MZUMBE UNIVERSITY

SCHOOL OF BUSINESS

THESIS ON

THE CONTRIBUTION OF MICROFINANCE INSTITUTIONS IN DEVELOPMENT OF SMALL ENTERPRISES

THE CASE OF ILALA MUNICIPALITY

By

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A thesis / Dissertation Submitted in Partial/ Fulfillment of the Requirements for the Degree of Masters of Business Administration (Corporate Management)) of Mzumbe University

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CERTIFICATION

We, the undersigned, certify that we have read and hereby recommend for acceptance by Mzumbe University, a Dissertation/Thesis entitled: The Contribution of Microfinance Institutions in Development of Small Enterprises: The case of Ilala Municipality, in partial/fulfillment of the requirements for award of Masters degree of Business Administration in Corporate Management of Mzumbe University.

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I **Jenipher Ng'ana,** declare that, this thesis/dissertation is my own original work; it has neither been submitted nor presented for any academic or professional award in any other institution.

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DEDICATION

To my Lord and Savior Jesus Christ who strengthens me. To my lovely husband Tumain Dobeli, you stood up your ground to rescue my life. Out of all the language I have learned so far, never have I found a word good enough to thank you. Thank you my husband and may our heavenly God bless you. This success is equally yours.

ABSTRACT

The study intended to assess the contribution of Microfinance institutions in development of small enterprises in Tanzania, in the context of limited financial services in both rural and urban areas in the greater part of Tanzania, the study attempt to assess the role of Microfinance institutions (MFI) in facilitating micro enterprise development at Ilala Municipality in Dar es salaam region in order to increase prospects for economic and social development.

The general objective was to explore the contribution of Microfinance institutions to development of small enterprises at Ilala in Dar es Salaam. The study was carried out in Dar es Salaam region as it was easier to obtain information from three different Microfinance institutions and some government Officers. Case study research design was adopted. Interview, questionnaires and observation data collection methods were used to collect data. A total number of sixty (60) respondents were given the questionnaires and interviewed.

The findings revealed that microfinance institutions are the options and self-confidence of small businesses by contributing to their expansion and diversification of their businesses. They also help small businesses to decrease risks, increase profit, store their excess liquidity, obtain returns on their savings, and to conduct their businesses with dignity. The standard of living also improves in terms of education, housing, and health. In addition, the economic activities often create jobs for others; among those who gain employment in this way are some of the extreme poor people. They impact by mobilizing savings for investment, facilitate and encourage inflows of foreign capital and optimize the allocation of capital between competing uses. Generally, there is a need to create favorable environment for attracting more establishments of Micro Finance Institutions for sustainable economic development in the poor communities.

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ABBREVIATIONS

BFIA	-	Banking and Financial Institutions Act
BEST	-	Business Environment Strengthening for Tanzania
CBO	-	Community Bank Organizations
CBs	-	Community Banks
CRDB	-	Cooperative Rural Development Bank
CRMP	-	Cooperative Reform and Modernization Programme
DCDO	-	District Cooperative Development Officer
FAIDA	-	Finance and Advances in Development Association
FINCA	-	Foundation for International Community Assistance
GDP	-	Gross Domestic Product
IFAD	-	International Fund for Agricultural Development
K-REP	-	Kenya Rural Enterprise Project
MDG	-	Millennium Development Goal
MFI'S	-	Microfinance Institutions.
MKUKUTA	-	Mkakati wa Kukuza Uchumi na Kupunguza Umaskini
NBS	-	National Bureau of Statistics
NEEC	-	National Economic Empowerment Council
NEEP	-	National Economic Empowerment Programme
NGO's	-	Non Governmental Organizations
NMB	-	National Microfinance Bank
OSS	-	Operational Self Sufficiency
PHD	-	Poverty and Human Development
PPF	-	Parastal Pension Fund
PRIDE	-	Promotion of Rural Initiative and Development Enterprises
PRSP	-	Poverty Reduction Strategy Programme
ROSCA	-	Rolling Savings and Credit Associations
SACCAs	-	Savings and Credit Cooperative Associations
SACCOS	-	Savings and Credit Cooperative Societies.

SCCULT	-	Savings and Credit Cooperatives Union League of Tanzania
SIDO	-	Small Industries Development Organization
SMEs	-	Small and Medium Enterprises
SOE s	-	State Owned Enterprises
TRDB	-	Tanzania Rural Development Bank
URT	-	United Republic of Tanzania
VICOBA	-	Village Community Bank
WCDO	-	Ward Economic Development Officer
WEO	-	Ward Economic Officer
WEDA	-	Women Empowerment and Development Agency

CHAPTER ONE
INTRODUCTION

1.0 Background information

Microfinance institutions were introduced in developing countries for lending small amounts of money to small entrepreneurs who had no credentials and collateral demanded by commercial banks. Today Microfinance Institutions (MFIs) act as providers of financial services to economically active individuals. The financial services involve savings and credits.

Apart from financial services, some MFIs provide social services such as group formation and training on investment skills and group management. MFIs seem to be supportive and friendly to poor communities that are otherwise not having an opportunity to access loans from commercial banks.

Historically, it was by 1990s that such business started to emerge in Tanzania either as Micro-Finance Institutions or as Financial NGOs. To mention just few, we have the following banks and financial institutions; National Microfinance Bank (NMB), Akiba Commercial Bank, CRDB Bank, Mufindi Community Bank, Mwanga Community Bank, Dar es salaam Community Bank, Tanzania Postal Bank (TPB), Mbinga Community Bank which deal with Micro-finance activities. We also have financial NGOs like Promotion of Rural Initiatives and Development of Enterprises (PRIDE- Tanzania), Women Empowerment & Development Agency Ltd (WEDAC LTD), Foundation for International Community Assistance (FINCA), Youth Self-employment Programmed (YOSEFO), Mennonite Economic Department Association (MEDA/ Haiti) among others providing micro-financial services to economically active poor people.

Apart from the above instructions, the government, in the process of reducing poverty has established some programs, which deal with micro-finance services as TASAF and SELF.

Generally, the economic growth of most developing countries depends heavily on private sector in which, micro, small and medium enterprises are major players. It is estimated that about a third of GDP IN Tanzania originated from SME's (Wangwe, 1999).

Small enterprises play significant economic, social roles in employment creation, resource utilization, and income generation, contribute to exports and make the economy more dynamic. Government in most countries, whether they are highly industrialized, developing or among the least developed, have expressed increased enthusiasm for microenterprises because of their contribution to the people's well being and satisfying their needs.

Most policy makers, planners and academic in developing countries, have now acknowledged the fact that the future of their countries' competitiveness and economic growth heavily depend on the private sector, in which the SME's play a major role (Rutashobya, 1997).

1.1 The History of Banks and Financial Institutions in Tanzania

1.1.1 An Overview to the Financial Sector Reform

Tanzania embarked on the financial sector reform with the enactment of the Banking and Financial Institutions Act (BFIA) in 1991, which marked an important milestone towards improving the soundness of the financial sector in Tanzania. The BFIA was aimed at enhancing efficient mobilization and use of financial resources in order to improve economic development in the country. The BFIA allowed not only the establishment of both local and foreign private banks and financial institutions in the country, but also restructuring and recapitalization of the publicly owned bank (CRDB, NBC and THB) as a result, CRDB was fully restructured and privatized in 1996. THB closed in 1995 following huge losses, while NBC split into two banks in 1997, which were finally recapitalized to improve their efficiency. Recapitalization of NBC and NMB also took place in 1997. The BFIA also gave the Bank of Tanzania (BOT) the powers to regulate and supervise the banking sector.

Prior to the financial sector reforms in 1991, interest rates were not liberalized. BOT set minimum and maximum interest rates for saving and lending. As a step towards liberalization of interest rates the BOT removed the maximum lending rates imposed on commercial banks in 1992, and in 1993 BOT introduced Treasury bill auctions as a reference point for the determination of market rate. On the following year BOT removed the remaining restriction on minimum deposit rate. All these measures were intended at improving efficiency on financial resource mobilization hence accelerate the country's economic development via investment growth.

The liberalization of the financial sector and the establishment of the open market operations in foreign exchange and government paper (Treasury bills) have extended the scope for the implementation of active monetary policy. The BOT completely liberalized interest rates with effect from 1993 with launching of regular Treasury Bills auctions in August 1993; it has been possible for BOT to peg its discount rate to bond yields, so the general rates are restructured.

Pursuant to the BFI Act, 1991, the entry of the new banks together with recapitalization and restructured publicly owned banks has fueled competition in financial services; the situation has compelled every financial institution to look for ways that would enable them to cope with competition. This in actual fact has resulted into some improvement of the quality and quantity of the financial services offered notably; credit excellence, global payments, mobility led self service and wealth management. In an effort to modernize their operations and build a stronger relationship with customers, most commercial banks have now and are continuing to install Automated Teller Machines (ATMs) outside their respective banking premises at convenient, customer friendly locations like in shopping malls, petrol stations, casinos, hotel and airports.

According to URT (2003)[1] shows that several public and private MFIs including some of banks have been reported to provide Micro Finance Services. Reports show that majority of these institutions offer credit to women and youth entrepreneurs (MEs) with establishments in urban areas while a few operating in rural areas. Some of key microfinance institutions (MFIs) which currently issue credits to MEs include, Promotion of Rural Initiatives and Development of Enterprises (PRIDE- Tanzania), Tanzania Finance and Advances in Development Association (FAIDA), USACA SACCOs LIMITED. Small Enterprises Development Agency (SEDA), Women Empowerment and Development Agency Ltd (WEDAC LTD), Foundation for International Assistance Community (FINCA), Mennonite Economic Development Association (MEDA). The microenterprises were acknowledged to have huge potential for employment and wealth creation in any economy. Yet in Tanzania the sector was stagnant and remained relatively small and micro in terms of its contribution to Gross Domestic Product or to add employment. Microenterprises activities play a great role in diversifying the Tanzania economy since they contribute to national income and emergence of cities and municipals. For example Ilala Municipal council.

1.2 Statement of the problem

The prevailing operation of the formal or conventional financial institutions in many low income countries such as Tanzania is inefficient in providing sustainable credit facilities to the poor. Access to the institutional credit which contributes to the increase in investment of small enterprises is very limited in Tanzania. Majority of the poor people do access financial services through informal channels, money lenders, friends, relatives, and traders (Amha, 2002).

Most microcredit services are limited. For example in Ilala municipality, Vendors (Street vendors, retail shops, e.t.c) are considered by formal and informal lending

[1]United Republic of Tanzania (2003), Small and Medium Enterprises Development Policy, Unpublished Report, Ministry of Industry and Trade, Dar-es-Salaam.

institutions as high risk borrowers. They therefore lack access to the financial market (Microfinance) which offers financial services to the most disadvantaged people. This was a constraint on MEs operation in Ilala Municipality and Tanzania as a whole. Therefore, targeting credit to the poor people was found to be one of the instruments for poverty reduction. In Tanzania context, microfinance institutions have been established and operating with the ultimate goal of poverty alleviation.

Based on above points, microfinance institutions are the economic solution to the small businesses and the poor but still no enough emphasis is given to realize their potential in influencing community development, Therefore the researcher found it was necessary to assess the contribution of Microfinance Institutions to the development of Small enterprises in Ilala Municipality.

1.3 Objectives of the study.

1.3.1 General objective

The general objective of the study was to;

Assess the contribution of Microfinance institutions in development of small enterprises in Ilala Municipality.

1.3.2 Specific objectives

The specific objectives of the study were;

(i) To find out challenges faced by Small Enterprises in Ilala Municipality.

(ii) To assess the loan process and conditions set by Microfinance Institutions for the Small Enterprises to access loan in Ilala Municipality.

(iii) To identify the impact of Microfinance services on Small Enterprises in Ilala Municipality.

1.4. The Research questions.

The study attempted to answer the following research questions;

(i) What are challenges faced by Small Enterprises in Ilala Municipality?

(ii) What are the processes and conditions set by Microfinance institutions for entrepreneurs to access loans?

(iii) What are the impacts of microfinance services on Small Enterprises in Ilala municipality?

