature, especially as its impact on all kind economies cannot be overlooked. Worldwide, the SMEs have been accepted as the engine of economic growth and for promoting equitable development. The major advantage of the sector is its employment potentials at low capital cost. The labor intensity of the SME constitutes over 90% of total enterprises in most of the economies and is credited with generating the highest rate of employment growth and account for major share of industrial production and exports (Government of India, 2007), and the rapid expansion of small enterprises in economies of developed countries in the 1980s and 1990s has created a widespread conviction that small, new ventures are the most important source of entrepreneurship and as a dynamic and innovative factor, they contribute directly to economic growth. (Piotr and Rekowski, 2008) However, the SMEs sector is faced with many constraints. Among them is the most pressing one known to be financing.

Mosley (2001), in his research on microfinance and Poverty in Bolivia, assessed the impact of microfinance on poverty, through small sample surveys of four microfinance institutions. Two urban and two rural, using a range of poverty concepts such as income, assets holdings and diversity, and different measures of vulnerability. All the institutions studied had on average, 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. The studies revealed also that in comparison with other anti-poverty measures, microfinance appears to be successfully and relatively cheap at reducing the poverty of those close to the poverty line. However, it was revealed to be ineffective, by comparison with labour-market and infrastructural measures, in reducing extreme poverty.

Nichols (2004) 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.

Review study in Tanzania.

In Tanzania several studies has been done on microfinance institutions service, one of the researcher who have done research on MFI service is Kuzilwa and Mushi (1997) examined the role of credit in generating entrepreneurial activities. He used qualitative case studies with a sample survey of business that gained access to credit from a Tanzanian government financial source. The findings reveal that the output of enterprises increased following the access to the credit. It was further observed that those 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.

Chijoriga (2000) evaluated the performance and financial sustainability of MFIs in Tanzania, in terms of the overall institutional and organizational strength, client outreach, and operational and financial performance.²⁸ MFIs and 194 MSEs were randomly selected and visited in Dar es Salaam, Arusha, Morogoro, Mbeya and Zanzibar regions. The findings of this revealed that, the overall performance of MFIs in Tanzania is poor and only few of them have clear objectives, or a strong organizational 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. In conclusion, the author pointed to low population density, poor infrastructures and low house hold income levels as constraints to the MFIs' performance.

Rweyemanu et al (2003), he evaluated the performance and constrains facing semi-formal microfinance institutions in providing credit in Mbeya and Mwanza regions. The primary data were collected through a formal survey of 222 farmers participating in the Agriculture Development Programme in Mbozi and the Mwanza Women Development Association in Ukerewe .In the analysis of their study the interest rates were found to be a significant barrier to the borrowing decision. Also the borrowers cited other problems like

lengthy credit procurement procedures and the amount disbursed being inadequate. On the side of institutions, Mbeya and Mwanza credit programme 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-repayment.

In a study conducted by Kessy & Urio (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 (T) Ltd 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.

Generally Small and Micro Enterprises face considerable problems in seeking funds necessary to innovate. Intangible activities like R&D or innovation are considered riskier, so that these enterprises face a higher cost of capital. Yet, often intangible assets are undervalued when being used as collateral for credit. These result in reductions in the amount of capital debt rise. Considering this, MSEs investing in technology and innovation have a higher chance of finding difficulties in accessing credit than other MSEs which focus on more traditional businesses. High transaction costs, the risk connected to their business, the limited possibility to appropriate innovations and the difficulties of lenders to understand the real value of innovative projects are all factors that seem to limit the capability of innovative MSEs to raise external funds (Stiglitz, 1993)

2.5 Conceptual Framework

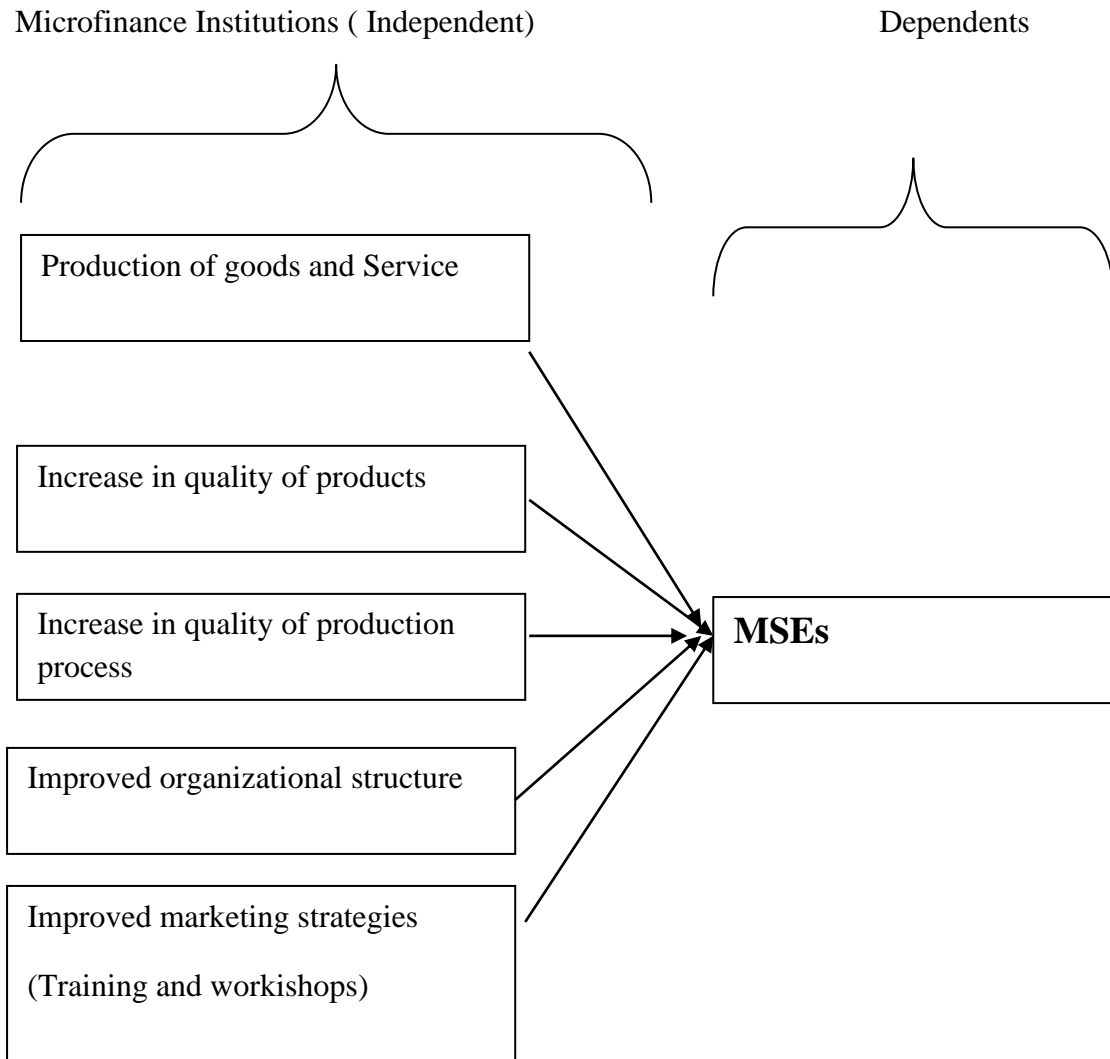
A concept is an image or symbolic representation of an abstract idea. Chinn and Krammer (1999) defined the concept as a complex mental formulation of experience. While the

theoretical framework is the theory on which the study is based, the conceptual framework is the operationalization of the theory.

Independent variable is the variable that stands alone and is not changed by the other variables you are trying to measure whereas dependent variable is something that depends on other factors. Conceptually, the MSE (dependent variable) which is described have based upon five theoretical assumption on Financial institutions which are Production of goods and Service, Increase in quality of products, Increase in quality of production process, Improved organizational structure, Improved marketing strategies, (Training and workshops) (independent variables).

