

**THE IMPACT OF RURAL FINANCING ON THE PERFORMANCE OF SMALL
AND MEDIUM ENTERPRISES: A CASE OF MUFINDI COMMUNITY BANK**

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**A RESEARCH PAPER SUBMITTED IN PARTIAL FULFILMENT OF THE
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ABSTRACT

The importance of small and medium enterprises sector has necessitated to the great emphasis on small and medium enterprises financing for the development of the sector. However, with the current small and medium finance institution in Tanzania, there is no sufficient documentation of the extent and strength of small and medium enterprises performance as a result of accessing credit from MFIs. The study thus aimed at evaluating the performance of SMEs a result of provision of credit from MuCoBa in Mufindi. Primary data were collected using questionnaires from selected samples of 45 small and medium respondents. Borrowers and institution respondent were interviewed f. Secondary data were collected from the university of Sokoine libraries and MuCoBa. Descriptive statistic (means, percentages, frequencies) were major tools employed in data analysis. Small and medium enterprises financing was confirmed to play a vital role in boosting sales revenues, Enterprises with access to credit employed significantly more laborers than those without credit. Many borrowers respondent (68.9 %) reported to acquire more assets than non-borrowers (13.3 %). Also micro enterprises with credit have higher ability to meet their basic needs and other household's expenses like paying school fees, meeting medical etc. Hence, SMEs financing has a major role for starting and sustainable growth of profitable enterprises for the development of SME sector. The study recommended that proper measures such as creation of favorable environment for SME sector, conducting of feasibility study to SMEs before issuing credit to SMEs, extending credit for business start-up, provision of grace period to SMEs after loan disbursement, extension of repayment period, provision of entrepreneurship skills and business training for SMEs operators and increasing the size of the base loan.

DECLARATION

I, GODFREY GODWIN, do hereby declare to the SENATE of the Sokoine University of Agriculture that this research paper is my original work and that it has never been submitted for a degree in any other University.

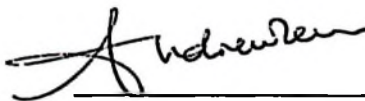


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DEDICATION

To my lovely mother Leah Jacob Mpogole who sacrificed a lot towards my education.

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LIST OF ABBREVIATIONS

GDP	Gross Domestic product
ILO	International Labour Organization
LIC	Low Income Countries
MEs	Micro Enterprises
MFIs	Micro-Financial Institutions
NGO	Non Governmental Organization
MP	Member of Parliament
PTF	Presidential Trust Fund
SEDA	Small Enterprise Development Agency
SMEs	Small and Medium Enterprises
UNCTAD	United National Secretariat for Development
URT	United Republic Of Tanzania
PRIDE	Promotion for Rural Initiatives Development Enterprises
MET	Mufindi Education Trust
MuCoBa	Mufindi Community Bank
SACCOS	Savings and credit cooperative society
GSS	Ghana Statistical Services
ESRF	Economic and social research foundation
SHO	Self-help organizations
SPSS	Statistical Package for Social sciences
TZS	Tanzanian shilling

CHAPTER ONE

1.0 INTRODUCTION

1.1 Background on Rural Financing

Access to credit in rural sectors of developing countries is critically low. A majority of the financial institutions in these areas are conservative, relying on heavy asset and collateral-based requirements to induce them to invest locally. They are reticent to lend to potentially risky smaller enterprises and especially to sectors where they have little or no lending experience.

As a result, the growth of financial markets in rural areas has been slow, challenged also by the cyclical nature of business, volatility of weather conditions, and perceived lack of investment options. In the absence of viable local opportunities, many of these countries are net exporters of capital, to avoid currency devaluation. The portion of private capital that remains in-country is predominantly held “under the mattress” or in banks that only lend to large customers with significant assets as collateral. Cash deposits with these banks are often put into government securities to avoid market volatility and the risk of currency devaluation. These investments decrease the liquidity in the banking community and therefore diminish funds available for lending.

1.1.1 The Challenge – Limited Access to Capital

In the rural sector, a significant amount of the credit available for lending has been supplied and subsidized by donor programs and donor-created funds. But increasingly, these funds are competing with local private financial intermediaries which cannot afford to offer the same rates.

Understandably, the resulting imbalance has unfairly skewed the growth of these local financial institutions and is contrary to the principles of sustainable development. Although the demand for financing is strong, the rural sector remains underserved. When funding is made available, the typical commercial bank has collateral requirements of 100-200 percent of the value of the loan, a cost far too high for most borrowers. Creditworthy private farmers and small agribusinesses have difficulty meeting such conditions and often lack the long-term operational or repayment track records they should have to establish their credibility as borrowers. Consequently, financial institutions continue to prefer established lending activity and business relationships, while small rural businesses have very limited, if any, access to financing for critical improvements to their operations.