1.5 Significance of the study

It is expected that the results of the study will provide further insight into the role of Microfinance in contributing to the development of small businesses. It is further hoped that it will bring up and solve issues facing Microfinance institutions in one hand and Microenterprises on the other hand so as to achieve the same goal. The study will also be expected to identify areas for improvement which will be useful to stakeholders. Finally, the study will assist the policy makers to improve microfinance institutions policy in order to best serve the small businesses, and highlight the possibilities of improving the savings and credits society's guidelines, rules, and regulations. The recommendations of the study will be beneficial to the community and policy makers.

1.6 Limitation of the Study

Limited time and funds have also posed a limitation to the researcher to exhaust all methods of collecting data to ensure that all required data were obtained to prepare the report. Budget limitations have enabled the study to take place and include only few small businesses in Dar es Salaam.

Confidentially of some of data limited the researcher to get enough data from respondents.

The researcher tried to reduce the number of visits and set appointments date to reduce transport costs and time could have been wasted. This was helpful but could not discard the problem completely. The researcher also tried her best to explain to the respondents the purpose of the study to ensure they were comfortable to release data/information required.

1.7 Scope and Delimitation of the Study

Concentration of the study in Dar es Salaam was done with the assumption that, Dares Salaam was the biggest commercial centre in the country and thus all types of small businesses can be found there. Therefore small businesses in Dar as Salaam, particularly in Ilala municipality were considered to be a good representative of studying the problems facing small businesses in Tanzania.

CHAPTER TWO
LITERATURE REVIEW

2.0 Introduction to literature review.

This chapter provides definitions of key terms that were used in this study. It further presents a review of theories appropriate for the study. The chapter also provides empirical literature review from similar studies done on the contribution of Microfinance institutions in development of Small enterprises. Finally, the chapter ends up by providing Conceptual Framework that guided the study.

2.1 Theoretical Literature Review

This chapter is concerned with the review of the other relative literature to what other authors and researchers observed about microfinance institutions with their contribution to development of small, medium enterprises.

2.1.1 Microfinance institution definitions

It is first necessary to make explicit definitions of microfinance institution, Microfinance service refers to the delivery of financial services such as credit, savings, insurance etc to low income clients who are without access to the delivery of financial services of formal sector financial institutions on sustainable basis (Parker, 2000). According to Aredo (1998) MFIs are often defined in terms of the followings characteristics (i) targeting the poor (ii) extending small business (iii) building capacity of the poor (iv) extending loans without collateral (v) combining credit with saving and (vi) charging market interest rate. Thus owner expects to get higher return from the savings or shares while as a client expect to enjoy low borrowing rates. The inherent encouragement is to improve the living condition of low income earners. Sound practice in microfinance institutions is based on ability to provide appropriate financial services to the individual and households that are otherwise excluded from the financial system (Parker, 2000).

Finally financial institution like Microfinance institution is not a new phenomena to any of nation in the world especially the developing countries.
Many author and scholar has done their investigation of formal bank and come up with different findings on developing countries where by Tanzania is included.

There is growing realization about potential contribution of micro business both developed and developing countries, because of their economic and organizational characteristics micro business played important economic social and political roles in employment creation resources utilization and peaceful manner (Robert, 2008).

Many micro business continue exist in these economies showing a skewed distribution of manufacturing enterprises with the model size being close to the smallest and along rightward tail stretching towards the giants. Most of the micro enterprises are service oriented or specialized niche in the market. Micro enterprises sector rightly considered to be the backbone of any developed economy, the most countries in Eastern Europe have already switched over to market based economy. The development which took place in USSR in 1991 also provides much scope to micro small, medium business in reviving the disintegrated economies (Dhameja, 2004).

Developing countries like India, china, Pakistan, Sri Lanka, Malaysia and many other south Asia countries have always considered micro small business as important sector for economy (Dhameja, 2004).

Fidler and Webster (1996) indicated that inclusion of saving in the microfinance menu of services could help in the generation of local funds for microenterprise development and contribute to sustainability of microfinance institution. They also argued that saving services enable the poor to accumulate surpluses that can be used at a later date to ride out dips in income or respond to emergencies.

2.1.2 SME's Definitions

A small business may be defined as a business with a small number of employees**.** The legal definition of "small" often varies by country and industry. Wangwe, (1999) argues that the definition of Micro and Small Enterprises (MSE) is slippery and has not been universally agreed. 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, (2003) defines Small and Micro Enterprises as those employing up to 4 persons; Small Scale Enterprises as those employs between 5 and 49 persons and Medium Size Enterprises as those employing between 50 and 99 persons.

In the European Union (EU), Small to Medium Enterprises is defined as a business with a headcount of fewer than 250 is classified as medium-sized; a business with a headcount of fewer than 50 is classified as small, and a business with a headcount of fewer than 10 is considered a micro business. The European system also takes into account a business's turnover rate and its balance sheet (Kirkpatrick, 2008). In most economies micro enterprises are much greater in number. In India the major advantage of the sector its employment potential at low capital cost. As per available statistics this sector employs can estimates 31 million persons spread over 12.8 million enterprises and labor intensity in micro enterprises (MEs) sector is estimated to be almost 4 times higher than the large enterprises. But according to small business Administration, micro business is one that does not dominate its industry has less than 250 employees. Exceptions to these criteria but, small business Administration use these benchmark for evaluating loans and business assistance.

In the U.S Micro Enterprises is regarded as business with 5 or fewer employees. Many of this business have no employees other than the self employed owners. Such micro enterprises generally need less than 35,000 US dollars in loan capital and do not have access to the conventional commercial banking sector. Most organizations in the field also focus their services on those micro entrepreneurs who are low to moderate income. Microenterprises in U.S has 20 years history as field, it was commonly used internationally by the late 1970s and most of these micro entrepreneurs are minorities, recently immigrant, women, disabled or for other reasons have special challenges that reduce their ability to access traditional and other services.[2]

In developing countries micro enterprises comprises the vast majority of small business sector as result of relative lack of formal sector jobs available for the poor. Micro enterprises in developing countries then tend to be most frequent form or size of business (Wangwe and Tsikata, 1999).

In India, the Micro and Small Enterprises (MSEs) sector plays a pivotal role in the overall industrial economy of the country. It is estimated that in terms of value, the sector accounts for about 39% of the manufacturing output and around 33% of the total export of the country. Further, in recent years the MSE sector has consistently registered higher growth rate compared to the overall industrial sector. The major advantage of the sector is its employment potential at low capital cost. As per available statistics, this sector employs an estimated 31 million persons spread over 12.8 million enterprises and the labor intensity in the MSE sector is estimated to be almost 4 times higher than the large enterprises[3].

In South Africa the term SMME, for Small, Medium and Micro Enterprises, is used. Elsewhere in Africa, MSME is used, for Micro, Small and Medium Enterprises. Size thresholds vary from country to country.[4]

In Kenya microenterprises about 70% of their business do not employ outside labor and the owner is the sole owner. Most of the employees are casual workers, trainees or family members especially in rural areas. In Kenya urban micro enterprises

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[2] *http://*www.simplifiedbiz.com accessed on 17 of February 2013

[3] *http://*www.simplifiedbiz.com accessed on 17 of February 2013

[4] *http://*www.simplifiedbiz.com accessed on 17 of February 2013

business are more likely to close than rural business. The MEs cover nonfarm economic activities mainly manufacturing, mining, commerce and services. There is no universally accepted definition of MEs.

Different countries use various measures of size depending on their level of development. Commonly used yardsticks are total number of employees, total investment and sales turnover.

In the context of Tanzania, micro enterprises are those engaging up to four people and in most cases the family members under informal sector with capital investment of up to five million Tanzania shillings. Small enterprises are mostly formalized businesses engaging between five to forty nine employees or with capital investment from five to two hundred million Tanzania Shillings, medium enterprises employing between fifty and ninety nine people or use capital investment from two hundred million Tanzania shillings to eight hundred million Tanzania shillings (see Table 2.1) (URT, 2003)[5].

The main types of MEs identified in study area are food vending, retail (shops/ kiosks and retail general (i.e. Genge), used cloth selling and tailoring that were few in number contribute total number of micro enterprises financed by WANAMA SACCOs in Ilala municipal. (USACA SACCOs report 2008).

Table 2. 1 Categories of SMEs in Tanzania

CATEGORY	EMPLOYEES	CAPITAL INVESTMENT (Million TShs.)
Micro Enterprise	1 – 4	Up to 5m
Small Enterprise	5 – 49	5m < x ≤ 200m
Medium Enterprise	50 – 99	200 < x ≤ 800m

[5] [5]United Republic of Tanzania (2003), Small and Medium Enterprises Development Policy, Unpublished Report, Ministry of Industry and Trade, Dar-es-Salaam.

Large Enterprise	x ≥ 100	800 m < x

Source: MIT (SMEs Development Policy, April.2003, p.5)

2.1.3 Microfinance and Poverty Reduction

Microfinance has become very famous in the past decade and has boosted among the public interest on poverty reduction tools. The majority of people in developing countries are considered to be very poor and unable to accumulate substantial savings. They need an external finance to break away from the bad circle of poverty (Robinson, 2000).

Robinson, (2000) reviewed that microfinance institutions are important for poor people in providing credit and mobilizing savings. MFI can expand and diversify enterprises and helps to reduce risk, improve management, raise product, helps in increase household's income and provide credit at much lower cost than credit from informal commercial moneylenders. Cohen, (2000) concluded that access to microfinance is a key risk management strategy for clients, and MFIs services reduce vulnerability and contribute to poverty alleviation. Scholars and development practitioners have in recent years devoted considerable attention to lend successfully to poor people.

Bamco, (2000) argued that microfinance institutions have found that, poor household are interested in a variety of saving services and products. Deposits services allow low income households to save for different reasons including accumulate funds for future investment such as purchasing livestock, children's education ,housing construction ,purchasing of machinery, managing irregular income streams and social and religious obligations such as life crises, ceremonies, religious holidays ,contribution to local funds and functions old age and disability.

From perspective of microfinance institutions clients, the advantage of deposit facilities includes a combination of access to cash, rate of return and divisibility of savings. On other hand, from an institutional perspective ,well designed and well delivered deposit services can lead to the successful intermediation of financial services by microfinance institutions through reducing their dependency on external funding and generating stable stream of capital to support financial operations (Bamco,2000).

2.1.4 The Microfinance in Household level.

The assessing impact at the participant level requires adjustment to control for differences in unobservable household and village characteristics That is, to measure the credit impacts of programs that are due to variations in individual level participation, it is necessary to control for differences in village level characteristics that attract a program to particular village.

According to Yaron, (1997), the impact of program placement on village level average income, employment and poverty is estimated at the village level regression that measures the difference impacts of program placement at the village level while controlling for observable characteristics of the village. Group-based credit program may be efficient for joint production and consumption behavior of households. It may also be beneficial for such households to borrow from group –based credit program, which charges less than informal lenders, in order to make more efficient use of available resources, mainly family labor. In this case the evaluation of the effects of program participation on household's resource allocation is based on this efficiency argument.

Assessing the impact of credit involves one basic program; unless household are shown to be credit constrained (meaning that households are constrained by lack of liquidity and do not have access to credit to solve their credit problem), it may be difficult to show the impact of credit on behavioral outcomes such as income and employment.

Khandker, (1999) recommended that rather than formally test whether borrowers of group based credit program are constrained by program design. This assumption seems valid for several reasons. First, in the case of group-based lending to the

landless, the time path of credit allocated to the members is part of the dynamic optimization problem of group and the level of credit provided to each individual in the group is tailored to fund a new self –employment project of certain size. Second the cost of credit includes not only the interest rate but also the timing of repayment and the penalties associated with defaults.
Third, group based credit is packaged with both responsibilities (meeting attendance, forced saving default risky) and benefits (Training, insurance and consciousness raising), which are likely to make cost of credit endogenously determined by household characteristics. Finally, the close monitoring aspects of group based lending make group credit no fungible.

If there were no monitoring of the use of borrowed funds and no group responsibilities and decision- making in the lending program, individual would likely want to borrow much more than they actually do in order to capture the premiums associated with the soft terms of the loans. The most important effect of borrowing from a micro credit program is its impact in the per capita expenditure. Because borrowers are poor, increase in consumption as a result of borrowing from micro credit program had a positive effect on per capita expenditure. Because borrowers are poor, increase in consumption as result of borrowing from a micro credit program constitute an immediate welfare gain. Microcredit programs facilitate self-employment, mostly in rural non-farm activities that can be undertaken at home without high transaction costs.