With MFIs that have favorable terms and conditions for investments in innovation activities, MSE will be able to acquire loan. These loans will then be invested by MSE activities through training, workshop, acquiring of new machinery etc. The result of this is an increase in quality of products, production processes, market strategies and better organizational structure of the MSE. This will increase in output that result into an increase in income and more MSEs will come and apply for loans

Figure 2.1 Conceptual Framework



Source: Researcher construction, 2014

2.6 Research Gap

Based on the above study reviewed, it is evident that much of the studies related to this study have been done. Kessy & Urio (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. Rweyemanu et al (2003), he evaluated the performance and constrains facing semi-formal microfinance institutions in providing credit in Mbeya and Mwanza regions. Chijoriga (2000) evaluated the performance and financial sustainability of MFIs in Tanzania, in terms of the overall institutional and organizational strength, client outreach, and operational and financial performance. Nichols (2004) used a

case study approach to investigate the impact of microfinance upon the lives of the poor in the rural China. Mosley (2001), in his research on microfinance and Poverty in Bolivia, assessed the impact of microfinance on poverty, through small sample surveys of four microfinance institutions. The literature review show that there is nothing the scholars have been able to highlight on assess the contribution of MFI services on the growth of MSEs in Tanzania with a case study of EFC

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter provides a description of research design, study population, sampling design which include the sampling method, sampling procedures and sample size, sources of data, data collection methods, data processing, analysis and presentation.

3.2 Study Area

The study was conducted at the EFC Microfinance institution by visiting individual staff and customers to collect information related to MSEs. The reason for selecting EFC Microfinance is from the fact that This research study was conducted at EFC office in Dar-es-salaam region. The researcher selected this area because there are many SMEs with different life background and lifestyle in terms of education, culture, believes characteristics

3.3 Research Design

This study used descriptive method by using both qualitative and quantitative techniques. To make this study effective a case study will be used. This research design enabled the researcher to report not only the findings but also analysing, comparing and interpreting data. The data that will be collected by using a questionnaire which will be administered to staff and customers of EFC

Research strategy was guided by research question(s) and objectives, the extent of existing knowledge, time and other resources available as well as philosophical underpinning. The rationally of using this method was that the case study are flexible hence it was easier to make intensive research, the method is easily to be verified on the spot through observation and is also both time and cost effective taking into account the time and funds allocated for conducting this study

3.4 Population of the study

Population includes all members of a defined group that we are studying or collecting information on for data driven decisions. For this study the population of study was employee and customers of EFC. EFC is among the microfinance which has more offices almost every region in Tanzania and more customers

3.5 Sample Size

Sample size is an optimum sample is the one which fulfill the requirement of efficiency, representativeness, reliability and flexibility. Also the sample size is the exact number of items selected from a population. The study included 125 respondents where by 5 were EFC management staff, 30 were ordinary staff and 90 were MES respondents

3.6 Sampling Techniques

Sampling techniques as a selection of some part of an aggregate or totality of what the population is made. Sampling procedure are techniques which are used to determine the number of respondents that were involved in the study so as to provide the necessary knowledge. In this study purposive and random sampling techniques were employed.

3.6.1 Purposive Sampling Technique

Purposive sampling is based on researcher's judgment and purpose of the study. This technique was used to 5 administrative staff. In purposive sampling the units are selected according to the researcher's own knowledge and opinion about which ones they think was appropriate to answer the research objectives, and thus the sample selection was based entirely on their opinion of who are the most appropriate respondents to select.

3.6.2. Random Sampling

Random selection each individual is chosen randomly entirely by chance, such that each individual has the same probability of being chosen at any stage during the sampling process and each subset of individuals have the same probability of being chosen for the sample as any other subset of individuals. For this study, random selection was applied to 30 respondents who were operations department staff and 90 customers who were MSE from EFC financial institution

3.7 Type of Data to be used

There are two types of data which were the primary data and the secondary data. These data were expected to supplement each other.

3.7.1 Primary Data

In this study primary data were collected through the use of self administered questionnaires and interview.

3.7.1.1 Interview

Interview refers to the verbal interaction between interviewer and interviewee. This is designed to collect information, views and an opinion from respondents. The researcher obtain information on financial information and how customer benefits with loans from EFC microfinance. The study was used to select 5 respondents from the management staff

The researcher tall scores and tabulates all the responses in the provided interview questions. Moreover, the interview was structured, it contains a list of specific questions and the interviewer deviated from the list or injects any extra remarks into the interview process. The interviewer encouraged the interviewee to clarify vague statements or to further elaborate on brief comments. Otherwise, the interviewer attempted to be objective and try not to influence the interviewer's statements. The interviewer shared his own beliefs and opinions. The structured interview is mostly a "question and answer" session. (As attached in appendix ii)

3.7.1.2 Questionnaire

This method of data collection is quite popular, particularly in a case of large inquires. There are two broad categories of questions that are used in questionnaires such as structured or closed ended and unstructured or open ended questions. Closed-ended question refers to question which are accomplished by list of all possible alternatives from which respondents' select answers that describe their situation while open-ended question refers to question which give the respondent complete freedom of response. These free responses permit an individual to respond in his or her words. Structured and unstructured

questions were distributed to the respondents. Questionnaires were used to 30 respondents from operations department staff and 90 customers who were MSE from EFC Microfinance. (As attached in appendix i)

3.7.2 Secondary Data

During the study the researcher gathered further information through internet and reading various publications, reports, books and materials relevant to the study

In this research, documentary review was used as a secondary source of data, and a means of triangulating the data collected through questionnaires and interviews. The documents review were circulars, manual, regulations and reports that were generated within a year by the EFC Microfinance.

3.8 Data Collection Techniques

This is a systematic collection of information concerning the problem under the study. There are two sources of data namely primary and secondary sources of data. Therefore, primary and secondary sources of data were used.

3.9 Data Processing

The collected data were analyzed by using Statistical package for Social science (SPSS) and Microsoft Excel. Then the results were presented by means of words, numbers and percentages in the form of tables, charts and graphs. Data analysis and interpretation enabled the researcher to get a clear understanding of the research findings and use those findings to arrive at a conclusion and make recommendations.

CHAPTER FOUR

DATA PRESENTATION, ANALYSIS AND DISCUSSION OF FINDINGS

4.1 Introduction

This chapter presents data presentation, analysis and discussion of the finding. The chapter is divided into two parts, part one discusses general overview of respondents and part two deals with the general description of the respondents.

The primary data that were collected from the field has been presented and analyzed by using Microsoft excel and statistical package for social science (SPSS) and discussed in order to give meaningful information. The study aimed at assessing the contribution of MFI services on the growth of MSEs in Tanzania, with a case of EFC. EFC employee and customers were used as a sample, the study divided the respondent in three categories the management, subordinates at different department and customers.

4.2 Respondent Rate.

The sample size of 125 respondents were expected to be used in this study, where as 30 respondents were from EFC employee and 90 respondents were EFC customers 125 questionnaires and interview were conducted at the field of respondents, 120 responses were collected from the questionnaires and interview conducted to the field of respondents, this represent a response rate of 96 % of total distributed/conducted interview and questionnaires. However because of some of employees went for a leave for longtime and others were out of the office for long time some of respondents did not return the questionnaires provided regardless of the effort made by the researcher to convince them from time to time.

Table 4.1 : Response Rate the Respondents (N=120)

	Distributed Questionnaires	Collected questionnaires	Actual Percentage
Management	5	5	100%
Employees	30	25	83.3
Customers	90	90	100
Total	125	120	92%

Source: Field Data (2014)

As shown in the Table 4.1 above, 125 questionnaires were distributed to all respondents but only 120 questionnaires were collected. 120 responses were obtained from the questionnaires and interview conducted to the respondents, this represented a response rate of 92 % of total distributed questionnaires.