Financial institutions have little motivation to reduce the requirements for securing such a loan; therefore, educating local financial markets is crucial to lowering their sensitivity to risk. Unless lending institutions are provided the training and technical assistance to find bankable loans in the rural sector, only established areas and business entities will receive financing. Donor capital will continue to be the principle source of that credit until local capital can be mobilized for local investment at market rates. Since development credit will always be limited, the supply of funds will always fall short of demand.

1.2 Mufindi community bank

Financial assistance in Mufindi is obtained from different Non-governmental organization, the National micro finance bank but the major source of capital to rural people businessmen or farmers is Mufindi Community Bank (Mucoba).

Mufindi community bank was formed in 1998 after the increase demand of for financial services in the area. The original of the bank is linked to that of Mufindi Education Trust (MET), which was formed with a grant from a Belgian NGO promoting secondary education in Mufindi district, ACT. In 1996, MET formed INCOMET LDT FUND to coordinate income generating activities which included; tile industry, chalk production, seed farm, garage, fill factories and carpentry. INCOMET also provided financial support (credits/loans) to workers of MET and INCOMET and later to parents of MET students. On 30th December 1998 INCOMET was incorporated under companies' ordinance (cap 212) with a registration number of 35471, and on 11th may 1999 licensed by Bank of Tanzania (BOT) as the first community bank in Tanzania with a registration number of MFI A 00001, and the bank started its operation on 01st June 1999. The first Chairman of the board of the bank is Hon. J.J Mungai (MP) who is one of the first shareholders of Mucoba.

1.2.1 Mission of MuCoBa

MuCoBa wants to be a leading provider of bank services, providing employment to the society and building capacity to its shareholders and customers therefore improving their lives in and outside Mufindi.

1.2.2 Vision of MuCoBa

MuCoBa wants to be the best community bank in Tanzania leading in profit generation and high quality services to its customers and shareholders.

1.2.3 Shareholders

MuCoBa has several shareholders. The bank started with a capital investment of Tshs 50 millions, now the bank has a capital of Tshs 100 millions. The distribution of shares is as

follows; Mufindi Education Trust (MET) 60%, other development organizations 20%, Mufindi district council 10%, SACCOS 7.5% and Individual shareholders 2.5%. To increase its capital and customers goodwill, the bank plans to open windows and sell some of its shares to other individual customers in the near future.

1.2.4 Services offered

MuCoBa offers two kinds of services, namely

- Deposit services
- Credit/Loan services
- Deposit services
- MuCoBa offers two types of deposits, and these are saving and fixed deposits.

1.2.4.1 Saving deposit

This requires a minimum initial cost of ten thousands (10 000/=) where 5 000/= is for administration cost for opening and running the account and other 5 000/= as the minimum saving of the customer. The interest rate for this saving is 4% per annum.

1.2.4.2 Fixed deposit

Fixed deposit gives the customer maximum interest for a fixed time of 3 months, 6 months, 9 months or 12 months. The minimum amount for opening the account is Tshs 50 000/= with different interest rates depending on the amount of money. But it ranges from 4% to 10%.

1.2.4.3 Increase of customer's deposits

Customer's deposits and customers themselves have been increasing from year to year. When the bank started its operation in 1999 had only 323 customers with deposits of Tshs 107.5 millions. Customers increased to 4 821 with deposits of 1.035 billions Tshs in July 2004.

1.2.5 Credit/loan services

1.2.5.1 Individual business loan

The aim of these loans is to help small and medium business people to develop their economic activities therefore improving their living standards in Mufindi district and the whole nation in general. The duration of this loan between 3 to 18 months. The loaner must have a MuCoBa account, must have at least a one year experience on the same business, the loaner must also have a collateral (Fore example a house, farms, machine, cars e.t.c). The minimum amount to loan is 500,000/= and the highest amount is 20 000 000/=

1.2.5.2 Employee's loans

These types of loans are given to employees from Government and non government organization, where their employees guarantee them. The aim of these loans is to help employees from different organizations to tackle their social and economic problem. The loan payment will be from their monthly salaries.

1.2.5.3 Group loans

This involves a group of 20 – 40 people, where in the main group small groups of 5 – 7 people are formed. These small groups will guarantee themselves. Before receiving a loan each group member must open a Saving Account and he/she will get three (3) times the

saving amount as a loan. The aims of these loans are to help small low-income earners to get cash to run their economic activities. Also it helps people who does not have collateral since in this case will use their savings and their group union as collateral.

1.2.5.4 Loans to SACCOS

The main purpose is to provide loans to more community member by using Savings and Credit Cooperative Societies (SACCOS) so as to reduce costs of reaching individual clients as well as motivating SACCOS in using financial services for their development. Under this system, MUCOBA issues loans to SACCOS and SACCOS give loans to their respective members according to their needs. The loan size range from Tshs 1,000,000/- to Tshs 10,000,000/=. The repayments are in installments (monthly) but with specific project the repayment amounts and installments are negotiable.