Microfinance had a significant impact on children's schooling especially for boys, girls for nutritional well being. Also to households who were relying on agriculture by diversifying into rural non-farm activities. Participation in a micro credit also affected socio economic variables, including children's schooling and children's nutrition (Tsehay and Mengistu, 2002).

2.2 Empirical literature Review

2.2.1 Microfinance and Poverty Reduction

Studies done by Rhyne, (2001) revealed that, although most microfinance institutions were far from achieving financial self-sufficiency, there was evidence that poor households participating in micro-credit programmes benefited in terms of positive effects on incomes and poverty, but seem to have limited effects on employment and technology.

Although, the relationship between poverty reduction and microfinance is debatable, Rhyne (2001) noted that the field knows little about the poverty level of the clients in various programs. Just as the causes of poverty are complex so is its reduction. This means microfinance as it is, should run in a more or less commercial basis while poverty is a complex phenomenon needing complex and multisectoral solutions. Many researchers argue that the microfinance can reduce poverty through increased income which will improve standard of living, empowering women financial power so that they are able to access loan and start their own businesses, develop the business sector through growth potentials, and develop a parallel financial sector.

2.2.2 The Role of Credit in Generating Entrepreneurial Activities in Tanzania

Study carried by Rweyemamu, (2003) on the role of credit in generating entrepreneurial activities in Tanzania found that, the output of enterprises increased following the access to the credit whereby, the enterprises whose owners received business training and advice, performed better than those who did not receive training. Therefore an environment should be created where informal and quasi-informal financial institutions can continue to be easily accessed by micro and small businesses. However, access to formal banking services is difficult for the poor. The main problem being difficult collateral demanded by these formal financial institutions when one need to acquire loans.

In addition, the process of acquiring a loan entails many bureaucratic procedures, which lead to extra transaction costs for the poor. Formal financial institutions are not motivated to lend money to the poor. In general, formal financial institutions show preference for urban over rural sectors, large-scale over small scale transactions, and non-agricultural over agricultural loans. Formal financial institutions have little incentives to lend to the rural poor for the following reasons:- Administration difficulties: small rural farmers often live geographically scattered in areas with poor communication facilities, making loan administration difficult.

Systematic risks: agricultural production is associated with some systemic risks, such as drought and floods, which is reflected in a high covariance of local incomes; Lack of information: the absence of standardized information, standard lending tools, such as financial statements or credit histories, does not exist in these areas; Repayment problems: the repayment of working capital may be required only once a year for example during the harvest season.

2.2.3 The Role of SME's Policy in Development of Small, Medium, Micro Enterprise in Tanzania

According to Edward, (2003) in his study on the Role of SME's Policy in Development of Small, Medium, and Micro Enterprise in Tanzania, he concluded that, it is now increasingly recognized that the Small and Medium Enterprises (SMEs) play a crucial role in employment creation and income generation in Tanzania. SMEs all over the world and in Tanzania in particular, can be easily established since their requirements in terms of capital, technology, management and even utilities are not as demanding as it is the case for large enterprises. These enterprises can also be established in rural settings and thus add value to the agro-products (Supporting Kilimo Kwanza) and at the same time facilitate the dispersal of enterprises. Indeed SMEs development is closely associated with more equitable distribution of income and thus important as regards poverty alleviation. At the same time, SMEs serve as a training ground for emerging entrepreneurs.

Thus SMEs need special attention and good atmosphere that can assist them to grow and sustain in this stiff business environment. It is for this reasons Government and other stakeholders need to implement the SMEs development policy and other government policy to nurse SMEs development.

According to the research findings, the role of SME's development Policy in development of SME's revealed that its positive that the SME's Development policy plays it role in development of SME's as revealed though the findings on the responded research questionnaires which mainly targeted to check the role of SME's in the core areas which are the major constraints on SME's development such as legal and regulatory framework, infrastructure, Business development services, and access of SME's to finance and further to the needs for Government to formulate SME for implementation of the SMEs Policy in Tanzania.
As revealed from the distributed questionnaires, more than 70% of the respondents support and agree with the role of SME's development policy in contribution towards development of SME's in Tanzania. SME Development Policy was formulated so as to address the constraints and to tap the full potential of the sector, constrains include unfavorable legal and regulatory framework, undeveloped infrastructure, poor business development services, limited access of SMEs to finance, ineffective and poorly coordinated institutional support framework etc.

The policy also serves as guidelines to all stakeholders and thus stimulates new enterprises to be established and existing ones to grow and become more competitive

It is therefore a joint responsibility between Government, other stakeholders and SMEs to make sure there is a growth of SMEs in Tanzania as well as conducive business environment.

In conclusion, the Government, NGOs, and banks should have a big role to play on improving the position of small-scale industries. Government should help small-scale industries groups by encouraging existing financial institutions to extend credit to SMEs. NGOs could support SMEs sector by providing funds directly or through joint ventures. They could provide training facilities, consultancy funds and technical assistance. Financial institutions too could simplify credit procedures and link them to small- scale industries self-helped and pressure group. This will enable the SMEs to produce at lowest cost, as well be able to compete in the market for the high quality of products produced by SMEs.

2.2.4 The Role of Microfinance and Implications to the Poor

According to the study done by Andrew, (2011) on The Role of Microfinance and Implications to the Poor: A Case of FINCA – Dar es Salaam, he pointed out that, one of the major objectives of MFIs is to access money to the poor who are denied by the formal banks and who are unable to afford the prohibitive interest levied by private moneylenders. Thus MFIs, including FINCA are expected to aim at reducing the dependence of poor households on private moneylenders, even for consumption during difficult seasons in their effort to reduce income variability.

Most programs are not optimally designed nor necessarily offering the most desirable financial products as observed by (Murdoch, 1999). Similarly as shown in the findings, a significant part of FINCA loan is spent on household consumption and other non-productive activities. Therefore it is important to identify and bridge such demand gaps and make microfinance services demand driven instead of supply driven.

There is no agreement among people seeing poverty reduction as the ultimate goal of microfinance as to whether this goal is best fulfilled by exclusively targeting the poorest of the poor or by providing financial services on a broader basis to low income people.

2.2.5 The ME's sector in Lagos.

In Lagos study focused also in a wide range of activities including a few enterprises in primary industries relating to agriculture and mining and utilities. About 70 percent of the female labor force in Lagos in 1963 was in petty trading and others related occupations but recently the situation has increased in which about 88 percent both female and male engage in petty in informal sector. The national statistic shows that 11 percent of the entrepreneur had formal education at all, while 89 percent had informal education (Sethuraman, 1997).

2.2.6 Development community supports SME's Development

According to Deloitte, (2004), In order to achieve the millennium Development Goals (MDG), including the goal of reducing by 50% the number of people living in extreme poverty by 2015, it will be necessary to stimulate the development of the private sector in developing countries including the SME's sector. Growing the SME sector in developing countries leads to broad based growth, job creation, economic stability and more flexible economy. SME's are also risk takers and provide innovation and an entrepreneurial approach in the commercial sector. SME's are the critical engine for private sector led growth and increasingly important from an environmental perspective.

The social benefits of a strong and vibrant SME sector are also provide empowerment and a route out of poverty for many of the poor in developing countries. SME's have a positive impact on income distribution although it is recognized that it is the smaller enterprises that must be specifically targeted in order for the benefits of SME's development to reach the poorest (Deloitte, 2004)

2.2.7 Sustainability of Microfinance Institutions

Hossain, (1988) argue that the Grameen Bank approach has a fair chance of success in densely settled poverty stricken areas of Asia, but for Africa an appropriate delivery mechanism has to be worked out through trial and error. The Grameen Banks approach of formation of small homogenous groups for group guarantee of loan and supervision of loan utilization, recovery of loan in small regular installments and institutions of collective saving could work well across different environments. However, elements like taking the bank to the poor people and intensive interaction of bank staffs with borrower may not appropriate and could become too costly for sparsely settled people.

According Bediye (1997), to be successful in credit provision and savings mobilization, there are a number of strategies that can be adopted but there is no single approach, which is applicable for all countries. For example, Grameen Bank approach may not work for all in delivery of credit but one of the appropriate procedures can be developed only after considerable experimentation through understanding of the physical and social economic conditions.

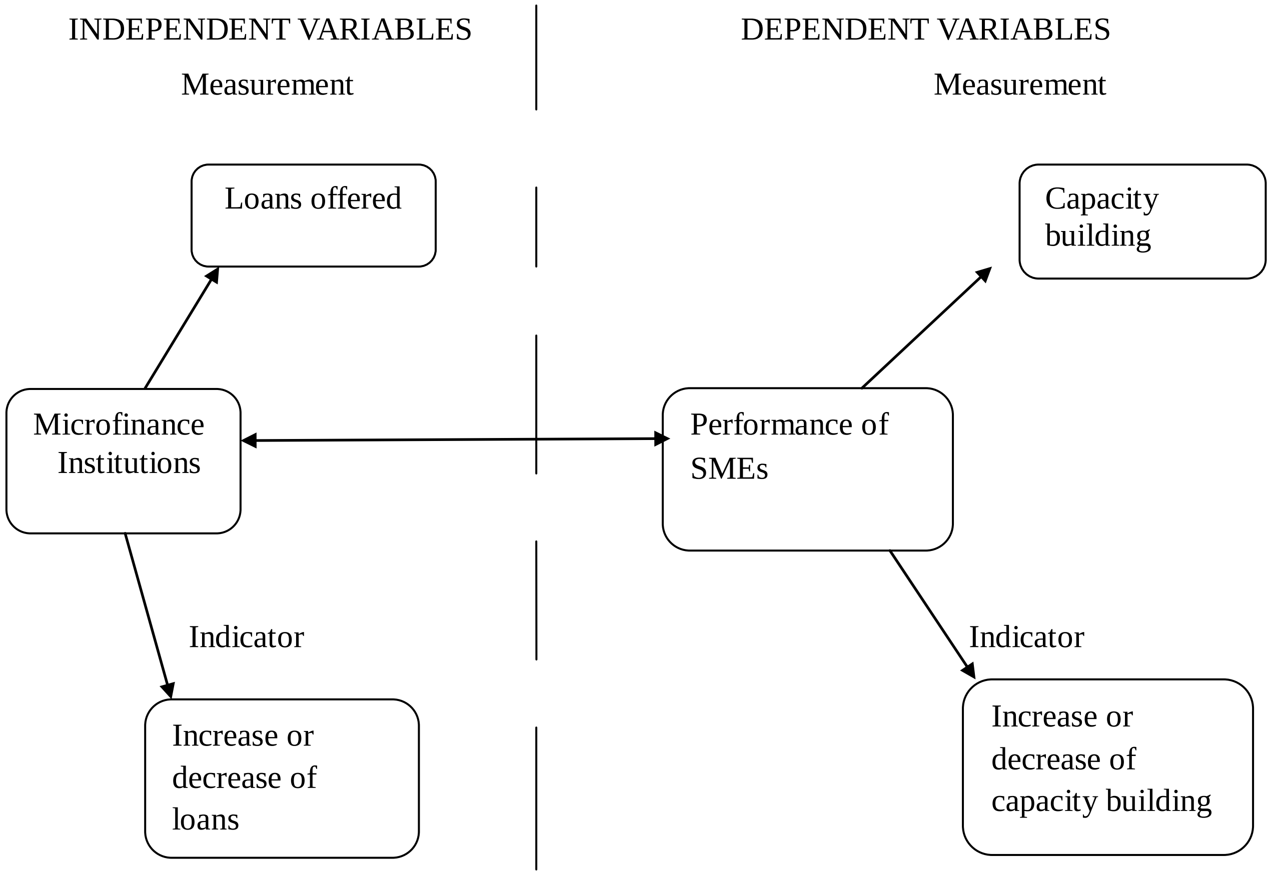
Bediye, (1997) concluded that credit analysis and appraisal should at least cover the following points: Client background, past and existing client institution relationship, purpose of loan, group pressure (collateral), business plan, risk analysis and recommendation.

After the disbursement of loan, credit monitoring is important in ensuring that loan proceeds are directed to the intended purpose and provide appropriate advice to the borrowers.

Adams, (1988) suggested the criteria for success of loan recovery. The criteria should include the number of client, declining transaction cost overtime, improved loan recovery and total volume of savings achieved. Loan defaults are caused by two main factors. These are inability to repay and unwillingness to repay.