4.2 The Demographic Characteristics of Respondents.

In this part, the sample demographics were fully analyzed. For this study the demographic observed included gender, age, level of education and working experience. The review of these characteristics gave some insights as to why the answers of the respondents may vary according to the demographic of respondents.

4.2.1 Gender of Respondents

Sex or gender of respondents was sought by the researcher in order to examine the relationship between gender and the contribution of MFI services on the growth of MSEs in Tanzania. The finding shows that 74(61.7%) of respondents were female and the remaining 46(38.3%) were male. The structure is clearly described in table 4.2 below.

Table 4.2. Gender of Respondents

	Gender	Frequency	Percent	Valid Percent
Valid	Male	46	38.3	38.3
	Female	74	61.7	61.7
	Total	120	100.0	100.0

Source: Field Data (2014)

The researcher revealed that female from the EFC employee and customers respondents had got highest frequency as shown on a table above, it was about 61.7 of all respondents. The finding from a table above implies that respondents participated in this study in terms of gender there was no gender balance between respondents, this may be due to the nature of finance which is microfinance whereby the most customers were female since most of them are participating in small business like food vendor and other small jobs. Therefore nature of SMEs is among the factors mostly influence MFI borrower

4.2.2 Respondent's Age

This question was asked to all respondents about their age, Majority of respondents were the age between 31-40 making 52(43.3%), 41(34.2%) of respondents were aged between 18-30, 19(15.8%) of respondents were at the age between 41-50, and the last group 8(6.7%) of respondents were the age above 50 years. The structure is clearly described in Table 4.3 below.

Table 4.2: Age Profile of Respondents

	Age	Frequency	Percent	Valid Percent	Cumulative Percent
Valid	18-30	41	34.2	34.2	34.2
	31-40	52	43.3	43.3	77.5
	41-50	19	15.8	15.8	93.3
	Above 50 yrs	8	6.7	6.7	100.0
	Total	120	100.0	100.0	

Source: Field Data (2014)

Out of the three categories Management, employee and customers of EFC it was noted that the age difference was not much deviation with respect to age as most fall at the age between 18-40 This implies that with this large number of respondents fall under that age due to the nature of their business, most of them have not attended high level of education as they are doing small business due to the capital they possess, as large number of them

are still entrepreneurs so their dealing with small scale business as opposed to other older age who deal with large scale business.

4.2.3 Education Level Attained by the Respondents

The researcher was interested to know the educational level of the respondents. Out of 120 respondents 39(32.5%) of respondents were secondary level, 26(21.7%) of respondents were diploma holders followed by 23(19.2% of respondents were primary level, 18(15%) were degree holders and only 8(6.7%) of the respondents had a master degree. Table 4.4 below provide a brief description.

Table 4.4: Education Level Attained by the Respondents

	Education	Frequency	Challenges	Valid Percent	Cumulative Percent
Valid	Primary	23	19.2	19.2	19.2
	Secondary	39	32.5	32.5	51.7
	Diploma	26	21.7	21.7	73.3
	Advanced Diploma	6	5.0	5.0	78.3
	Degree	18	15.0	15.0	93.3
	Master	8	6.7	6.7	100.0
	Total	120	100.0	100.0	

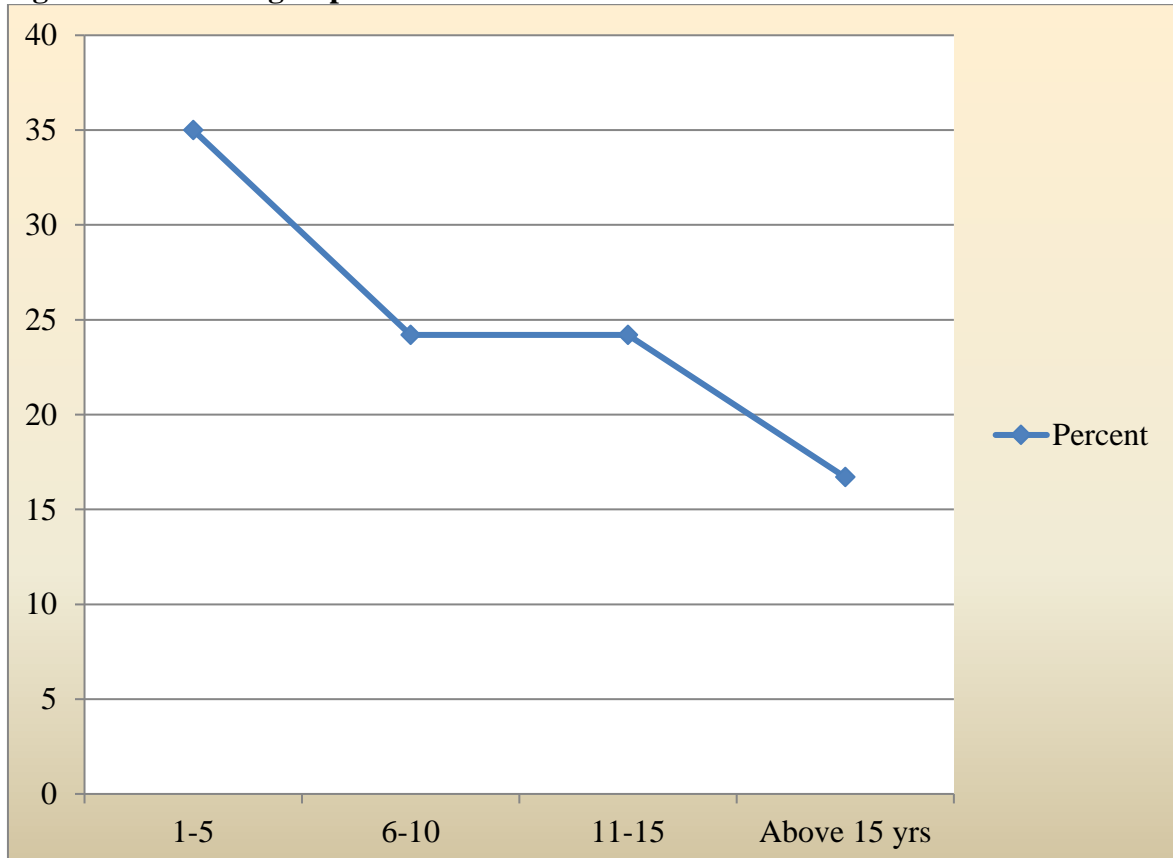
Source: Field Data (2014)

Data from a table above implies that most of respondents who answered questionnaire concerning the assessing the contribution of MFI services on the growth of MSEs have secondary level, diploma and primary education. At this demographic, a researcher believed that knowing education of respondents was good so as to understand their ability on dealing with business, nature and size of the business. From this findings it implied that most of the SMES are doing small business which require a minimal level of education and those with degree and master were MFI employees also their education gave hope to the research that all information that was been given was true based to their knowledge.

4.2.4. Working Experience

The question was asked to the respondents about their experience at the at their business together with MFI employees. The finding shows that 42(35%) of respondents had an experience of 1-5 years, 29(24.2%) of respondents had the working experience of 6-10 and 11-15 years and 20(16.7%) of respondents had the working experience of above 15 years and 20(16.7%) of respondents more that 15 year. Table below shows more details.