1.3 Problem statement

Millions of people in rural Tanzania areas are poor not because they cannot manage money, but because they have too little of it. While studies show that rural micro-entrepreneurs produce high rates of return on the capital they invest, the problem is they lack access to sufficient funds, which means their aggregate return remains low, thus perpetuating a life in poverty.

A key objective of rural finance is to provide those people with the funds and financial services they need to multiply their earnings and build a more prosperous future. The future of rural poverty alleviation is investment in all aspects of rural development, not only agriculture. More business in rural areas generates the economic incentive to improve infrastructure, which boosts the competitiveness of production. But development can only

occur when a rural area is able to attract and sustain rural investment, through a conducive operating environment, suitable financial products and services, and attractive returns. The provision of credit to the poor is supposed to be a leading component of many of all financing institution because the lack of access to productive capital is thought to be one of the main factors preventing the poor from breaking away from the "poverty trap." This trap, it is argued, makes it extremely difficult for the poor to overcome poverty without outside intervention. In its simplest form, this trap can be viewed in terms of the poor person's low capacity to generate income, savings, and investment in the economic environment

1.4 Justification of the study

The evidence on the role of rural financing in small and medium enterprises performance will offer insight into the organizational features conducive to the sustainable supply of financial services. The findings will also generate useful information for the entrepreneurs to realize their enterprises performance and potential contribution to the national economy. Also the study will provide recommendation on how to improve small and medium enterprises sector.

1.5 Objectives of the study

1.5.1 General Objective

Economic Analysis of rural financing to small and medium enterprises in Mufindi District.

1.5.2 Specific Objectives

- To study the effect of rural financing to small and medium enterprises and accessibility barriers.

- To examine whether a microenterpreneur can meet his/her personal needs and other needs as a result of participating in rural financing programmes.
- To evaluate whether microenterpreneur assets accumulates as a result of participating in rural financing programme.

1.6 Research questions

- Are there any barriers in accessing rural finance to small and medium enterprises in Mufindi district?
- Is there any relationship between participating in rural financing and;
 - (a) Assets accumulation in terms of ownership of productive assets
 - (b) Possession of cash in hand
 - (c) Reinvesting in current business or starting a new business
- Is there any relationship between small and medium enterprises participation in credit programme and microenterpreneur ability to meet basic needs and other household's needs?

CHAPTER TWO

2.0 LITERATURE REVIEW

This chapter reviews the literature on different issues in respect of the study.

2.1 Definition of Micro Enterprises

The definition of Small and medium sized enterprises varies from country to country and from time to time. The definitions use various measures of size depending on the purpose, and the person doing the measuring. Some of the yardsticks that have commonly been used are total number of employee, total investments and sales turnover. (Rutashobya and Olomi, 1999) In Tanzania most small and medium sized enterprises are normally family business or self-employed person operating in the semi formal and informal sectors. Most of them fight very hard accessing bank finance or becoming internationally competitive. Serving them requires distinct institutions where the institution bares a very high risk in giving those credits or loans.

Small scale enterprises have been defined by Ghana Statistical Services (GSS) as those that employ less than 10 employees as medium or large scale enterprises (Sowa et al., 1992). In Tanzanian context, Small enterprises are defined as those units with capital investment in plant and machinery from 5.1 millions to 200 millions Tanzanian Shillings and where the number of employees does not exceed 50 (ESRF, 1996) with a turnover of not more than 150 million per annum.

Medium sized enterprises are defined as those businesses with capital investments in plan, machinery or goods from 201 million to 800 millions Tanzanian shillings and where the

number of employees does not exceed 100, with a year turnover of 300 million Tanzania shillings.

In this study the definition of the Ministry is adopted.

Table 1: Micro enterprises definition as per SME development policy

Category	Employees	Capital Investment (Million TSh)	Turnover (Million TSh)
Micro enterprises	1 – 4	Up to 5.0	12.0
Small enterprises	5 – 50	5.1 – 200.0	150.0
Medium enterprises	51 – 100	201.0 – 800.0	300.0
Large enterprises	101+	Above 800.0	300.0+

Source: Ministry of Industry and Trade SME Development Policy 2002.

2.2 The role and function of small and medium Enterprises.

Small and medium enterprises should be supported because they contributed to economic development. They also increase employment, as they are usually more labour intensive (after micro enterprises) implying that they reduce poverty and contribute to fairer income generation.