2.3 Conceptual Framework

Figure 2. 1: Relationship of Variables



Source: Adopted Kikula, 2012

2.3.1 Description of the conceptual frame-work

Performance of Microenterprises (dependent variable) can be a result of the many factors. The assumption of this study is that, there are both direct and indirect factors which are referred to as independent (direct) and intermediate (indirect) variables. Independent (direct) variables are those variables that influence the dependent variables. They cause or affect the dependent variables to change; while intervening variables are variables through which independent variables act to influence the dependent variables. They intervene the relationship between independent and dependent variables, (Kombo & Delno, 2006).

Access of loans to Microenterprises will lead to their performance in terms of income increase and growth. Capacity building is required to ensure performance of SMEs once they access loans from Microfinance institutions. Increase or decrease of capacity building will have positive and negative effect to SMEs performance respectively.

Performance of SMEs will depend on microfinance loans. An increase or decrease of number of loans offered by microfinance institution will directly affect microenterprises performance. A good microfinance policy is required for guiding and regulating microfinance operations and to facilitate access to loans by microenterprises. Establishment of more microfinance institutions will mean more loans opportunities available to microenterprises. Without a good microfinance policy, it will be difficult for microfinance institutions to serve their purpose. For micro enterprises to enjoy the loans MFIs will be required to offer affordable interest rates, a short loan process and affordable collateral which will implicate to the number of loans offers to MEs. This is to make the loans accessible at the right time and make it helpful to the micro enterprises instead of being a burden to them.

CHAPTER THREE

RESEARCH METHODOLOGY

3.0 Introduction

This chapter presented the research methodologies used by researcher for gathering information from the field. It describes, research design, study area, sampling techniques, and tools in collecting data as data analysis techniques.

3.1 Area of the study.

Ilala Municipal Council is the one of three Municipal Councils within the city of Dar es Salaam in Mainland Tanzania. Ilala municipality bears of status of administrative district between 6° and 7° and longitude 39° and 40°East south of the equator . It has an area of 210km². The Municipality is boarded by the Indian Ocean on eastern part with distance of about 10 km, on southern part is boarded by Kisarawe district and on the north is boarded by Kinondoni municipality.

The choice of the study area was due to the reason that 60% of microfinance institutions in Dar es Salaam region are located in Ilala Municipality (Ilala Municipality, 2010)[6]. Small businesses were also concentrated in Ilala municipality especially Kariakoo, Ilala and Buguruni areas. Therefore the researcher was interested to find out the impact of the available microfinance institutions to small businesses in the area.

3.2 Research design.

Research design refers to the arrangement of conditions for collecting and analyzing data in a manner that aim at combining relevance to the research purpose with economy in procedure. Moreover Research Design refers to the strategy to integrate the different components of the research project in a cohesive and coherent way. It is

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[6] Ilala Municipal Council (2010) Five Year Performance Report(2010-2015);for submission to PO-RALG

a means to structure a research project in order to address a defined set of questions (Trochim and Land, 1982).

In this study, the researcher used case study design which involved collection of empirical data from the Ilala Municipality sampled microenterprises owners and microfinance officers. Case study design was used in order to have in-depth study and contextual analysis of the situations in Ilala Municipality so as to come up with a general conclusion of the study.

3.3 Target populations and Sample Size

3.3.1 Target Population

A population comprises of any set of persons or objects that possess at least one common characteristic (Busha and Harter, 1980). The population is the entire group a researcher is interested in; the group about which the researcher wishes to draw conclusions. The population can be very large or small, depending upon the size of the group of persons or objects from which researcher plans to make an inference.

According to national house hold census 2002, Ilala municipality had a population of 634,924 with an average growth rate of 4.6%. The inhabitants are of mixed tribe ethnic and with different dialect.

Since the study aimed at making the assessment of contribution of Microfinance Institutions in development of Small Enterprises in Tanzania by taking Ilala Municiparity as a case study, the target population composed of two categories, which included the Small Enterprises operators who have accessed Microfinance Institution services and Microfinance Officers. The Small Enterprises operators were those based in Ilala Municipality, they included SME traders from Kariakoo, Karume, Kongo, Msimbazi, Mnazimmoja, Mchafukoga, Jangwani and Ilala boma. Since the targeted population was too large to work with, constrains limited the researcher to a small sample in both categories.

3.3.2 Sample Size

A sample is a small group of respondent drawn from the population that the researcher is interested in gaining information and drawing conclusion.

Researchers are forced to take samples instead of complete enumeration for two basic reasons that relate to efficient utilization of the budget (cost) and time. Baradyana and Ame, (2007).

The sample size for the study was 60 respondents who included 40 Small enterprises owners who have accessed loans from different microfinance institutions and 20 Microfinance Institutions officers in Ilala Municipality.

3.4 Sampling procedures

Non-probability sampling methods were employed by the researcher. Convenience and judgmental sampling methods were used. Convenience method was used to select 40 respondents from Small enterprises operators and judgmental methods was used to select 20 respondents from Microfinance Institutions officers from the targeted population who were regarded to be resourceful in terms of data and other information concerning the study.

Table 3. 1 Sample size distribution of the population n=60

Category of Respondents	Frequency	%
Micro Entrepreneurs (Retail shops, used cloth sellers, Food vendors, Hardware shops and Tailors)	40	66.66%
Microfinance Institutions Employees (Branch managers, Loan Officers)	20	33.34%
TOTAL	60	100%

Source: Field data, 2012

3.5 Data Collection Methods

Due to complexity of the study, the researcher employed a number of data collection methods which included; Primary data and Secondary data; in the primary data include; interview, questionnaire, observation, and focus group discussion. Secondary data include; Documentation.

3.5.1 Primary Data

3.5.1.1 Interview

The method was used by researcher to obtain the data related to demographic variables such as age, sex, marital status, occupation and life style as well. Also information on the contribution of Microfinance institutions to the development of micro enterprises in Ilala Municipal council was collected through this method.

3.5.1.2 Questionnaire

This method was used by a researcher to attain information related to the contribution and role of Microfinance institutions to development of micro enterprises in Ilala Municipal council. Both open ended and closed ended questionnaire were used to collect data.

3.5.1.3 Observation

This method was used to obtain data concerning the contribution of microfinance institutions to development of micro enterprises of some of information is sensitive for it tone collected in a structured interview situation because what people say may differ from what happening in reality.

3.5.1.4 Focus Group Discussion

During the study, researcher conducted group discussion in Ilala involving food vending (Mamalishe), retail shops and used cloth sellers (Mchikichini) as representatives in Ilala Municipality. Information obtained through this method complements data collected by primary data collection methods. Researcher recorded data obtained through the discussion.

3.5.2 Secondary Data

3.5.2.1 Documentation

This method was used as source of obtaining data which have been collected by others; a researcher used various books, pamphlets, journals, magazines and files as well as research reports and report from various current websites.

3.6 Data Analysis

Bodgan and Biklen, (2003) define data analysis as working with data, organizing and breaking it into manageable units, as well as discovering the most important facts and lessons. Further, data interpretation involves deciding about what data and information should be used to respond to the specific objectives of the study both in quantitative and qualitative terms. In this study, both quantitative and qualitative data analysis methods were used. Quantitative data were analyzed and presented in tables, figures and percentages supplemented by short descriptions. Qualitative analysis involved examining data by basing on attributes. Moreover descriptive method was used to elaborate and make the data more explicit and understandable.

CHAPTER FOUR

RESULTS AND DISCUSSIONS

4.0 Introduction

This chapter presents, scrutinises, and analyses the data so collected from the field work. With the help of the use of the measures of central tendency, findings have been presented using tables, graphs and charts. Analysis was done qualitatively with the help of quantitative techniques presented data using the above mentioned measures.

4.1 Respondents Age Distribution Structure

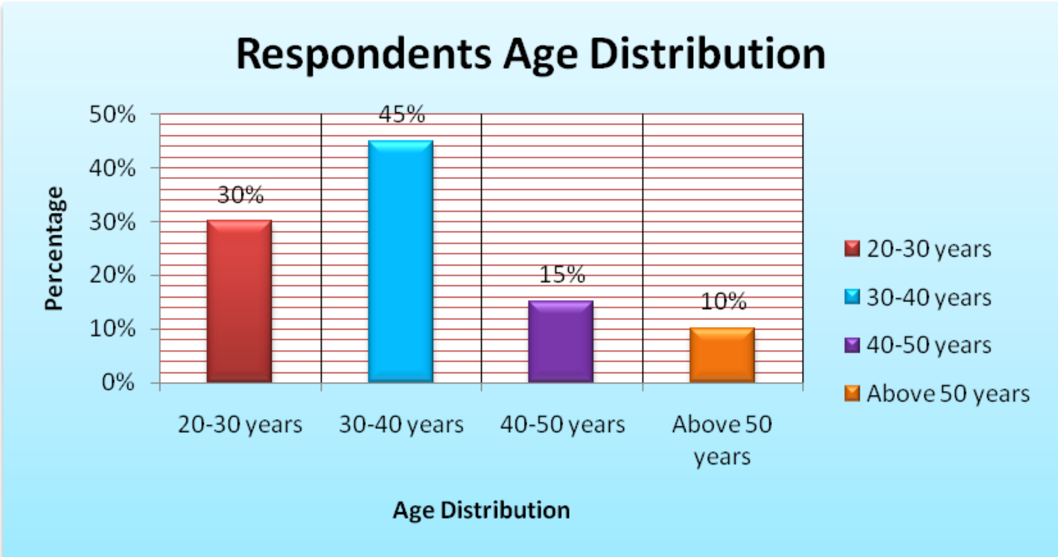
Table 4. 1 Age Distribution of Respondents **n=60**

Age of Respondents	No of the Respondents	Percentage (%)
Between 20-30 years	18	30
Between 30-40 years	27	45
Between 40-50 years	9	15
Above 50 years	6	10
Total	60	100

Source: field data, 2013

The age distribution structure of 60 respondents who included 40 microenterprises and 20 microfinance institution officers in Ilala municipality participated in this study. The table 4.1 summarizes the age distribution structure as per study findings.

Figure 4. 1. Respondents Age Distribution Structure n=60



Source: Field data, 2013

Figure 4.1 represents findings on age distribution for 60 respondents involved in the study (40 microenterprises and 20 microfinance institution officers).

18 respondents who represented 30% of the total respondents participated in this study were having the age of between 20 to 30 years. 27 respondents who represented 45% of the total respondents participated were having the age of between 30 to 40 years, and this was the largest age group in the sample. 9 respondents who represented 15% of the total respondents participated were having the age of between 40 to 50 years, and 6 respondents who represented 10% of the total respondents participate were having the age above 50 years. Findings showed that majority of microenterprise respondents were of age between 30-40 years. Respondents of age above 50 years were fewer because it was the old age.

4.2 Respondents Gender Distribution Structure

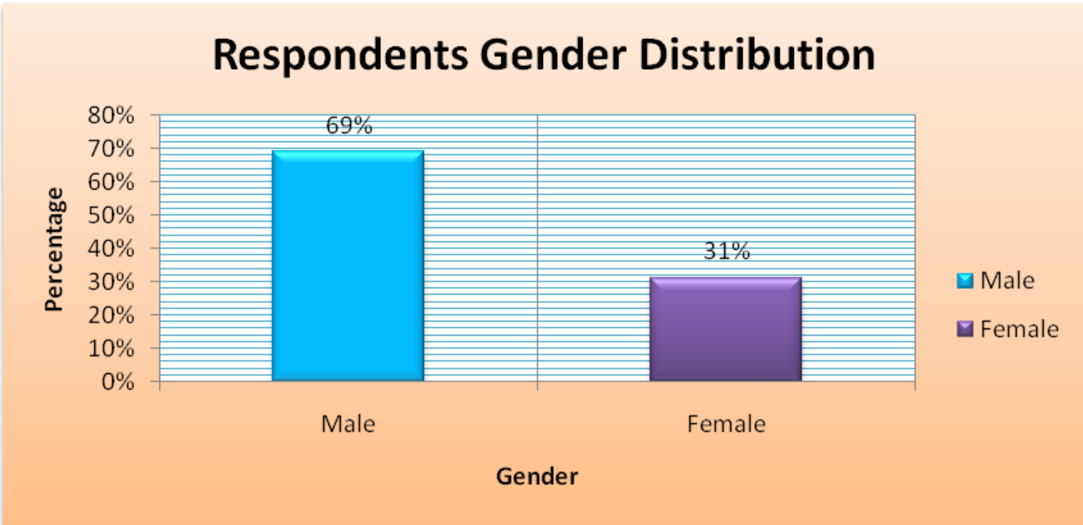
Table 4. 2 Respondents Gender Distribution Structure n=60

	Gender category		
	Male	Female	Total
No. of Respondents	41	19	60
Percentage of respondents	69%	31%	100%

Source: Field data, 2013

In assessing the contribution on Micro-Finance Institutions in development of small enterprises in Tanzania 60 respondents were involved in the study. Table 4.2 summarizes the gender distribution structure as per study findings.