Figure 4.1: Working Experience



Source: Field Data (2014)

The finding from figure 4.1 above implied that the working experience for staff is largely from 1-5 followed by 6-10 and 11-15years which account for 35% and 24.2% each of the total respondents. Researcher think of having considerably fewer numbers of employees provided there is a good financial yield. Beyond 5 years working experience the workers are very few about 16.7% of the total respondents. This implies that most of SMEs have very short period with their business as their SMEs with small business. The important for those having experience is easier for them to adhere financial regulations, to access loan

easily due to possession of collateral and wide networking in business for customers and financial institutions which make them to have a confidence and multiple business acquired due to its up and down of the business as opposed to other new SMEs.

4.3 The benefits of MFI on medium and small scale enterprises growth

The first objective aimed at finding the benefits of MFI on medium and small scale enterprises growth. In order for the researcher to attain this objective, respondents were asked various questions that were intending to reach at the above specific objective as they are indicated below with their responses.

4.3.1 Sources of Business Capital and Adequacy of Capital for Business

The respondents were asked about the source of business capital and adequacy of capital for business. The findings showed that 82(68.3%) of respondents said they get capital from banks and MFI, 18(15%) of respondents said they get capital from friend and 8(6.7%) of respondents said they get capital from self sources. As shown in table 4.5 below

Table 4.5 . Sources of Business Capital and Adequacy of Capital for Business

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Self	8	6.7	6.7	6.7
	Friend	12	10.0	10.0	16.7
	Partnership	18	15.0	15.0	31.7
	Loans from banks and MFI	82	68.3	68.3	100.0
	Total	120	100.0	100.0	

Source: Field Data (2014)

The findings from table above indicated that most of the SMEs get business capital for their business loans from banks and MFI as 68.3% of respondents indicated. This analysis

also brought to bear that, the sample of this study is mainly associated with respondents who always deal with the MFIs. However, it was unanimously agreed among all respondents that the capital for the operation of their businesses are not adequate as per the demand of goods and services they need for their operations. Implications when capital are not adequate is to take loan from different sources which lead to make business to take long time to provide profit as opposed to whom got enough capital who take short time to make a profits and make the business to prosper.

In relation to other scholars on source of capital and benefit of MFI on medium and small scale enterprises growth, Thomas *et al.*, (2003) explained that “Micro-credit consists of small loans provided to poor households or micro-enterprises. Micro-credit is normally characterized by standardized loan products with short maturities, limited amounts, fixed repayment schedules and high interest rates. Most micro-finance institutions require potential borrowers to save before applying for a loan in order to demonstrate their intention to develop a long-term banking relationship. When the amount saved reaches a specific level, the lender will consider granting a certain amount as a loan. Although forced savings might be effective in helping to control moral hazard risks, they increase the effective interest rate and restrict potential borrowing. Small-scale enterprises, especially when engaged in wood forest production, may need financing for larger investments that have prolonged amortization periods”. Due to the gestation period, there is normally a significant time lag between the initial expenditures and the time when investment creates a positive cash flow and the enterprise can repay the loan.

4.3.2 Prerequisites for accessing MFI credits--Collateral Securities

The question was posed to the respondents about the Prerequisites for accessing MFI credits--Collateral Securities. The finding showed that 62(51.7%0 of respondents said shop, 46(38.3%0 of respondents said car and 12(10%) of respondents said land, as shown in table below

Table 4.6. Prerequisites for accessing MFI credits--Collateral Securities

	Response	Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Land	12	10.0	10.0	10.0
	Shop	62	51.7	51.7	61.7
	Car	46	38.3	38.3	100.0
	Total	120	100.0	100.0	

Source: Field Data (2014)

The finding from the table above showed that most of MFI requested collateral as a security for loan application as 51.7% of respondents said, it was observed that, security is required for certain kinds of credits. Some MFIs do not require any form of security at all but rather grant credit based on the savings capacity of the client. In situations where collaterals are needed, it was found that, the MFIs requested any of the following collaterals; Land, Car, Shops as a reference point for guarantee

Diagne and Zeller (2001) argue that insufficient access to credit by the poor just below or just above the poverty line may have negative consequences for SMEs and overall welfare. Access to credit further increases SME's risk-bearing abilities; improve risk-copying strategies and enables consumption smoothing overtime. With these arguments, microfinance is assumed to improve the welfare of the poor.

It is argued that MFIs that are financially sustainable with high outreach have a greater livelihood and also have a positive impact on SME development because they guarantee sustainable access to credit by the poor (Rhyme and Otero, 1992).

Buckley (1997) argue that, the indicators of success of microcredit programs namely high repayment rate, outreach and financial sustainability does not take into consideration what impact it has on micro enterprise operations and only focusing on “microfinance evangelism”. Carrying out research in three countries; Kenya, Malawi and Ghana,

Wenner D (1995) argued that “Micro-credit is most often extended without traditional collateral”. If physical collateral were a requirement for borrowing, most MFI clientele would be unable to participate due to their extreme poverty level. Because borrowers do not have physical capital, MFIs focus on using social collateral, via group lending. Group lending encompasses a variety of methodologies, but all are based on the principal of joint liability. In essence, the group takes over the underwriting, monitoring, and enforcement of loan contracts from the lending institution

4.3.3 The extent money is considered as important factors from the growth of the firm

The question was asked to the respondents about the extent money is considered as important factors from the growth of the firm. The finding showed that 80(66.7%) of respondents said money is very important factors for the growth of the firm, 34(28.3%) of respondents said fairly important, 5(4.2%) of respondents said slightly important and 1(0.8%) of respondents said not important

Table 4.7: The extent money is considered as important factors from the growth of the firm

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Not Important	1	0.8	0.8	0.8
	Slightly Important	5	4.2	4.2	5.0
	Fairly Important	34	28.3	28.3	33.3
	Very Important	80	66.7	66.7	100.0
	Total	120	100.0	100.0	

Source: Field Data (2014)

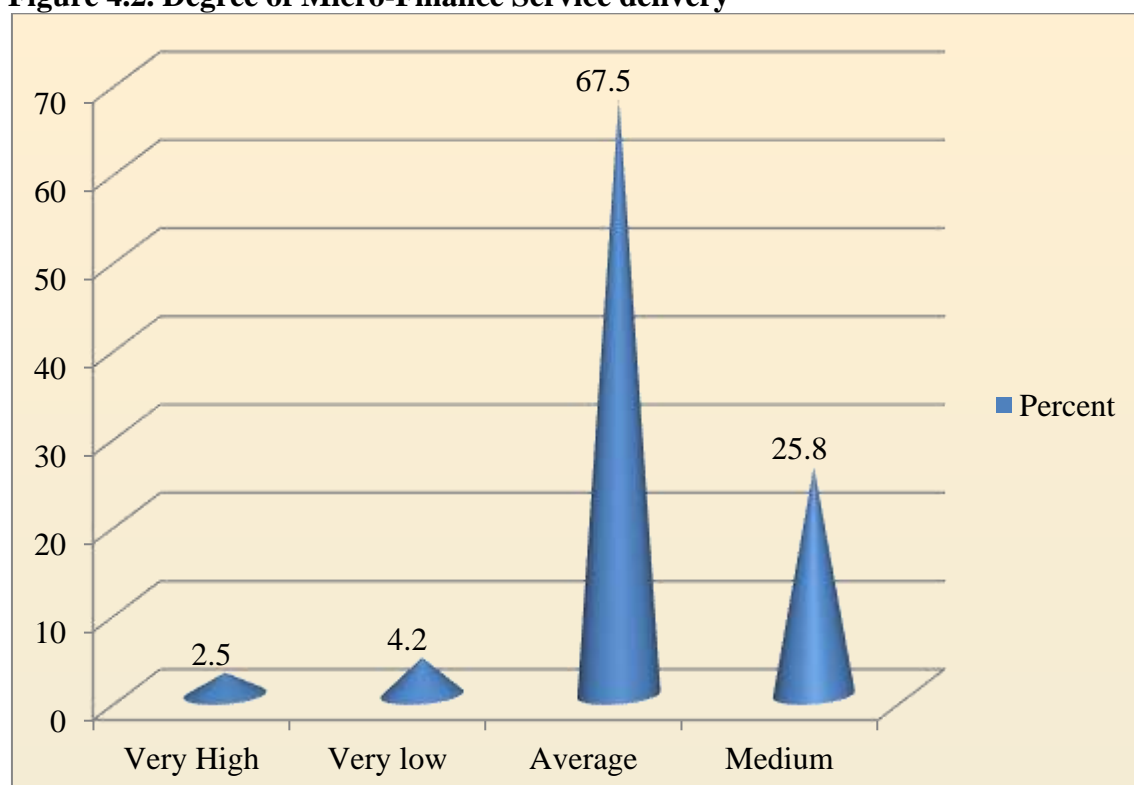
The finding from table 8 above implied that the money is very important factors for the growth of the firm as 66.7% of respondents said. It is true that money is the main factor for development and growth of the SMEs in general but also conducive environment, networking, trustworthy, individual and stakeholders attitude bring development.