2.2.1 Contributions of Small and Medium enterprises on employment

One of the most pressing challenges facing policy makers in sub-Saharan Africa today is unemployment. The growth of the labor force, primarily as a result of population growth, far surpasses the number of new opening in large enterprises while in many countries the growth in employment in the public sector has been sharply restricted, partly as a result of structural adjustment programs. Some of the new entrants to the labour force have found work in agriculture either on their own farm or as paid workers. The absorptive capacity

of agriculture sector in many countries of this region is, however, limited in a number of countries. Then, a substantial number of new job seekers have turned to small and medium enterprises as a source of live hood (Mead, 1994).

Small and medium enterprises are pervasive features of the landscape in all low-income countries. According to the research findings in the study of the contribution of small and medium enterprises to employment growth in Southern and Eastern Africa, it has been found that small enterprises have absorbed close to a third of the total increase in population of working age (18 – 64) and over 40% of the total increase in the labour force during 1980s (Mead, 1994).

In Tanzania mainland, the 1990/1991 labour force surveys indicated also that about 21% of the labour forces were employed in small and micro business.

2.2.2 Contribution of Small and Medium enterprises on income, welfare and *GDP*

Small enterprises are important source of live hood for many people in the low-income countries (Nyagori, 1995). A substantial literature discusses the development of small and medium enterprises and the most appropriate ways to assist them to raise income for the poor. Government and donor agencies are funding an increased interest in private firm, a belated recognition that many individuals make their live hood from small business (Webster, 1989) In Tanzania, the majority of urban poor, the middle and high-income urban and rural working classes supplement their income from SME sector. It was observed that some years ago, wages of an ordinary worker in Tanzania were enough to support the family of the worker and other relatives. In recent years (1990's) most of such workers cannot sustain their life using wages alone. Kashuliza, *et al.* (1998) noted that

these workers are forced to engage in other income generating activities as a survival strategy. The study carried out in Kenya by Daniels and Mead (1998) showed that small and micro enterprises were found to generate 12 – 14% of the national income of the country.

The contribution of an enterprise to the GDP can be measured in terms of the payments made to factors of production employed in the enterprises, rental payments for land, interest on capital invested, wage payments for labour and profit earned by the owner of the enterprise. This implies that the contribution may be in both qualitative and quantitative terms. In the qualitative sense the sector offers basic goods and services, which are cheap and easily accessible to the most low-income earners (Bagachwa, 1991).

2.2.3 Contribution of SMEs to well being among women

In many countries at all levels of development, women's access for the labour market is consistently more difficult than men's. Employment opportunities are often denied to women because of their family responsibilities, lack of skills, and social and cultural barriers. Mgina (1992) observed that micro enterprises provide employment to women most of whom have low education and hence cannot be employed in the formal sector. Self-employment in the micro-enterprises may thus, constitute the only possibilities for women to get access to employment and to earn an income. This is because the private sector is more taking precedence over the public sector in term of employment creation. An increasing number of women have come to realize this and have launched some kind of economic activity.

In Tanzania it was observed that women's access to wage and salary employment is small, about 20% of total. They are also concentrated in less skilled low salary position (Bureau of Statistics, 1995). Adding to that they have been among those formal sector workers most affected by public services retrenchment policy. However, they account for over 35% of natural informal sector employment, rising to almost 42% in urban areas. In Tanzania mainland women accounted for over 34% while Zanzibar were over 50% of the total informal sector entrepreneurs (Bureau of Statistics, 1995). It is argued that the rationale for supporting the development of women headed small and medium enterprises is two folds. First, it contributes to poverty alleviation. Second, it contributes to women's economic and social empowerment (ILO, 2000).

2.3 Types of Small and medium Enterprise

Activities within the informal sector vary considerably; however, depending on the location, service type enterprises predominate, while manufacturing are few. These include, local brewer, food/beverage and tobacco, wearing and apparel; textile /leather, wood products, manufacturing and wholesale. Other include, retail agricultural produce, retail fuel and charcoal, retail hardware, retail ready made garments, retail secondhand garments, general kiosk, retail shoe /leather goods, processed food sales, bars /restaurant and hotels, beauty saloon and all other services. Some are involved in agriculture, animal keeping, bakeries, tailoring, food vending, and carpentry, among others that produce income.

2.4 Credit and Small and medium Enterprises

2.4.1 Meaning of credit.

Literally credit means money lent with an interest for profit. However, others define credit as a transaction between two parties in which one party supplies money, good, service or securities in return for promised future payment. Such transaction normally includes payment of interest to the lender (Labie, 2003) and that interest rate will be paid as some sort of rent use or price of borrowing money (Berthold, 1996). The credit impact under NGO perspective is generally perceived as a supply of money input by donor institution to the project executing agencies or NGO. Then the latter may pass some of it to the target group in the form of loans, enabling them to finance development activities over a set of time and repay the loan with interest (Berthold, 1996). Usually the lender must judge each loan he/she makes on the basis of character of the borrower, capacity to repay and collateral.

2.4.2 Sources of credit/finances for SMEs

There are several sources of credit or financial services to micro enterprises. These can be grouped as formal, semi-and informal sources.