Figure 4. 2 Respondents Gender Distribution n=60



Source: Field data, 2013

Figure 4.2 show that, 41 respondents which was equivalent to 69 percent of total respondents were males, while 19 respondents which was equivalent to 31percent of total respondents were females. The ratio of women to males as per findings was 1 to 2, such higher proportion of percentage indicated a disparity between males and females and this was attributed from the fact that there were few women among microenterprises owners approached by the researcher in the field who were ready to be included and participate in the study.

4.3 Microenterprises Respondents Education Distribution Structure

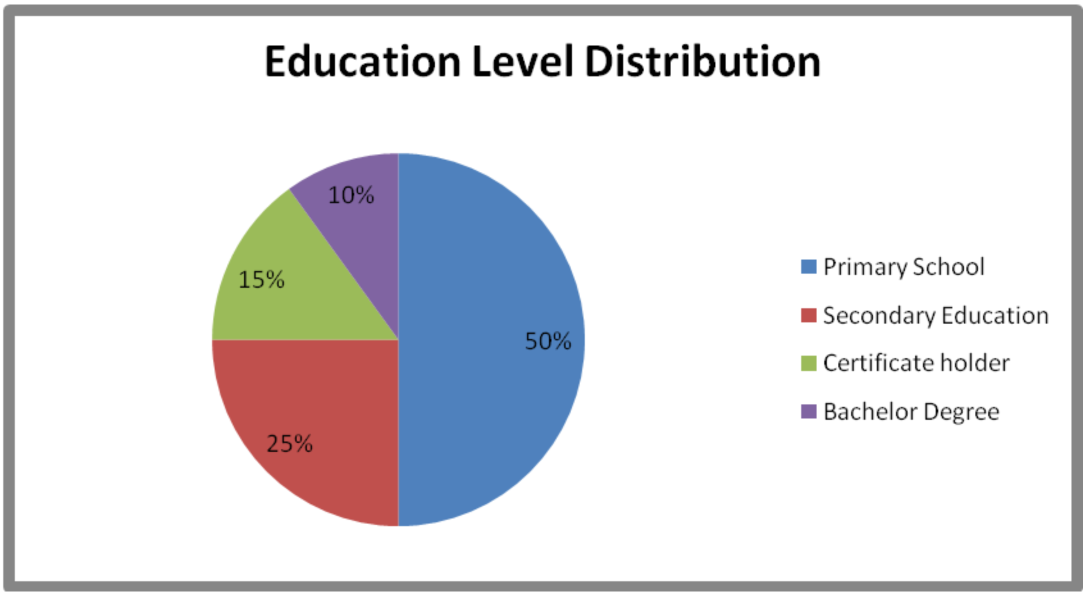
Table 4. 3 Microenterprises Respondents Level of Education n=40

Education level	No of the Respondents	Percentage (%)
Primary school	20	50
Certificates holder	10	25
Diploma	6	15
Bachelor degree	4	10
Total	40	100

Source: Field data, 2013

A total of 40 respondents from small enterprises operators were asked on their level of education. Table 4.3 summaries the education level distribution structure of microenterprises owners involved in the study.

Figure 4. 3 Education levels of the Microenterprises Respondents n=40



Source: Field data, 2013

Figure 4.3 portrays that, among the 40 microenterprises respondents involved in the study, 20 respondents who represented 50% of total respondents had Primary education level. Those with secondary school education were 10 which represented 25% of total respondents, Diploma holders were 6 respondents representing 15% of total respondents, and bachelor degree were 4 respondents which represented 10% of total respondents. Based on these results it can be suggested that the majority of small enterprises operators were holders of primary school and secondary school education. The results were consistent with Diyamett, (2012) on education level of microenterprises were majority of respondents (71%) were primary level holders.

4.4 Types of Small Enterprise Respondents

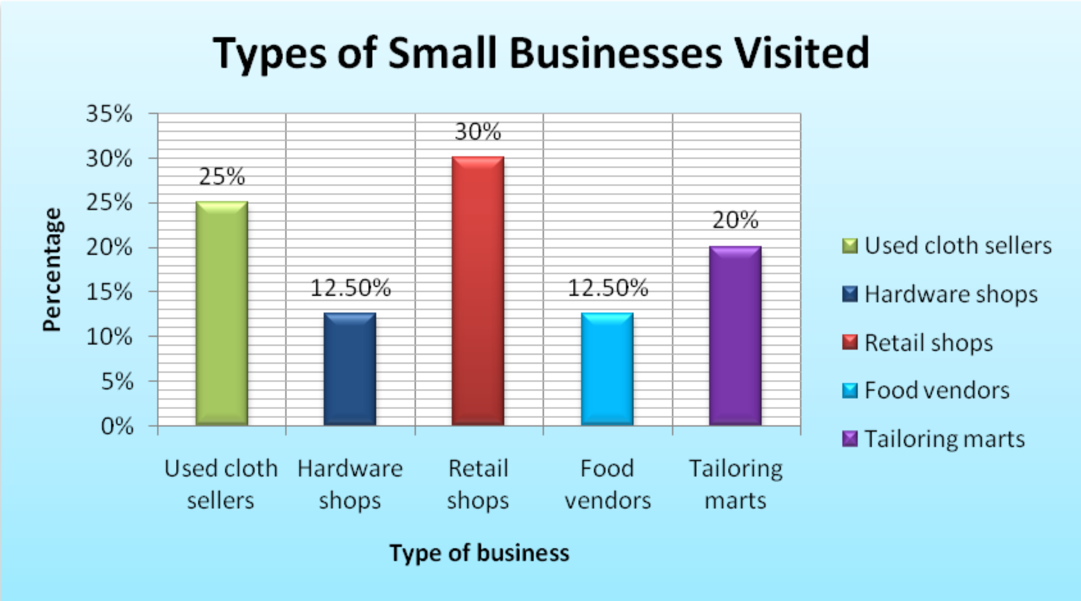
Table 4. 4 Types of small enterprises included in the study n=40

	Types of Businesses Visited					
	Used cloth sellers	Hardware shops	Retail shops	Food vendors	Tailoring marts	Total
No. of Respondents	10	5	12	5	8	40
Percentage %	25	12.50	30	12.50	20	100

Source: Field data, 2013

In response to the questionnaire administered regarding the type of business microenterprises, Table 4.4 summarizes data from the responses from 40 respondents involved in this part of study.

Figure 4. 4 Types of small enterprises included in the study n=40



Source: Field data, 2013

Figure.4.4 shows that 10 respondents who represented 25% of total respondents were used cloth sellers, 5 respondents who represented 12.5% of total respondents were hardware shops, 12 respondents who represented 30% of total respondents were retail shops, 5 respondents who represented 12.5% of total respondents were food vendors, and 8 respondents who represented 20% of total respondents were tailoring mart. From above findings, majority of microenterprises respondents were retail shops, used cloth sellers and tailoring marts. Results indicated the large group of microenterprises in Ilala was retail shops and the ones who were fewer in number were hardware shops and food vendors. These results are inconsistence with Andrew, (2011) on the type of small enterprises which in addition he included saloon and poultry keeping businesses.

4.5 Financial knowledge of Microenterprises Respondents

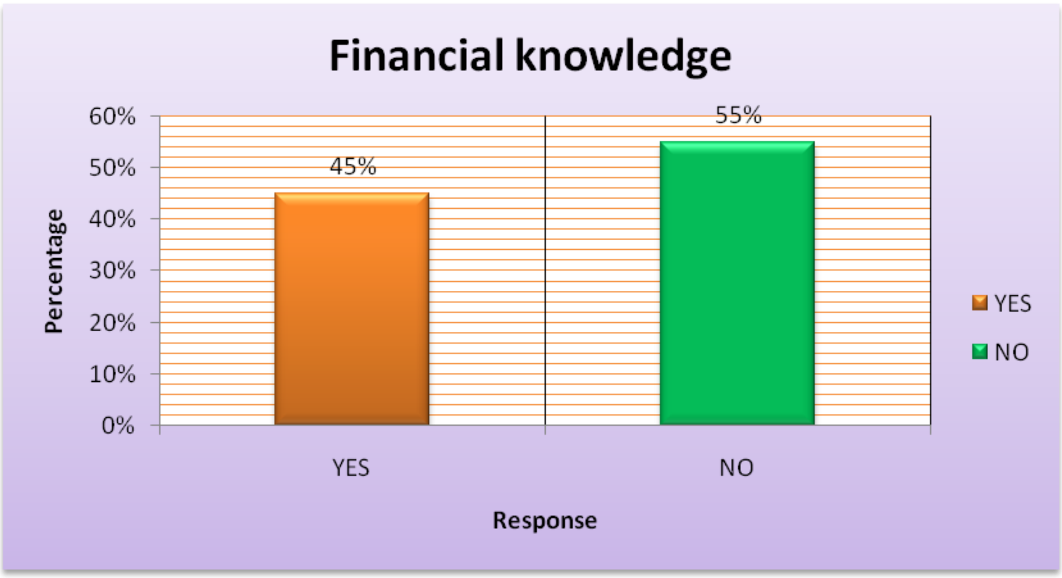
Table 4. 5 Financial knowledge of Microenterprises Respondents n=40

Response	No of Respondents	Percentage (%)
YES	18	45%
NO	22	55%
TOTAL	40	100%

Source: Field data, 2013

In order to identify the financial knowledge of the respondents, respondents were asked to state whether he/she had any knowledge on operating the business, accounting and business plan, a closed ended questionnaire was administered. The responses are shown in Table 4.5.

Figure 4. 5 Financial knowledge of Microenterprises Respondents n=40



Source: Field data, 2013

Figure 4.5 shows that, respondents with financial knowledge were 18 this was equivalent to 45% of the total respondents and those who had no financial knowledge were 22 which was equivalent to 55 % of the total respondents. These results suggested that majority of the small enterprises operators do not have financial knowledge to operate their business efficiently.

4.6 Services Provided to Microenterprises

Response from the question which asked *"What kinds of services were provided to micro enterprises?"*all 20 Microfinance Officers which was 100 percent of the total respondents who were given the questionnaire mentioned loans and savings as the main service provided to micro entrepreneurs. When interviewed they said, loans were the main services required by small businesses in order to increase their capital and expand their businesses. They said most of them become their clients because of the loan product offered. Very few of them opened account in order to save and if they deposited normally was for loan repayment and not savings.

4.7 Conditions Used by Microfinance Institution in Lending Loans

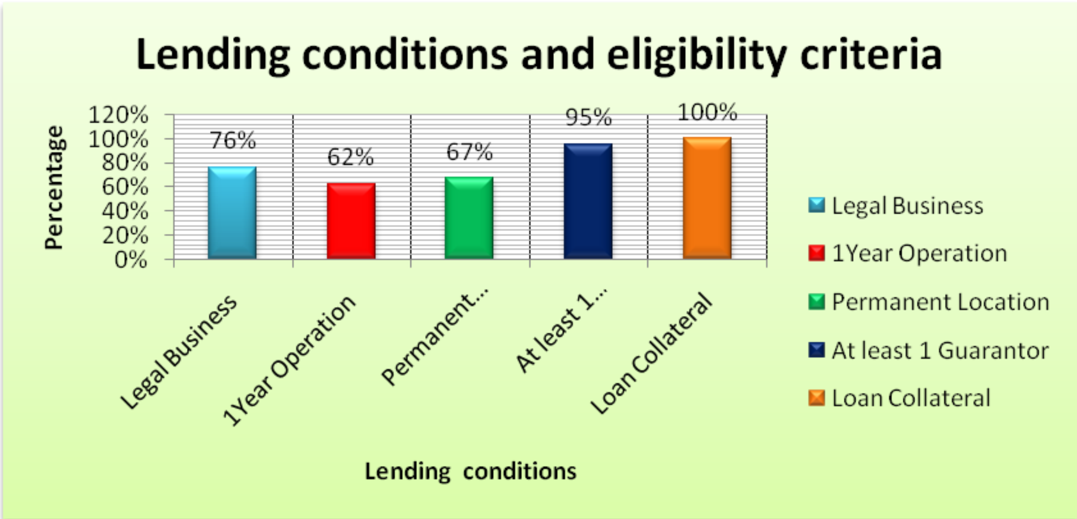
Table 4. 6 Lending Conditions and Eligibility criteria n=60

Conditions	No. of Respondents mentioned a condition	Percentage of Mentions per Total Respondents
Legal Business	46	76%
1 Year Operation	37	62%
Permanent Location	40	67%
At least 1 Guarantor	57	95%
Loan Collateral	60	100%

Source: Field data, 2013

In response to the question which asked, *"What were the conditions that Microfinance institutions use to provide loans to micro entrepreneurs?"* a total of 60 respondents from both microfinance institutions and micro entrepreneurs were given the open ended questionnaires.The study aimed to determine lending procedures and conditions employed by microfinance institutions. Interview, observation and documentation were also used to add to the findings obtained through questionnaires. Table 4.6 indicates the results on conditions mentioned.