In Tanzania the banking and financial institution act 1991, marked the beginning of the on going financial reforms, the law among other things permitted entry of private banks and provided the supervision and regulation framework for the financial sector. (Llwiza and Nwako, 2002). A large body suggest that financial development contributes significantly to growth of the economy, (word development report, 20002). Through its strong effort on overall economic growth, financial development is centrally to the poverty reduction, research done by world also shows that financial development directly benefits the poorer segment of the society and it is associated with improvement in income distribution. (World development report, 2002).

4.3.4 Degree of Micro-Finance Service delivery to the SMEs

The question was asked to the respondents about the degree of Micro-Finance Service delivery to the SMEs. The finding showed that 81(67.5%0 of respondents said average, 31(25.8%) of respondents said medium, 5(4.2%) of respondents said very low and the last group of respondents said very high.

Figure 4.2. Degree of Micro-Finance Service delivery



Source: Field Data (2014)

The finding from the table above indicated that most of the respondents 67.5% indicated that the degree of microfinance service delivery is average, followed by only 2.5% of respondents indicated that degree of micro-finance service delivery is very high. On average the micro-finance service delivery was credited basing on reasons that there was multiple branches opened across the areas, increased advertisements, some SMEs appreciated that the low interest rates charged by MFIS especially to money lending compared to other related banks. However, low service delivery was based on numerous reasons included. As discussed here under

4.3.4.1 Lack of information access about the services,

Access to finance refers to the possibility that individuals or enterprises can access financial services, including credit, deposit, payment, insurance, and other risk management services. Those who involuntarily have no or only limited access to financial services are referred to as the unbanked or underbanked, respectively.

4.3.4.2 The lack of financial access

The lack of financial access limits the range of services and credits for household and enterprises. Poor individuals and small enterprises need to rely on their personal wealth or internal resources to invest in their education and businesses, which limits their full potential and leading to the cycle of persistent inequality and diminished growth.

4.3.4.3 The strict terms and conditions associated with services among others.

Microfinance institutions typically provide short-term loans for small amounts of capital, while small-scale enterprises often need longer-term and larger loans. There is often a lack of cooperation between banks and forest sector

4.4 Impact of MFI loans on livelihood of Medium & Small Entrepreneurs

The second objective from this study aimed at finding the Impact of MFI loans on livelihood of Medium & Small Entrepreneurs. The objective was accompanied by the following questions

4.4.1 The extent the loans obtained from the MFI have contributed to the growth of the business

The question was posed to the respondents about the extent the loans obtained from the MFI have contributed to the growth of the business. The finding showed that 60(50%) of respondents said the loans obtained from the MFI have highly contributed to the growth of the business, 35(29.2%) of respondents said small contribution, 23(19.2%) of respondents said very small contribution and 2(1.7%) of respondents said no contribution.

Table 4.8: The extent the loans obtained from the MFI have contributed to the growth of the business

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	No Contribution	2	1.7	1.7	1.7
	Very small contribution	23	19.2	19.2	20.8
	Small contribution	35	29.2	29.2	50.0
	High Contribution	60	50.0	50.0	100.0
	Total	120	100.0	100.0	

Source: Field Data (2014)

The finding from table above indicated that loans from MFI have highly contribution to the growth of the business as 50% of respondents indicated. The interview conducted by the researcher showed that interviewed some of the business from the respondents had now turned into medium enterprises because of the extended support of these micro-finance institutions and among the appreciated services was the MFIs at a fair interest rates but they were dissatisfied with the terms and condition always attached to these services. In addition, some SMEs presented various reasons in explain why services were contributing to the growth of enterprise for example, one comment from one respondent argued: *“I opened up a savings account which helps me to save my money, increase my working capital, I have tried to expand my business of hardware because of good services from MFIs”*. 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 labor amongst poor people (Mosley (1999)).

4.4.2 The extent the loans obtained from the MFI have contributed to the increase level of income

The question was posed to the respondents if loans obtained from the MFI have contributed to the increase level of income. The findings showed that 47(39.2%) of respondents agreed that loans obtained from the MFI have contributed to the increase level of income followed by 34(28.3%) of respondents who said small contribution and very small contribution and only 5(4.2%) of respondents said no contribution

Table 4.9: The extent the loans obtained from the MFI have contributed to the increase level of income

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	No Contribution	5	4.2	4.2	4.2
	Very small contribution	34	28.3	28.3	32.5
	Small contribution	34	28.3	28.3	60.8
	High Contribution	47	39.2	39.2	100.0
	Total	120	100.0	100.0	

Source: Field Data (2014)

The finding from the table above showed that loan obtained from the MFI have contribution to the increase of income as 39.2% of respondents said followed by 28.3% indicated. This implied that Microfinance enables the poor and excluded section of people in the society who do not have an access to formal banking to build assets, diversity livelihood options and increase income, and reduce their vulnerability to economic stress.

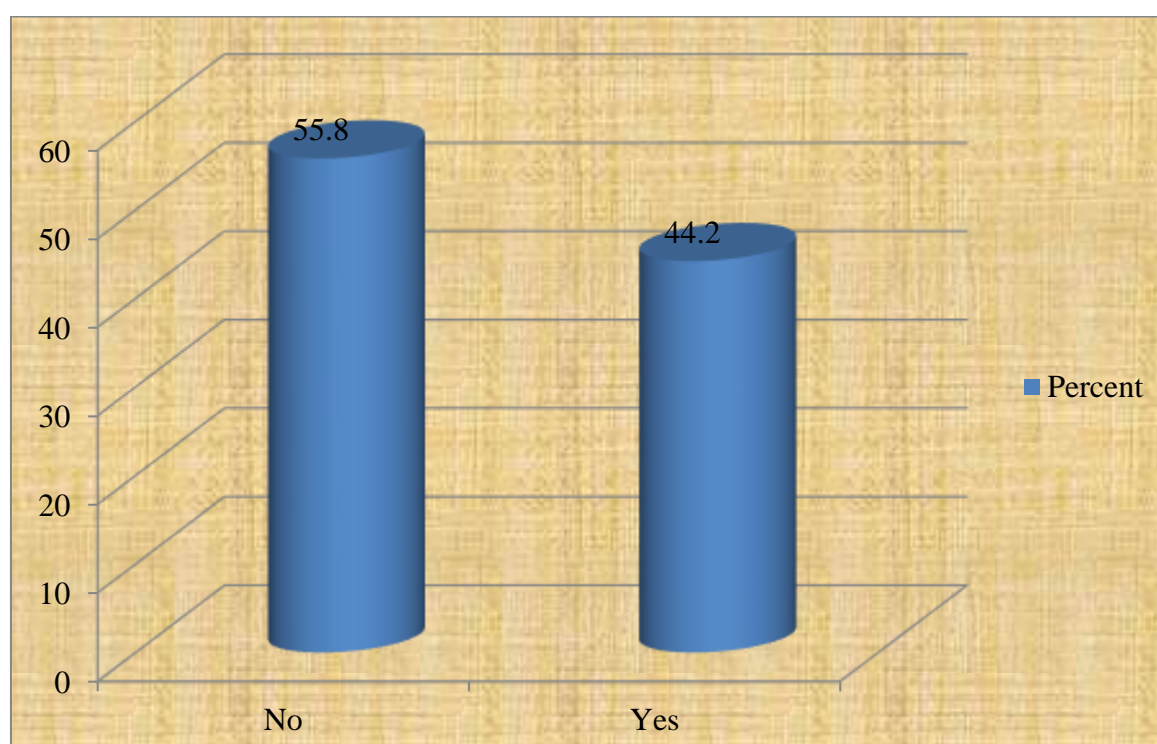
In the past, it has been experienced that the provision for financial products and services to poor people by MFIs can be practicable and sustainable as MFIs can cover their full costs through adequate interest spreads and by operating efficiently and effectively. Microfinance is not a magic solution that will propel all of its clients out of poverty. But various impact studies have demonstrated that microfinance is really benefiting the poor households (Littlefield and Rosenberg, 2004).