2.4.2.1 Formal sources

Formal sources are constituted by formal financial institutions. These institutions both private as well as public are characterized as being regulated by central bank authorities. These authorities decided on what kind of services the institutions are allowed to provide (Chijoriga and Cassimon, 1999). The mode of operation of formal financial institutions often lead to high borrower transaction costs which poor people may find prohibitive.

Together with other problems, transactions costs may exceed the interest on the loan (Nikos, 1997).

2.4.2.2 Semi-formal sources

Semi formal sources are financial institutions that are not subject to formal banking laws and the central bank supervision. They are also not like the traditional indigenous financial institutions. These include self-help organizations (SHO), for example, savings and credit Associations, Parastatal, government and non-governmental organizations (NGOs), such as different micro finance organization with credit components. These semi formal financial institutions mainly focus on the income generating activities for youth and women who are the most disadvantaged groups in poor societies (Dichter, 1999). Disregarding their internal deference, the majority of them are basing on Savings (Sumay, 1999). There are some successful examples of semi formal institutions, for examples, Banco Agricola based in Latin America, Action Aid, UAVEC in Bukinafaso and LCCUL in Lesotho (Berthold, 1996) while in Tanzania there are Oxfam, PRIDE Tanzania, SEDA, PTF and many others (Sumay, 1999).

2.4.2.3 Informal sources

Informal sources of informal financial institution on the other hand refer to all transaction, loans and deposit occurring outside the regulations of a central monetary and supervisory organ (Chijoriga and Cassimon, 1999). The sources are also considered by Levitsky (2000) as financial markets that include mutual support group, and individual brokers (money lenders, pawnbroker etc). The emerging view about informal lenders from studies conducted in the 1980s in a numbers of LICs is that, they generally perform legitimate economic functions in the rural financial markets. Their operations also are frequently

more cost effective and useful for the poor than those of formal credit commercial banks. In most cases, collateral and repayment conditions are flexible which an advantage is for those without collateral but with high interest rates rising to 100% a month (Levitstky, 2000). However, the repayments remain high because of the nature of the finance and credit transactions, which are largely conducted on the bases of the trust, and intimate knowledge of customers (Bagachwa, 1991).

2.5 The role of Micro Financing on SMEs performance

Finance has been identified as the most important factor determining performance of SMEs in both developing and developed countries. Access to finance allows SMEs to undertake productive investments to expand their businesses and acquire the latest technologies, thus ensuring their competitiveness and that of the nation as whole. Poor financing of SMEs can seriously undermine the microeconomic fundamentals of the country, resulting in lower growth in income and employment (UNCTAD, 2000).

The performance of SMEs can be catalyzed through the timely availability of credit. Timely availability of credit can add value to the success of SMEs provided they have a potential competitive advantage and operate in an enabling environment not distorted by uneconomical fiscal, regulatory, and exchange rate policies (Narasimham, 2001). The provision of finance to SMEs offer an opportunity to manage scarce resources more efficiently, protect them against risks, allow them to save for the future and unforeseen contingencies, give them chances of taking advantage of investment opportunities, and for economic returns (Buckley, 1997).

CHAPTER THREE

3.0 RESEARCH METHODOLOGY

3.1 Overview

The study was carried out in Mufindi district, Iringa region from June 26th to December 22nd 2006. The research station was chosen because it has the oldest community bank in Tanzania and a variety of economic activities. The researcher's familiarity with the district made client's accessibility and data collection processes easier.

Mufindi is one of the seven administrative districts of Iringa region, located in the southern highlands of Tanzania. The district capital is Mafinga, the total area of Mufindi is 7123 square kilometers and comprises of 126 official villages. In total, the district has a population of about 320,000 individuals. It is a typical district whose rural population are peasant households. The main opportunities and economic activities in which small and medium entrepreneurs include agricultural activities, forest products like timber, carving. Other economic activities in which people can engage in and acquire credits include wholesales and retailers, hotel, bar and restaurants, food processing like fruit, grain milling and oil crushing, livestock sector and construction.

The major focus of this chapter was on research design, nature and sources of data, sample size, data collection method, data collection instruments, interviewing technique, sampling design and sampling procedures, data management, study variables, data analysis, hypotheses testing and expected results.

3.2 Research design

A case study design was adopted for the study to focus the contribution of rural financing on the performance of small and medium enterprises. The purpose of the case study design was to obtain information on several variables from within a single administrative unit. In this case, MUCOBA was chosen as a case study.

Due to limited funds and time on sampling frame, the researcher had no other suitable design than a case study. Hence the case study design was preferable in obtaining viable and reliable data from various sources. Both descriptive and analytical approaches were applied. The descriptive part of the study dealt with explaining the general aspects related to small and medium entrepreneur under study and the institution offering micro financing services. Descriptions of the experienced impacts as a result of getting micro finance were also covered. The analytical aspect dealt with the analysis of the effect of participation on the performance of small and medium enterprises on their level of sales revenues, number of employees, the ability to meet personal and other household's needs and accumulations of assets.