Figure 4. 6 Lending conditions and eligibility criteria n=60



Source: Field data, 2013

Figure 4.6 represents findings on the lending conditions and eligibility criteria's for acquiring loans as mentioned by respondents. Operating legal business (registered or not registered) condition was mentioned by 46 respondents who represented 76% of the total respondents; 1 year operating business condition was mentioned by 37 respondents who represented 62% of the total respondents; having permanent business location condition was mentioned by 40 respondents who represented 67% of the total respondents; having at least 1 guarantor condition was mentioned by 57 respondents who represented 95% of the total respondents; and Pledge business/personal assets as collateral condition was mentioned by 60 respondents who represented 100% of the total respondents.

4.7.1 Operating Legal Business (Registered or Not Registered)

The study found that operation of a legal business (whether registered or not registered) was among the conditions and eligibility criteria for a business to access a loan in financial institutions.76 percent of the total respondents mentioned this condition as one of the important criteria which was normally checked during loan processing especially in the early stages of the process.

Legality of the business was important for the contract and also to make sure that microfinance are keen to social responsibility requirements, that is not to support illegal business by supporting their growth or capital.

4.7.2 Having Business that have operated for more than 1 Year

The study also found that 62 percent of the total respondents mentioned the condition of having a business that have operated for more than one year of business among the eligibility criteria for someone to apply for loan in financial institutions. This was because most microfinance institutions offer loans to businesses which are already in operation and not loans as capital for new business startup.

4.7.3 Having Permanent Business Location

It was revealed that having permanent business location (premises) was among the eligibility criteria for someone to be considered for loan application processing in financial institutions. This was mentioned by a total of 67 percent of the total respondents. This is very important in order to have assurance of the experience of the business operator in the area, provides assurance of the growing or stable business, and making it easy for follow up for loan repayment.

4.7.4 Having at least one guarantor

The study found that, having at least one guarantor who may be a business operator or an employee at a reputable organization is among the conditions and eligibility criteria for someone to apply for loan in microfinance institutions. This was mentioned by 95 percent of the total respondents. The guarantor was the person or company that provides a promise to assume responsibility for the debt obligation of a borrower if he/she defaults. In case the borrower defaults, the Guarantor can be contacted to help follow up with the client he /she has guaranteed to be given a loan by a microfinance institution, at the extremes, the guarantor properties may also be ceased to so as to pay back the loan defaulted by the borrower. Therefore Guarantor helps to reduce risk of defaulting by client and recovery of defaulted repayment money.

4.7.5 Pledge business/personal assets as collateral

It was also revealed that being able to pledge business assets or personal assets as collateral to secure the loan amount was among the conditions and eligibility criteria for someone to secure a loan from microfinance institutions. This was mentioned by all (100%) respondents. Lending agreement, collateral was a borrower's pledge of specific property to a lender, to secure repayment of a loan.

The collateral serves as protection for a lender against a borrower's default, that is, any borrower failing to pay the principal and interest under the terms of a loan obligation. If a borrower does default on a loan (due to insolvency or other event), that borrower forfeits (gives up) the property pledged as collateral and then the lender becomes the owner of the collateral. In a typical mortgage loan transaction, for instance, the real estate being acquired with the help of the loan serves as collateral. Should the buyer fail to pay the loan under the mortgage loan agreement, the ownership of the real estate is transferred to the bank. The bank uses a legal process called foreclosure to obtain real estate from a borrower who defaults on a mortgage loan obligation. These results are consistent with Mugendi, (2009) on the conditions and eligibility.

The results were inconsistent with Kessy &Urio, (2006) which included in addition to the later basic conditions; clients were required to form a group of five self selected members as a prerequisite for loan consideration for them to guarantee each other in their respective groups. Also in the case of default, it is even easier to make a follow up, since each group member knows each other better than the lender.

4.8. Required Documents for Business Loan Application in Microfinance Institutions

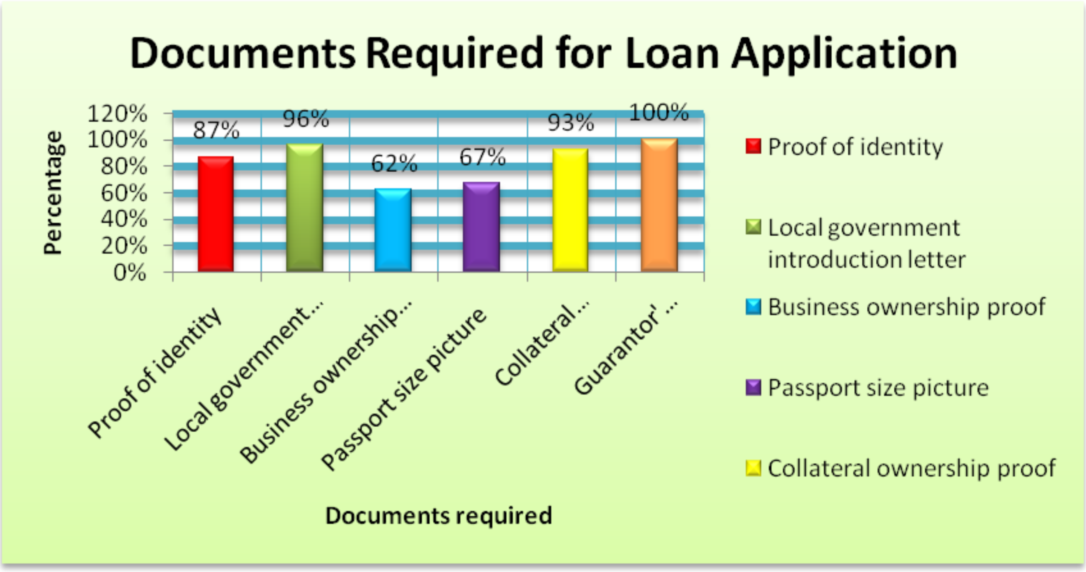
Table 4. 7 Documents required for loan application n=60

Documents for loan application	No. of Respondents mentioned a condition	Percentage of Mentions per Total Respondents
Proof of identity	52	87%
Local government introduction letter	58	96%
Business ownership proof	37	62%
Passport size picture	40	67%
Collateral ownership proof	56	93%
Guarantor' documents	60	100%

Source: Field data, 2013

The study aimed to determine types of documents required by the financial institutions to be presented by borrower at loan application stage. The open ended questionnaire asked the respondents to mention the documents required by microfinance institutions when applying for business loans. A total number of 60 respondents who included 20 employees and 40 microenterprises in Ilala municipality were involved to respond to the question. Interview as well as direct observation and documentation were used to collect additional data. Table 4.7 indicating respective percentages of mentions.

Figure 4. 7 Required Documents for Business Loan Application n=60



Source: Field data, 2013

Figure 4.7 represents findings on the documents required to apply for business loan in financial institutions which were as follows: - Proof of identity (Copy of identity card) document was mentioned by 52 respondents who represented 87% of the total respondents; Introduction letter from local government document was mentioned by 58 respondents who represented 96% of the total respondents; Proof of business ownership documents was mentioned by 37 respondents who represented 62% of the total respondents; Recent Passport size Picture was mentioned by 40 respondents who represented 67% of the total respondents; Proof of ownership of assets used as collateral was mentioned by 56 respondents who represented 93% of the total respondents; Guarantor's documents was mentioned by 60 respondents who represented 100% of the total respondents.

4.8.1 Copy of Identity Card

According to the information obtained by the study, it was revealed that copy of identity card was among the documents required to submit during loan application in financial institutions.

This was mentioned by total of 87 percent of the total sample. Respondents argued that the applicant was required to submit copy of original identity card such as voter's ID card, passport or driving license during loan application.

4.8.2 Introduction Letter from Local Government

It was also found that an introduction letter from local government was among the documents required to be submitted during loan application in Microfinance Institutions. This was mentioned by 96 percent of the total respondents. According to the views of the respondents the letter is required to provide proof of the residential areas where the client was living and if he was known by the local government authority where he was residing.

4.8.3 Proof of Business Ownership

Findings shows that Proof of business ownership was among the documents required to submit during loan application in Microfinance Institutions. This was mentioned by total of 62 percent of the total respondents. The documents that may be used are business license, business name registration certificate, taxpayer identification number (TIN) or if not registered the client is required to provide the letter from local government authority addressing his business. The proof of business ownership was explained to be important in order to have assurance on the eligibility and experience of the business owner. Apart from that it was said to minimize frauds made by unfaithful applicants claiming to operate business while not, and then at the end they became defaulters as they fail to repay the loan.

4.8.4 Recent Passport Size Picture

Recent Passport size Picture was among the documents required to be submitted during loan application in a Microfinance Institution. This was mentioned by 67 percent of the total respondents. The pictures are very important to recognize the person and make some crosschecks to make sure that the picture and the business owner are the same. If the client became a defaulter the picture was used to publish in the news papers for recovery actions.

4.8.5 Proof of Ownership of Assets Used As Collateral

The study also found that, provision of the Proof on ownership of assets used as collateral was among the documents required to be submitted during loan application at a Microfinance institutions. This was mentioned by 93 percent of the total respondents. These documents may be residential license for house, receipts for home appliances, registration cards for motor vehicles etc. It helps to prevent the borrower from having multiple loans using the same asset(s) and asset seizure in can the borrower defaults.

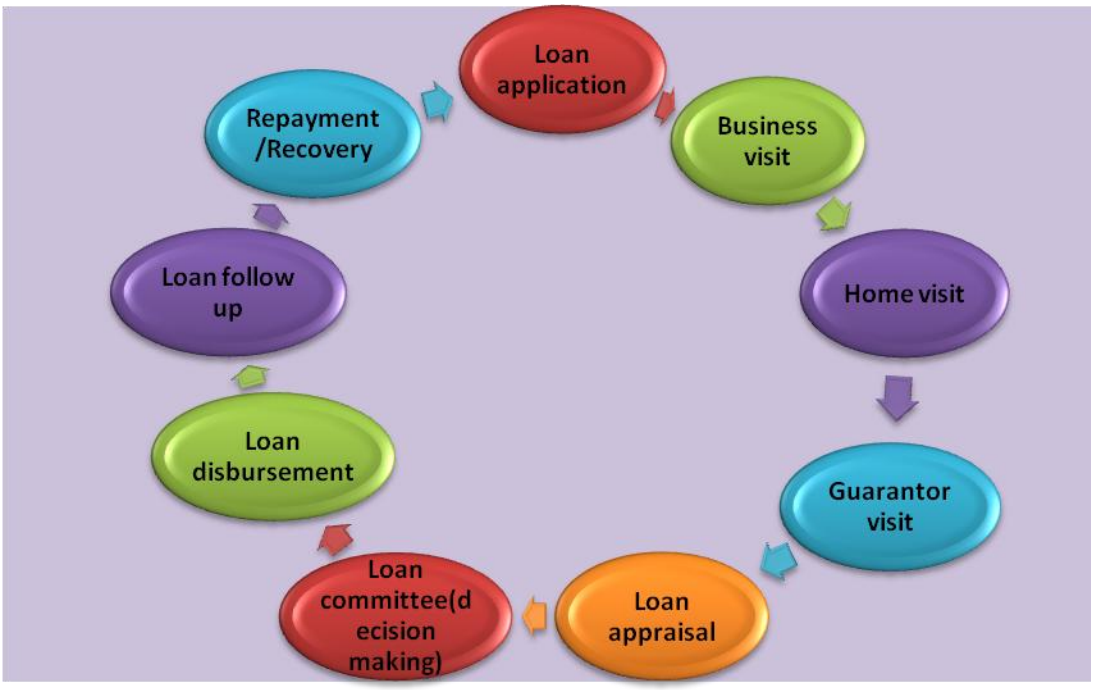
4.8.6 Guarantor's Documents

Guarantor's documents were among the documents required to submit during loan application in Microfinance Institutions. This was mentioned by total of 100 percent of the total respondents. It was a standard procedure required to be fulfilled by most microfinance institutions in order to process a loan request. It was part of risk management resulting from loan defaulting, misbehaving and disappearance of the borrower. These results are consistent with Mugendi,(2009) and Kessy &Urio,(2006) on the conditions and eligibility.