In relation to which extent the loans obtained from the MFI have contributed to the increase level of income. Microfinance can aid in the improvement or establishment of family enterprise, potentially making the difference between alleviating poverty and economically secure life. (Zeller and Sharma, 1998),

4.4.3 The need to acquire loan for the purpose apart from business

The respondents were asked if they acquire loan for the purpose apart from business. The finding showed that there some respondents who acquire loan apart from business as 67(55.8%) of respondents said and 53(44.2%) of respondents said yes.

Figure 4.3: The need to acquire loan for the purpose apart from business



Source: Field Data (2014)

The finding from table above indicated that there some people who apply loan for the purpose apart from business as 44.2% of respondents said although majority 55.8 said no. This implied that on the issue of how credits are utilized for business purposes, respondents gave some indication of situations not relating to business for which credits acquired are applied. payment of school fees , Medical bills, to purchase a vehicle for transportation for business purposes alike, for house building project, solve unexpected family issues, payment of rent, Data relating to the usage of the loans also indicates to some extent, the non-usage of the credit acquired for the intended purposes, which amounts to misapplication of funds. Amazingly, majority of the respondents concede that the loans they acquire lead to increase in their capital base for business operation. This shows that, the operations of the MFIs lead to improvement in the daily activities of the beneficiaries. However, the non-usage of credit for the intended purpose for which it was acquired, amounts to credit misappropriation. This is one of the major setbacks in the growth of SMEs as admitted by SME operators.

4.5 The costs that medium and small enterprises incur when accessing the microfinance services.

The third objective from this study aimed at finding the how the costs that medium and small enterprises incur when accessing the microfinance services. The following question was asked in relation to the objective.

4.5.1 Challenges facing the SMEs in Tanzania

The question was asked to all respondents about the challenges facing the SMEs in Tanzania, the findings showed that 89(74.2%) of respondents said one of the challenges facing SMEs in Tanzania is limited of capital followed by poor market as 78(65%) of respondents indicated, 56(46.7%) of respondents said infrastructure, 52(43.3%) of respondents said poor technology, 51(42.5%) of respondents said innovation and 10(8.3%) of respondents said Tanzania financial policy to enable Tanzania benefit from local and foreign capital market

Table 4.10: Challenges facing the SMEs in Tanzania

No	Variable	Frequency	Percentage	Total
1	Innovation	51	42.5	120
2	Technology	52	43.3	120
3	Infrastructure	56	46.7	120
4	Tanzania financial policy	10	8.3	120
5	Poor Market strategies	78	65.0	120
6	Limited Capital	89	74.2	120

Source: Field Data (2014)

4.5.1.1 Innovation

Innovation was a big challenge that Tanzanian SMEs faced. Most of Tanzanians are introvert that they took long time to make decision on different issues. They failed to create some strategies that could help them to develop their business and to survive in the market. One driver for innovation programs in corporations was to achieve growth objectives. Tanzanian SMEs could not grow through cost reduction and reengineering alone, Innovation was the key element in providing aggressive top-line growth, and for increasing bottom-line results

4.5.1.2 Technology

Technology significantly affects human as well as other animal species' ability to control and adapt to their natural environments. Now days different business are conducted electronically. Failure to change with change in technology would be a problem Tanzanian SMEs to be developed and to survive. Technology had seen to be a challenge to these Tanzanian SMEs because they had little ability to change when technology change.

4.5.1.3 Tanzania financial policy

Tanzania financial policy was not much a challenge to these Tanzanian SMEs since it enabled Tanzanian to benefit from local and foreign capital market and other financial cooperation's like allows people to form their savings and credit cooperation society (saccos), and other micro financial institutions to individuals levels, the challenge is

enough awareness to some of SMEs on the opportunity that offered by policy on how they can benefit and protected on their day to day activities so as they can be motivated and flourish to prosper to their business.

4.5.1.4 Poor Market strategies

Poor Market strategies were a challenge for these small businesses from Tanzania. Marketing strategies serve as the fundamental underpinning of marketing plans designed to fill market needs and reach marketing objectives. Plans and objectives are generally tested for measurable results. Commonly, strong marketing strategies are developed as multi-year plans, with a tactical plan detailing specific actions to be accomplished in the current year. SMEs failed to understand the internal and external environments which were the most issues involved in marketing strategy. Internal environmental factors include the marketing mix, plus performance analysis and strategic constraints. External environmental factors include customer analysis, competitor analysis, target market analysis etc

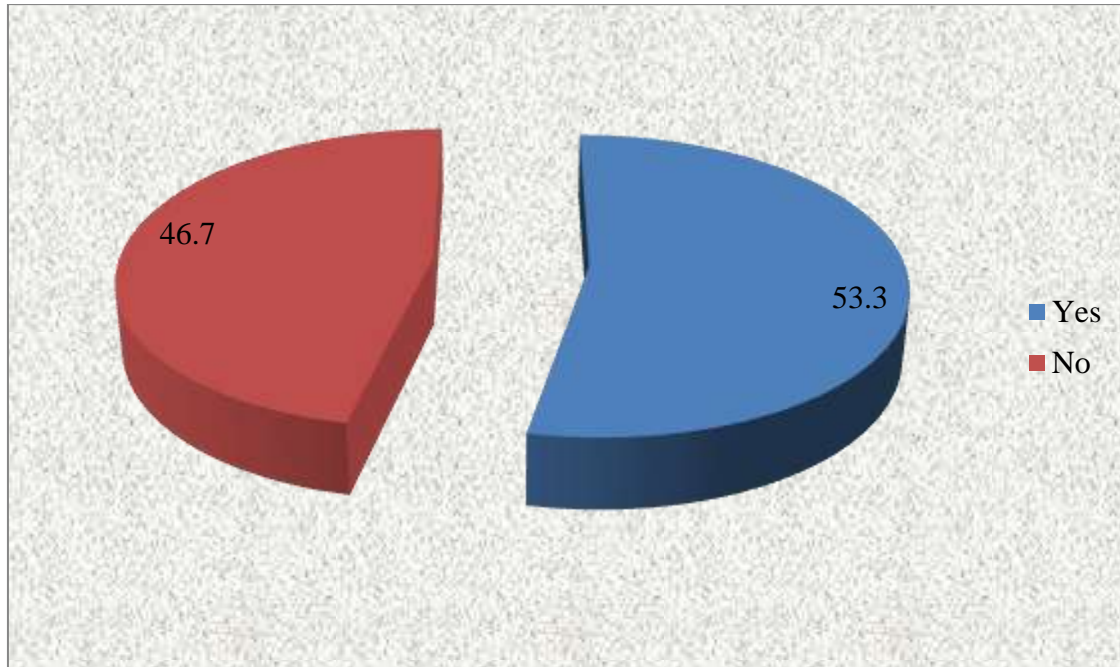
4.5.1.5 Limited Capital

The finding from table above showed that 74.2% of respondents said that the most challenge facing SMEs in Tanzania is limited capital, Limited Capital was mentioned by potential and existing SME operators as the most serious barrier to business start-up or growth. Lack of funds to start or run a business was sometimes a symptom of limited capacity to articulate and present ideas to appropriate financiers, failure to attract enough customers and poor management of finances. Most of these SMEs had little access to finance, so it was great problem for them to raise a capital.