3.2.1 Unity of Inquiry

This is an element or aggregation of elements from which information is collected. And an element is that unit about which information is collected and which provides the basis or analysis. In this study unit enquiry included one selected community bank, which is MUCOBA. From this unit of inquiry an element was being established. The elements are the individuals whom are stakeholders of this bank. These are clients and management staffs. MUCOBA as a study population is chosen out of these institutions. There are more

than 50,000 clients who have access and get services from this institution. Majority of clients are located in Mufindi district.

3.2.2 Nature and source of data

Data were collected from both primary and secondary sources. Primary data was collected from Mufindi Community Bank and its clients. Those who received loans (Borrowers) interviewed during repayment meetings. Loan applicants (non borrowers) were interviewed during training sessions conducted by credit officers prior to loan disbursement. Secondary data was obtained from documents of Mufindi Community Bank.

3.3 Data collection

Primary data were collected by using 45 structured questionnaires (closed ended) and group discussion. Secondary data were obtained from various sources including books, journal and Internet. Data which were used are those that assisted in defining relationship that exist between rural financing and SMEs performance as result of financing.

3.3.1 Interviewing techniques

Questionnaires were used as personal contact so as to avoid non-responses for those who could not spare their time and for those who are not used to questionnaire filling. Structured and unstructured interviews were conducted to a sample of MUCOBA officials and clients. In this case, the researcher asked various questions in a sequential order, and respondents had a chance to present their views freely.

3.4 Sampling design and sampling procedures

The general framework for sampling is both non probabilistic and realistic. In this case borrowers and non borrowers (loan applicants) respondents were randomly identified at the bank. The studied population consists of one institution. The sample was taken from groups mentioned in 3.2.1 above. Judgment and convenience sampling techniques will be used to select sample from clients and staffs of the bank management. That is, selection will depend on the availability and willingness to co-operate and provide information they have. These sampling techniques have been chosen because of cost effectiveness and representativeness.

3.5 Data management

Each questionnaire were inspected, and where necessary, corrected for the purpose of detecting error and cleaning data before they were keyed in the computer for analysis: i.e. at the field and in the office. The field edit assisted to decide on how data collection instruments containing incomplete answers, obvious wrong answers, and answer that reflect lack of interest, have to be handled.

3.6 Study variables

3.6.1 Dependent variables

According to Brush (1992), research that includes a consideration of organization performance must address the issue of selection of conceptual framework from which to define performance. Some years back Buckley (1968) included a consideration of effectiveness with respect to various constitutes of organization i.e. cash management, liquidity, profit, sales turnover, growth, survival, market share etc. For the purpose of this study, performance is defined as the increases in revenues, quality and number of

employees, assets accumulations, and the ability of the entrepreneurs to meet his/her household needs and other needs e.g. paying school fees, meeting medical expenses etc.

3.6.2 Independent variables

Participation in Small and medium financing program were used as an independent variable. The performances of small and medium enterprises will be compared depending on whether SME owners participate or do not participate in rural financing program.

3.7 Field work execution

The field exercise, involved distribution of questionnaires, interview and collection of secondary data. Questionnaires were randomly distributed to MuCoBa customers and some MuCoBa officials who have taken loans. Questionnaires were distributed to MuCoBa customers for the aim of collecting data relating to the performance of their enterprises and compare the performances between borrowers and non-borrowers SME owners. Questionnaires that were distributed to the bank officials aimed at collecting data on strategic issues in the institutions.

3.8 Data analysis and Hypotheses Testing

Statistical Package for Social sciences (SPSS) were used to analyse data to obtain frequencies, mean differences and percentages which will be used to compare between different SMEs. SPSS has been credible because it can take data from almost any type of file and use them to generate descriptive statistics easily.

CHAPTER FOUR

4.0 RESULT AND DISCUSSION

4.1 Overview

The purpose of this research was to ascertain the role played by rural financing to the performance of SMEs using Mufindi community bank as a case study. This chapter therefore, therefore, presents the study findings and discussion.

4.2 Profile of the business and business owners

The profile of the business owners in terms of age, marital status and education level shows that 46.7 percent had the age between 30—39, 33.3 % had age between 40—49, 11.1% had age of 20—29 and 8.9% had the age between 50—59 years old.

Table 2: Distribution of respondents by age

Value label	Frequency	Percent
20-29	5	11.1
30-39	21	46.7
40-49	15	33.3
50-59	4	8.9
TOTAL	45	100.0

Source: Data from survey (2006)

With regard to education level of the respondent, about 53.3 percent of them had secondary education, 36.7 had primary education and only 10 percent had completed college education.