4.9 The Typical Methodologies, Processes and Procedures for Loan Process: FINCA Tanzania Case

The study aimed to determine the typical lending procedures and conditions employed by most microfinance institutions. Several lending procedures and processes were identified to be employed by financial institutions in lending activities. This was done through documentary review at FINCA Tanzania. Review of various documents such as brochures, training modules, work processes, tools, and guides was done by the researcher. It was also done though direct observation conducted by the researcher herself. The results obtained were presented as follows.

Figure 4. 8 FINCA Loan Process Methodologies, Processes and Procedures



(**Source:** Adopted FINCA 2010)

Figure 4.8 represents typical methodologies, processes and procedures for loan process as adopted from FINCA Tanzania. It comprise loan application, business visit at business place, home visit, guarantor visit, loan appraisal, loan committee (decision making), contract signing and loan disbursement, loan monitoring and loan follow up actions, loan repayment /recovery process. Description of the process as obtained from interview and documentation is as hereunder;

4.9.1 Loan Application

The first stage in the loan process was the Loan application, where the client was supposed to visit the branch and submit his identity card, letter of introduction from local government authority, proof of business and two passport size photos. Also he/she was supposed to submit the same documents for the person who intends to be his guarantor. The application forms were completed and submitted the branch manager for the second stage of loan process. The branch manager assigns the file to any of the loan officers for appraisal process.

4.9.2 Business Visit at Business Place

The second stage was the Business visit, where the assigned loan officer makes a surprise visit at the business place to see how the business is doing. Aim of having surprise visit is to avoid any misleading information that may be done by the client to hide some of the realities of his/her business. During the business visit the loan officer records sales, purchases, account receivables and payables, various expenses incurred by the business, and obtaining proof of them by having copies of invoices, sales book etc.

4.9.3 Home Visit

The third stage was the home visit that was made one day after business visit, the aim of home visit was to know the place where the client was residing, his living standard as compared to his income status, and have a look on collaterals and their values. The loan officer prepares the list of assets pledged by the client as collaterals and makes him/her sign with his spouse or her husband.

4.9.4 Guarantor Visit

The next stage was the guarantor visit where the loan officer visit the person who wishes to guarantee the loan of the client to have look on the assets and have an estimations on their values and also obtain the information on the relationship existing between the client and the guarantor, then completes the list of asset and make the guarantor sign.

4.9.5 Loan Appraisal

After the three visits made by the loan officer, he stays in the office to prepare the financial statements by using the information obtained during business visit, home visit and guarantor visit. The loan officer constructs the cash flow statement, the balance sheet and ratios such as liquidity ratios, debt ratio, inventory turnover ratio and receivable ratio. The financial statement analysis generally involves common

size analysis, ratio analysis (liquidity, turnover, profitability, etc.), trend analysis and industry comparative analysis.
This permits the valuation analyst to compare the subject company to other businesses in the same or similar industry, and to discover trends affecting the company and/or the industry over time.

By comparing a company's financial statements in different time periods, the valuation expert can view growth or decline in revenues or expenses, changes in capital structure, or other financial trends. How the subject company compares to the industry will help with the risk assessment and ultimately help determine the discount rate and the selection of market multiples. Then the loan officer completes the loan appraisal form, and the synthesis form. Then he/she books for the loan committee for decision.

4.9.6 Loan Committee (Decision Making)

During the loan committee the loan officer presents the loan application and the appraisal forms to the committee and the committee discuss several items such as the project itself, its profitability, the supply chain, the amount requested versus the repayment capacity of the business obtained from cash flow statement, they also ask various questions on how the loan officer appraised the business, the collaterals used and their values, crosschecking on the documents of ownership of collaterals etc then they reach a conclusion by whether approving the loan amount of postponing for more information or even declining if they were not convinced by the business itself or the loan purpose (project profitability) the client was informed about the decision reached by the loan committee.

4.9.7 Contract Signing and Loan Disbursement

If the loan has been approved then the next stage was the loan disbursement, where the contract was prepared and the client together with his/her guarantor signs the contract together with the banks representative and the loan was disbursed though his account with the bank or being transferred to another account of the client or supplier. A contract was an agreement entered into by two or more parties with the serious intention of creating a legal obligation or obligations, which have elements in writing.

The remedy at law for breach of contract was usually "damages" or monetary compensation. In equity, the remedy can be specific performance of the contract or an injunction. Both remedies award the damaged party the "benefit of the bargain" or expectation damages, which are greater than mere reliance damages, as in promissory estoppels.

4.9.8 Loan Monitoring and Loan Follow Up Actions

After the disbursement the loan officer makes regular follow up on the business to have a look on the use of the loan comparing to the loan purpose, to have a look on how the business is performing and if it was appreciating or it was depreciating. Also to indicate various risks that may be facing the business and therefore advising the client on what measures to take and also the bank on how they can do to make sure that they don’t lose their money. Then the client was required to have monthly installment to repay his/her loan starting from three to twenty four months depending on the loan amount.

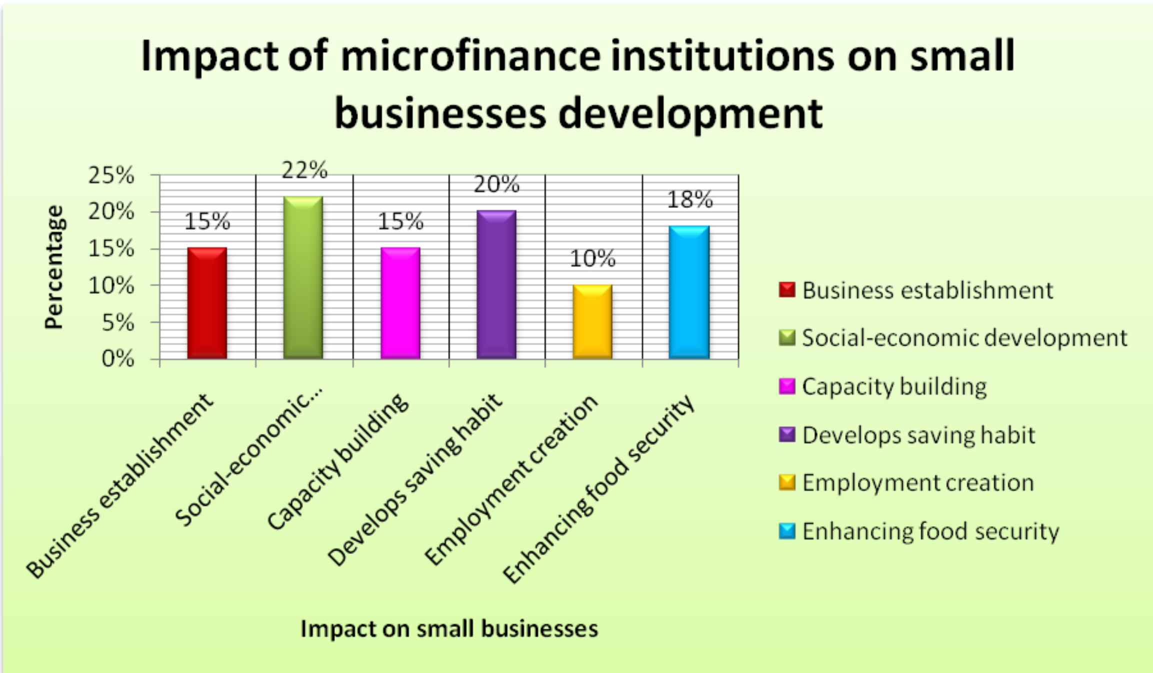
4.9.9 Loan Repayment /Recovery process

The client was supposed to repay his loan monthly on the aniversaly date and if it apperas that the client doesn’t repay his/her loan on time and or delaying for several days/weeks/months then the recovery actions are done by visiting his business place and home place to have a look on what was happening. The loan office will try to recover the loan by providing the past due notice to the client for 14 days, 30 days and then 60 days. If it appears that the cient defaults for more that 90 days then the bank contracts the auctioneers and court brokers to freeze the assets used as collaterals and sell them to recover the money back.

4.10 The Major Impact of Microfinance Institutions to Micro Enterprise Development

One of the objectives of the study was to determine the major impact of microfinance institutions on small enterprise development in Ilala municipality. A total number of 40 small enterprises respondents were involved to respond to the questions through interviews, questionnaires and direct observation conducted by the researcher herself as well as documents with relevant data for the study. The study identified a number of major impacts on micro enterprises development detailed as follows.

Figure 4.9 Impact of microfinance institutions on microenterprises development n=40



Source: Field data, 2013

Figure 4.9 summarized the information obtained during the study as follows;

6 respondents equivalent to 15% of total respondents, said that microfinance institutions influences the establishment of micro-business both in the rural areas and urban areas, the respondents added that this has raised the standard of living for the people in urban areas as well as in rural areas in Tanzania.

Another group of 9 respondents equivalent to 22% of total respondents participated in this study argued that, availability of financial services provided by microfinance institutions leads to economic and social empowerment. The respondents further argued that provision of financial services to all vulnerable groups including women, youth and disabled has helped to elevate their status in society through economic and social empowerment.
Microfinance institutions have enabled the clients to acquire the capacity to build low cost, yet high quality, housing units, and to buy vital household items, and put their children through affordable school system.

Moreover, 6 respondents equivalent to 15% of total respondents participated in this study said that, availability of microfinance institutions has led to capacity building for micro enterprise managers. They argued that some Microfinance Institutions members and staff provide awareness and training on various skills like entrepreneurship and management skills, record keeping, importance of savings, management of micro-projects and basic financial management has contributed to survival and growth of many microenterprises in Tanzania.

The study also found from 8 respondents equivalent to 20% of total respondents participated in this study responded that, the availability of microfinance institutions influence saving habit in the lives of people and discouraging non-productive expenditures among the societies. This contributed to social and economic advancement among people in the society.

4 respondents who was equivalent to 10% of total respondents participated in this study responded that, the availability of microfinance institutions facilitates and influence new employment creation and supporting the survival of small businesses. The participants responded that many urban and rural micro businesses such as restaurants, taxi business, saloons, handicrafts businesses, retail shops and kiosks have been started and developed by the loans taken from microfinance institutions.

Also it was found from 7 respondents equivalent to 18% of total respondents participated in this study that, microfinance institutions are enhancing food security among members of the society and facilitating economic development. The respondents argued that microfinance institutions have enabled members to put some of their loans in agricultural development or processing of agricultural products such as maize, fruits, cassava and others and thereby increasing the productivity in the agricultural sector and enhancing food security in the society.

4.11 Challenges encountered by Small Enterprises in Accessing Loans

Table 4. 8 Challenges Encountered by Small Enterprises in Accessing Loans

n=40

Challenges/problems	Respondents	Percentage
Lack of valid collateral	15	37.5%
Lack of entrepreneurship education	4	10%
High interest rate	10	25%
Long loan process	6	15%
Corruption	5	12.5%
Total	40	100%

Source: Field data, 2013

In responding to a question which aimed at finding out the challenges facing microenterprises in Ilala Municipality in accessing loans from microfinance institutions, most among the 40 respondents involved in the study mentioned issues below as the main challenges facing them. Most respondents admitted that there were several challenges they come across in transacting business with microfinance institutions, among them were;

(i) Lack of valid collateral.