4.5.2 The requirement from the financial institution affordable for SMES to loan

The question was asked to all respondents about the requirement from the financial institution affordable for SMES to loan the finding showed that 64(53.3%) said the requirement from the financial institution are affordable for SMES to loan and the rest 56(46.7%) said no.

Figure 4.4: The requirement from the financial institution affordable for SMES to loan



Source: Field Data (2014)

This implies that, restrictions for getting loans from different financial institutions were not of high level. Interest rate was the most things that these SMEs considered first before getting any loan from these institutions. High interest rate was not favorable for these small businesses to get loans because would be required to return more interest to those institutions. Not only rate as a factor SMEs in Tanzania considered but also an asset as a security for securing loans was needed. The most requirements for borrower to get loan is to submit asset like car registration card, certificate of land ownership which is equivalent to or above loan applied.

4.5.3 Problem encountered in using EFC services

The question was posed to the respondents on the problem encountered in using EFC Services. The finding showed that 99(82.5%) of respondents said Lack of collateral security followed by high interest rate, 89(74.2%) of respondents said limited capital, followed by short payment period as 81(67.5%) of respondents indicated, 78(65%) of respondents said poor strategies and minority 33(27.5%) said inaccessibility of EFC services

Table 4.11: Problem encountered in using EFC Tanzania Service

No	Variable	Frequency	Percentage	Total
1	High interest rate	93	77.5	120
2	Short payment period	81	67.5	120
3	Lack of collateral security	99	82.5	120
4	in accessibility of EFC services	33	27.5	120
5	Poor Market strategies	78	65.0	120
6	Limited Capital	89	74.2	120

Source: Field Data (2014)

The findings from table above indicated that lack of collateral security 82.5%% followed by high interest rate 77.5% were among the problem encountered in EFC Service. This implied that Accessing loan is the major constraint to SMEs ability to earn income since most traditional financial systems require physical collateral worth more than the amount of loan requested.

Most of SMEs find it difficult to generate significant income from such loan because interest rates are high. In addition, due to high rate of illiteracy,

Physical collateral is requirement for borrowing, most SMEs are unable to participate due to their extreme poverty level. Because borrowers do not have physical capital, MFIs focus on using social collateral, via group lending. Group lending encompasses a variety of methodologies, but all are based on the principal of joint liability. In essence, the group takes over the underwriting, monitoring, and enforcement of loan contracts from the lending institution

The interest rates may be too high or other lending terms might not be appropriate for certain firms. Most of SMEs do not afford most of interest loan used by microfinance. Poor Market strategies are also challenge for these small businesses for loan application Marketing strategies serve as the fundamental underpinning of marketing plans designed to fill

market needs and reach marketing objectives. Plans and objectives are generally tested for measurable results. Commonly, strong marketing strategies are developed as multi-year plans, with a tactical plan detailing specific actions to be accomplished in the current year. SMEs failed to understand the internal and external environments which were the most issues involved in marketing strategy. Internal environmental factors include the marketing mix, plus performance analysis and strategic constraints. External environmental factors include customer analysis, competitor analysis, target market analysis etc

4.6 Chapter Conclusion

This chapter presents data presentation, analysis and discussion of the finding. It has been noted that microfinance institutions play its role in growth of medium and small scale entrepreneurship in Tanzania is no longer a theory but tangible. It is true that most of the SMEs in Tanzania now get business capital for their business loans from MFI which enable the poor and excluded section of people in the society who do not have an access to formal banking to access the loans. Limited Capital, Poor Market strategies Innovation was a big challenge that Tanzanian SMEs faced.

CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Introduction

The purpose of this chapter is to cover summary of the study, conclusions and recommendations of the study in terms of the data which have been collected and analyzed with the regard of questionnaires and interview distributed to the respondents.

5.2 Summary of Findings

The study aimed at assesses the contribution of MFI services on the growth of MSEs in Tanzania. In this study the researcher adopted the following specific objectives; To identify the benefits of MFI on medium and small scale enterprises growth, to assess the impact of MFI loans on livelihood of Medium & Small Entrepreneurs, to assess the costs that medium and small enterprises incur when accessing the microfinance services. Also it helps other scholars who want to conduct research to the extent Microfinance has been contributing to growth of SMEs in Tanzania, to fill any gap which was left over.

The researcher reviews various sources of information written and presented by different scholars about microfinance and women empowerment in different regions. Review of related literature such as in text books, journals, and internet sources have been done. All these sources provided necessary background to the study, after that researcher was provided the research gap.

The Research methodology concerned about data collection where the researcher was applying systematic approaches in data collection so that to come up with the specific findings. The research used both qualitative and quantitative. Qualitative techniques were used because there was a need to explain the responses from the correspondents and analyze them. This chapter also focuses on research design where descriptive analysis used, The study included 53 respondents whereas, sampling techniques and methods of data collection (primary data and secondary data) tables were drawn by using special

program known as SPSS. The researcher presented analyses and discussed the findings of the study. This chapter segmented into three objectives based to the study.

The source of business capital and adequacy of capital for business. 82(68.3%) of respondents said they get capital from banks and MFI, Prerequisites for accessing MFI credits--Collateral Securities. 62(51.7%) of respondents said shop, 46(38.3%) of respondents said car and 12(10%) of respondents said land, The extent money is considered as important factors from the growth of the firm. 80(66.7%) of respondents said money is very important factors for the growth of the firm. The degree of Micro-Finance Service delivery to the SMEs. 81(67.5%) of respondents said average.

The extent the loans obtained from the MFI have contributed to the growth of the business 60(50%) of respondents said the loans obtained from the MFI have highly contributed to the growth of the business, it was only 35(29.2%) of respondents said small contribution, loans obtained from the MFI have contributed to the increase level of income as 47(39.2%) of respondents agreed that loans obtained from the MFI have contributed to the increase level of income but 67(55.8%) mentioned that there some SMEs which acquire loans for the purpose apart from business.

The challenges facing the SMEs in Tanzania, 89(74.2%) of respondents said one of the challenges facing SMEs in Tanzania is limited of capital followed by poor market as 78(65%) of respondents indicated, 56(46.7%) of respondents said infrastructure also the requirement from the financial institution affordable for SMES to loan. The problem encountered in using EFC Services, 99(82.5%) of respondents said Lack of collateral security followed by high interest rate, 89(74.2%) of respondents said limited capital, followed by short payment period as 81(67.5%) of respondents indicated, 78(65%) of respondents said poor strategies and minority 33(27.5%) said inaccessibility of EFC services

5.3 Conclusions

The concept of impact made by the microfinance institutions on growth of medium and small scale entrepreneurship in Tanzania is no longer a theory but tangible things which many people experience now and survives on it on one or other way. It is a matter of facts that many people had benefited from these microfinance to develop their carrier, got job opportunity, got loans and starts or improve their businesses for the better.

It is true that most of the SMEs in Tanzania now get business capital for their business loans from banks and MFI it was observed that, security is required for certain kinds of credits. In situations where collaterals are needed, money is very important factors for the growth, development and growth of the SMEs in general. The micro-finance service delivery was credited basing on reasons that there was multiple branches opened across the areas, increased advertisements, some SMEs appreciated that the low interest rates charged by MFIS especially to money lending compared to other related banks.