Table 3: Distribution of respondents by education level

Value label	Frequency	Valid percent 4.45.
Primary education	10	22.2
Secondary education	24	53.3
College and above	11	24.4
TOTAL	45	100.0

Source: Data from survey (2006)

In response to marital status, about 20% were single, 64.4% were married and 15.6% of the respondents were widows/widower.

Table 4: Distribution of respondents by marital status.

Value label	Frequency	Valid percent 4.45.
Single	9	20.0
Married	29	64.4
Widowed/widower	7	15.6
TOTAL	45	100.0

Source: Data from survey (2006)

4.3 Financial support and its accessibility

It is always argued that it is very difficult to get financial support in Tanzania, in my research using MuCoBa as a case study representing financial institutions the results were that 51.1 percent agree that there are a lot of obstacles/barriers in accessing loans, 22.2 percent strongly agreed about that, while 11.1 percent said there are no obstacles in accessing financial help and 15.6 percent of the respondents they could not know the answer. So the result shows that 73.3% of the respondents agree that it is difficult to access financial support in this area. This may be due to bank difficult terms in accessibility of finance like strong collaterals needed for loan application.

Table 5: Distribution of respondent's credit availability obstacles

Value label	Frequency	Percent
True	9	22.2
False	5	11.1
Sometimes	23	51.1
I am not sure	7	15.6
TOTAL	45	100.0

Source: Data from survey (2006)

4.4 Rural financial programs participation and life standard improvement

In the case of training and other awareness programs conducted by MuCoBa, it was observed that 68.9 percent of the respondents participate in these programs have increased knowledge and ability to save, they have also been exposed to the availability, existence, conditions which in turn have improved their ability to access bank loans.

Clients have also benefited in terms of increased business capital because saving at the bank means accumulating capital especially for start-ups. There as also been an improved understanding of the management and proper use of funds, which has been depicted on the business expansion/development and the ability of the business to repay the loans.

Table 6: Distribution of respondents by participation in financing programs

Value label	Frequency	Percent
Many times	11	24.4
Rarely	20	44.4
Never	14	31.2
TOTAL	45	100.0

Source: Data from survey (2006)

In this case the study shows that 66.7 percent agrees that credit has improved their standard of living and other benefit including acquiring family basic needs, sending children to good

schools, and being able to undertake construction and renovation of their houses, and 68.9 percent confess that they have accumulated assets like cash in banks, built more houses, cars due to proper use of the credit they got.

Table 7: Distribution of respondents by assets accumulation

Value label	Frequency	Percent
Yes	31	68.9
No	8	17.8
No credit	6	13.3
TOTAL	45	100.0

Source: Data from survey (2006)

4.5 Problems and Recommendations from the Respondents

The sale of properties/collateral of defaulters might quite usual threaten others from applying for loans because of fear of losing the pledged collateral and their reputation. In this regard more education should be provided on business management and proper use of funds so to minimise the number of defaulters and encourage more applicants at the same.

There were also complains on loan conditions were difficult especially for small businesses, that the loans are benefiting those who already have money. This comes because before one qualifies for credit she/he must deposit at least 20 percent of the amount of the loan applied at his/her MuCoBa account. Also it was argued that loaners having the required collateral should not be forced to deposit the 20 percent of loan being applied.

Also clients complained that it was unnecessary for familiar customers to go through similar processes each time they apply for credit because the bank already knows them

therefore they recommended that the bank should reduce interest rates especially to loyal customers, and they should also provide long term credit of two years and more.

Individual business loanees should be allowed to borrow loans of even less than TZS 500,000. This came because clients wishing to apply for individual business loans must apply the same from a minimum of TZS 500,000. These limit clients who do not own collaterals and are not willing to join the group loans.

4.6 Challenges Facing MuCoBa

The challenges facing the bank according to the credit manager, among others are that banking activities are not an African culture, most of the people fear to work with banks. They lack the understanding that banks could boost their savings by earning an interest and improve both their knowledge in business through training and expanding capital through credit at the same time.

Lack of enough transportation is also a challenge in the sense that some customers are up to about 100km from the bank. Fortunately the bank follows customers at such large distance to see their collateral, how they are progressing, conduct training.

4.7 Implication of the Study

Findings of this study shows that credit/capital availability is still a number one problem in small and medium start-up and performance. It is necessary for the bank to conduct campaigns, encourage people to deposit at the bank so as to accumulate capital, training on business activities and opportunities and conduct awareness programs on existence, conditions and terms of the bank loans.

Apart from training and education, collateral has been a long-time problem to the rural poor in accessing credit from banks. Even a few local people who had good houses or own land does not attract banks to give them loans because nobody would still be attracted to buy such good house at remote areas in case the customer default. Finally, although in the past anecdotal evidence showed that it was a sign of shame to borrow especially in rural areas, the positive response shown on this study is nonetheless evidence that such people are realising the importance of credit in business development.