(ii) Lack of entrepreneurship education

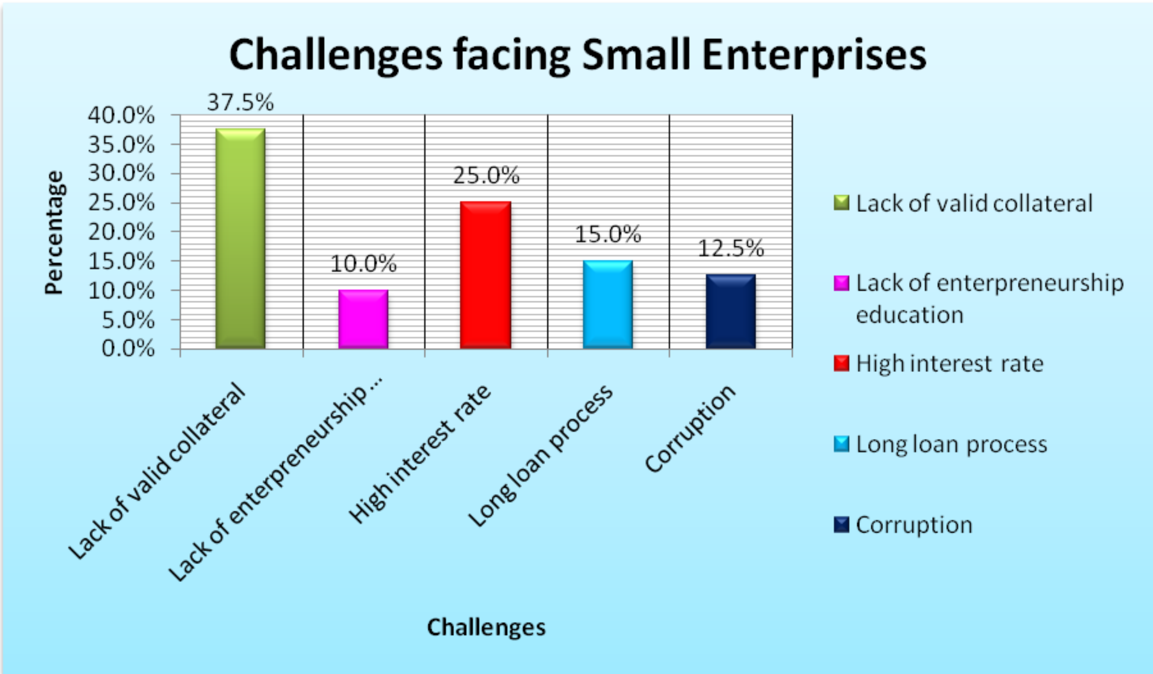
(iii) High interest rate

(iv) Long loan process

(v) Corruption

Mentioned challenges were rated according the frequency of mentions by microenterprises respondents. The summary of this response was presented in the Table 4.8.

Figure 4.10 Challenges facing Small Enterprises in accessing loans n=40



Source: Field data, 2013

Figure 4.10 illustrates the various challenges encountered by small businesses. It can be observed from the list that, 15 microenterprises who represent 37.5% of total respondents said that according to them the main challenge was lack of valid or suitable collateral required for loan application. Valid collateral includes a house with a valid title deed, vehicle registration card, valuable assets, e.t.c

4 respondents who represent 10% of total respondents stated that, according to them lack of entrepreneurship education/knowledge was the main challenge facing microenterprises in the attempt to grow the businesses. Loans secured from microfinance institutions sometimes not invested into intended business or not well managed in terms of expenditure. When loan funds were misused or misallocated it

becomes a problem when repayment was required, therefore loans becomes a burden to microenterprises instead of helping them to grow they pull back the business.

10 respondents who represent 25% of total respondents stated that, according to them high interest rate was the main challenge facing microenterprises.
The respondents argued that, rate of interest charged was high compared to expected increase in profit of the business on monthly bases. This was one of the reasons why many small businesses fear to look for loans from microfinance institutions for expanding their businesses as they find it difficult to repay the loan which was with high interest rate.

6 respondents who represent 15% of total respondents stated that, according to them long loan process was the main challenge facing microenterprises. They argued that before loan was disbursed it goes through long process which involves a number of visits and documentation. What was required to be submitted by small business (client) for loan consideration was normally fulfilled within a short time but it then takes a long time for the microfinance institution to decide to issue the loan. This long process sometimes distorted the investment plan or loan expenditure plan as a decision to take a loan was done for a reason with some expenditure to be met by using the loan. When the loan was delayed it can lead to misallocation of loan funds and make it difficult to repay the loan.

5 respondents who represent 12.5% of total respondents stated that according to them, corruption/bribe requested by some micro institution officers was the main challenge facing microenterprises. They further explained that some officers ask to be promised a certain amount or percentage of the loan amount in order to either process the loan or issue the loan immediately. This was a problem as it adds to repayment load as an extra loan cost.

CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Summary of findings

Generally it has been observed that to a great extent MFIs have contributed to the development of small enterprises. MFIs' clients have increased their incomes, increased the capital invested and therefore expanded their businesses.

The main objective of the study was to assess the contribution of Micro Finance Institutions (MFIs) on development of small enterprises in Ilala municipality. The study rely on the thinking that lack of sufficient services from MFIs to SMEs has been a serious obstacle to acceleration of microenterprises growth. The findings of the study have revealed that MFIs services offered to their clients have an impact on establishment of micro-businesses both in rural areas and urban areas, economic and social empowerment through raising the standard of living and poverty reduction, capacity building for micro enterprises owners, saving habit in the lives of people and discouraging non-productive expenditures among the societies, new employment creation and supporting the survival of small businesses and enhancing food security among members of the society hence improving livelihood.

Furthermore, findings have revealed that small and medium businesses are dominated by people with low level of education, therefore; Loans should be accompanied with provision of simple entrepreneurship education to small businesses. This would imply the need for capacity building and administrative assistance to small businesses besides financial loans.

The findings also have revealed that Microfinance Institutions' clients encounter problems of short repayment period, lack of entrepreneurship education and long loan process. However lack of valid collateral and high interest rates were the main challenges discovered to hinder small enterprises growth.

5.2 Conclusion

The findings revealed that microfinance institutions were the options and self-confidence of small businesses by contributing to their expansion and diversification of their businesses. They also helped small businesses to decrease risks, increase profit, store their excess liquidity, obtain returns on their savings, and to conduct their businesses with dignity. The standard of living also improves in terms of education, housing, health. In addition, the economic activities often create jobs for others; among those who gain employment in this way are some of the extreme poor.

On the other hand it was found that, microfinance institutions have direct impact on the poverty reduction, by widening access to the poor. They impact by mobilizing savings for investment, facilitate and encourage flow of capital and optimize the allocation of capital between competing uses. Generally, there was a need to create favorable environment for attracting more establishments of Micro Finance Institutions for sustainable economic development in the poor communities.

The researcher also concludes that the overall available mechanisms of micro financing services have a significant contribution in the development of Small enterprises. However, there are many setbacks facing microfinance institutions in their endeavor of service provisions to micro entrepreneurs. They include, inter alia, lack of appropriate knowledge and skills of basic financial management among small enterprises owners, limited access to relevant information on borrower history and, high levels of defaults and delinquencies. There were also some other issues such as, failure of the regulation and policy framework to support the micro lending provision; inadequate and inefficient infrastructural facilities which tend to increase costs of microfinance provision and lack of awareness of micro lending services among the small business owners.

5.3 Recommendations

To remedy the situation mentioned above, the microfinance institutions, government authority, small enterprises owners and financial and economic professionals have roles to play. The following roles are recommended to these stakeholders to enhance the contribution of MFIs in development of Small enterprises in Tanzania.

5.3.1 On the knowledge of Small Enterprises owners

Management training, entrepreneurship, bookkeeping and business planning was very important for any business. It is a mirror for a company to know how business of the company was, how cash situation of the company is, which area the company should improve and which one the company should reconsider if there is no management training on bookkeeping and business planning. Therefore there is a need to have a person who has a background on economics/ accounting or experience on that field to hold bookkeeping activities. In some case, for the manager who does not have an economic/accounting background but he/ she wants to hold all bookkeeping of his/ her company by herself, in this the manager should then attend training courses in accounting and business management.

5.3.2 On the Policies of Micro-Finance Institutions

Renovating the policies on financial and credit is needed. The policies on finance and credit for microenterprises need to be focused on the following issues. Firstly, Small enterprises should be treated equally with State Owned Enterprises when borrowing from the banks. In order for the enterprise to be relieved for difficulties in access to capital and for the banks to secure funds for lending, the banks need to take effective measures against risk. This can be carried out by constructing the database about the current and potential customers and by strengthening the accounting and auditing system with updated information.

Secondly, the procedure on credit should be reformed as follows. The local authorities should be responsible for evaluating the value of production areas and real estate of enterprises so that these assets can be used as collateral for bank loans. The financial transaction of enterprises should be carried on through the banks so that the financial of enterprises can be monitored exactly.

State commercial banks should be active in seeking SME's customers. In addition, banks and financial institution should improve their activities, consider the possibility of forming a lobby group for educating the prospective borrowers, and advise the government on the regulation and policy issues that could be necessary for the wide increase of the microfinance access.

5.3.3 On Support from the Government to Entrepreneurs

The government needs to emphasize on entrepreneurship education and training to microenterprises groups. This will help them in making profitable investment decision and avoid risk of failing to repay loan due to poor loan funds allocation and expenditure.

The government through its body that regulates microfinance institutions should find ways to reduce and regulate interest rate charged to microenterprises so that they become favorable.

The economic integration and co-operation between State Owned Enterprises and Non State Enterprises (Public Private Partnership) should be strengthened extensively to take advantage of each participant, for example, by utilizing idle production capabilities of SOEs: Industrial zones should be constructed to attract the domestic and foreign investors.

Government bodies that are concerned with Small enterprises development like TCCIA, CTI, SIDO and other trade associations can consider training and consulting on the following supporting activities;

(i) Supplying financial sources and market information.
(ii) Offer free-of-charge or low-cost short courses to SME's to prove management, financial skill.

5.4 Suggestion for further study

This study concentrated much in finding out the contribution of microfinance institutions on development of small enterprises.

Findings from the study came up with main challenges facing small enterprises. Since the main challenges have been identified, area for further study should be on solutions to encounter these challenges. Further studies should be on how to improve SMEs technical capacity through vocational training centres and the role of entrepreneurship education towards improving small enterprises competitive capability in the market they are operating. Findings which could be obtained from the later suggested studies can help coming up with ways/solutions to further improve small enterprises development and growth.

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APPENDICES

APPENDIX I:

Questionnaire Microfinance Institution Officers and some Government Officials in the Area.

1. Position…………………………………………………………….
   Gender…………………………………………………………...
   Age……………………………………………………………

2. What kind of services is provided to Micro enterprises?

…………………………………………………………………………………
……………………………………………………………………………..………

3. What are the conditions that Microfinance institutions use to provide loan to micro entrepreneurs?

a) …………………………
b) …………………………….
c) ……………………………….
d) ……………………………….

4. What are the documents required to apply for loan in Microfinance institution?

a)………………………………………………………………………………
b)………………………………………………………………………………
c)………………………………………………………………………………
d)………………………………………………………………………………

APPENDIX II:

INTERVIEW FOR MICRO ENTREPRENEURS

1. Gender ………………………………………………………………..
   Age ………………………………………………………………………
   Education level………………………………………………………..

2. What kind of business did you operate?

...……………………………………………………………………………………

3. Do you have financial knowledge to operate your business?

(i) Yes

(ii) No

4. What are the conditions that Microfinance institutions use to provide loan to micro entrepreneurs?

a) …………………………….

b)…………………………..

c)………………………………….

d) …………………………………..

5. What are the documents required to apply for loan in Microfinance institution?

a)……………………………………………………………………………………

b)……………………………………………………………………………………

c)……………………………………………………………………………………

d)……………………………………………………………………………………

6. In you are opinion what are the major impact of Microfinance Institutions to Micro Enterprise Development?

a)……………………………………………………………………………………

b)……………………………………………………………………………………

c)……………………………………………………………………………………

d)……………………………………………………………………………………

7. What are the challenges facing Small Enterprises in Accessing Loans?

a)……………………………………………………………………………………

b)……………………………………………………………………………………

c)……………………………………………………………………………………

d)……………………………………………………………………………………