Microfinance enables the poor and excluded section of people in the society who do not have an access to formal banking to build assets, diversity livelihood options and increase income, and reduce their vulnerability to economic stress. The provision for financial products and services to poor people by MFIs can be practicable and sustainable as MFIs can cover their full costs through adequate interest spreads and by operating efficiently and effectively. There is indication of situations not relating to business for which credits acquired are applied. payment of school fees, Medical bills, to purchase a vehicle for transportation for business purposes alike, for house building project, solve unexpected family issues, payment of rent there some challenges facing SMEs in acquired loans from MFI like limited capital, Limited Capital, Poor Market strategies Innovation was a big challenge that Tanzanian SMEs faced. Most of Tanzanians are introvert that they took long time to make decision on different issues and poor Technology, collateral worth more than the amount of loan requested. There is difficult to generate significant income from such loan because interest rates are high. If all these can get proper answer SMEs with have conducive environment to flourish and prosper in Tanzania and many people they can access loans for other family matter for improve their life and Tanzania will be a good place for people to live.

5.4 Recommendations

From the finding it is recommended that, in view of the findings made and conclusions drawn from the study the following recommendations are provided to help enhance an accelerated and sustained growth in the SME sector and also provide recommendations to help in the improvement of the services of MFIs.

The MFIs may be quick to measure their success rate by considering factors like high repayment, outreach and financial sustainability, but these may not be success if their activities do not reflect in the growth of SMEs. The growth of SMEs does not only rely on access to credits but also the creation of favorable and formidable business environment.

The MFIs have a great responsibility of ensuring the proper use of credit which is an important facility in business acceleration. To achieve this, credits should client-oriented and not product- oriented. Proper and extensive monitoring activities should be provided for clients who are granted loans.

In order to reduce the rate of default, MFIs can research into very profitable business lines and offer credit to clients who have the capacity to exploit such business lines.

Finally, the researcher recommends that business and financial training should be provided by MFIs on a regular basis and most cases should be tailored toward the training needs of the clients.

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APPENDICES

Appendix 1: Questionnaires to MFI employees Respondents.

These Questionnaires are on the assessment on impact of microfinance institution on growth of medium and small scale entrepreneur in Tanzania. The major targeted respondents are microfinance practitioners and actors as well as beneficiaries.

Please fill free to express your opinion on the questionnaires and let you assured of confidentiality and be informed that, will be used to the intended purpose only.

A: Background Information

A. DEMOGRAPHIC

1. Gender

- i - Male ()
- ii - Female ()

2. What is your Educational level?

- i. Diploma ()
- ii. Advanced Diploma ()
- iii. Degree ()
- iv. Postgraduate Degree/Diploma ()
- v. PhD ()
- vi. Other (please specify) ()

3. Age of Respondents

- i. 18-30 ()
- ii. 31-40 ()
- iii. 41-50 ()
- iv. Above 50 yrs ()

4. Working experience

- i. 1-5 yrs ()
- ii. 6-10 yrs ()
- iii. 1-15 yrs ()
- iv. Above 15 yrs ()

Part B: Respondents to MFIS managers.

5. To what extent do you consider money as one of the important factors for growth of your firm in terms of the number of employees?

- i. Not important ()
- ii. Slightly important ()
- iii. Fairly important ()
- iv. Very important ()

6. To what extent do the loans obtained from the MFI have contributed to the following?

	No contribution	Very small contribution	Small contribution	High contribution
Growth of your business				
Increase in the level of income				
Improved family living standard				

7. What is the amount of loan SMEs enjoying with MFI? Tsh.....

- a) 10,000-100,000 ()
- b) 100,000-500,000 ()
- c) 500,000-1,000,000 ()
- d) 1000,000-5,000,000 ()
- e) 5,000,000-50,000,000 ()
- f) Above 50,000,000 ()

8. Types of Business

Registered company () Partnership ()

Registered company () Joint Venture ()

9. Amount of loan.....

10. Loan repayment per week: Tshs.....

11. Name of the MFI

12. Are SMEs satisfied are you with MFIs services?

I. Highly satisfied ()

II. Neither satisfied nor dissatisfied ()

III. Dissatisfied ()

IV. Highly dissatisfied. ()

Appendix 2: Questionnaires to MFI customers (SMEs) Respondents.

These Questionnaires are on the assessment on impact of microfinance institution on growth of medium and small scale entrepreneur in Tanzania. The major targeted respondents are microfinance practitioners and actors as well as beneficiaries.

Please fill free to express your opinion on the questionnaires and let you assured of confidentiality and be informed that, will be used to the intended purpose only.

A: Background Information

A. DEMOGRAPHIC

1. Gender

- i - Male ()
- ii - Female ()

2. What is your Educational level?

- a) Diploma ()
- b) Advanced Diploma ()
- c) Degree ()
- d) Postgraduate Degree/Diploma ()
- e) PhD ()
- f) Other (please specify) ()

3. Age of Respondents

- a) 18-30 ()
- b) 31-40 ()
- c) 41-50 ()
- d) Above 50 yrs ()

4. Working experience

- a) 1-5 yrs ()

- b) 6-10 yrs ()
- c) 1-15 yrs ()
- d) Above 15 yrs ()

13. What are the main problems that hinder expansion of your business

	Highly hinders	Slightly hinders	Fairly hinders	Does hinders
High taxes				
Lack for business premises				
High rent for business premises				
Lack of enough demand				
Lack of Education on how to run the business				

5. What is the number of employees are in your business

- a. 1-5
- b. 6-10
- c. Above 15

6. What other money generating activities are you involved in?

.....

7. What was the main source of your start op capital? In Tshs.

.....

8. For how long (in years) have you been a member of the MFI?

- a) <1yr ()
- b) 1-3 ()
- c) 4-6 ()
- d) >7 ()

9. What was your source of information about MFI?

- a) People ()
- b) Newspapers ()
- c) Television ()
- d) Radio ()
- e) Others ()

10. What was your source of credit prior to joining the MFI?

- a) Private money lenders ()
- b) Relatives/friends ()
- c) Equib/iddir ()
- d) No means ()

11. Why do you like the loan provision by the MFI?

- a) Low interest rate than other informal sources of credit ()
- b) Steady source of working capital ()
- c) Group solidarity and/or group dynamics ()
- d) Easier guarantees than other loan alternatives ()

12. What are the limitations of the MFI?

- a) High interest rate ()
- b) Too small loan size ()
- c) Repayment policy ()
- d) Problematic groups dynamic ()
- e) Do not know
- f) High interest rate, small loan size, repayment policy ()

13. For how long have you been in the business?

- 1-5 ()
- 6-10 ()
- 10-15 above 15 yrs ()

14. Is there any significant improvement?

a. Yes ()

b. No ()

If No, why.....

15. What motivate you to borrow?

.....

16. Do you have any knowledge or awareness of microfinance?

a. Yes ()

b. No ()

From where

17. Do you have any strategy/motives for growth?

a. Yes ()

b. No ()

What strategies.....

18. Do you have any other sources of income?

a. Yes ()

b. No ()

If no why?

.....

.....

19. What is the best sources of credit from your experience and why?

.....

.....

20. What challenges your business face?

.....
.....

21. Do they limit you to borrow?

.....

Appendix ii Interview guide

1. To what extent do you consider money as one of the important factors for growth of your firm in terms of the number of employees
2. What are the main problems that hinder expansion of your customers business
3. What is the amount of loan your customers enjoying with MFI?
4. What other money generating activities are you involved in
5. What was the main source of your start up capital
6. How satisfied are you with MFIs services
7. What is the best sources of credit from your experience and why
8. What challenges your business face