CHAPTER FIVE

5.0 SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Summary

The purpose of the study was to investigate the role played by financial institutions, MuCoBa in particular, in the performance of SMEs in Mufindi district in Iringa region.

Specific objective included, to study the effect of rural financing to small and medium enterprises and accessibility barriers, to examine whether a microenterpenuer can meet his/her personal needs and other needs as a result of participating in rural financing programs, to evaluate whether micro-entrepreneurs' assets accumulates as a result of participating in rural financing programs.

Although clients ranked credit/capital availability as the most important factor in SME performance especially in starting up the study observed that also individual willingness to start up businesses is an affecting factor, therefore the bank, however had developed strategies like awareness programs on existence, conditions, and terms of bank loans. Furthermore, the business studied showed that they were development in terms of growth and expansion; also a comparison of start-up and present capital showed an impressive development. And in terms of credit availability, MuCoBa showed to be able to meet the increasing credit demand by strongly encouraging people to save by depositing at the bank.

5.2 Conclusion

Although small and business in Mufindi district has to somehow rise own funds for starting, the majority of the SME owners considered credit/capital as a very necessary

condition for their business survival. However credit availability especially to small enterprises is still a big problem. MuCoBa as an example of financing institution played an important role in SME by providing training and management skills and providing credits; most of which are were to be repaid within a year, at least once each month.

Mostly Agricultural loans are repaid during and after harvest. Study, further, showed a strong positive relationship between MuCoBa and businesses development in Mufindi. Finally, with regard to the credit availability from MuCoBa it was established that the bank was able to meet the increasing demand. It can therefore, be concluded that MuCoBa plays a significance role both stimulating and development of SME in Mufindi district.

5.3 Recommendations

5.3.1 Recommendation for MuCoBa

Robust and healthy economies, especially local economies, are dependent on the formation and development of small and medium enterprises. Hence much effort must be directed not only on the formulation of new SMEs but also on the expansion of the existing ones. The government should further develop policies that will facilitate good performance of rural financing institutions in the districts; it should also enhance the capacity of institution providing business training to SMEs. As for MuCoBa, more awareness campaigns are still needed especially to people who still think that credit is an embarrassment.

It is generally agreed that type of loans, individual or group, have its advantage to the respective group. Those who have collaterals and securities to pledge, with good business plan and big business, would prefer to opt on individual loans. On the other hand, those

who lack collaterals, securities to pledge as well as having small business would prefer to join in groups for loans. Each circumstance has its own players and way to handle.

Furthermore, loan officers may use their skills to advise clients to enter into groups they think clients may fit in. The balance between individual loans and group loans may be ideal for the survival of the bank. If loan officers would comply with their professional skills and adhere to scholars views on advancing loans, it may in one way or another help in the whole process of advancing loans that would be profitable and risk free for the bank and the clients. Hence, the bank becomes successful and its clients advance through loans advanced to them.

5.3.2 General recommendations

As with financial institutions, the focus is on broadening the outreach and enhancing the financial sustainability of rural operations of the appropriate financial institutions: commercial banks, non-bank financial institutions, microfinance organizations, and village-based financial institutions. The approach would entail:

- (i) Seminars and workshops to expose all players to best practice techniques for managing risk, reducing cost, and increasing revenue;**
- (ii) Performance-based assistance (rewarding financial sustainability first, and outreach increase second) to those institutions that take up the proposed approach, with funding for start-up costs, improvement of management information systems, training for staff and management, and equipment and hardware as appropriate; and**
- (iii) The formation of networks of institutions, to advocate for supportive policies and share learning experiences and training facilities.**

Social development and investment funds may be able to play a complementary role by building up the capabilities of the client base. Social funds and welfare-oriented revolving funds have not proven very successful in establishing sustainable credit programs, but they may be able to develop the capabilities of rural clientele to form community groups and manage business activities to enhance their attractiveness as microfinance clients. To overcome the problems of risk management and the cost of obtaining information on potential borrowers in rural areas, the regulatory structure should facilitate the formation of a broadly dispersed network of institutions, capable of mobilizing savings, as a first step into financial intermediation.

To develop financial services in rural areas in a manner that is both responsive to client needs and financially sustainable, three main approaches can be used:

- (i) Bring the commercial system closer to the rural clientele by improving the business environment (reducing uncertainty and risk, and reducing costs of information gathering, client monitoring, and other transactions) and designing financial products that are attractive to both clients and providers. For this purpose, work on the commercial financial system would include activities such as: prudential supervision frameworks and specialized provisions for rural banks and financial institutions (with adapted supervision requirements); improved transfer payment networks; improved financial product definition and market identification; risk-reducing strategies (warehouse receipt collateral systems); credit bureaus to monitor repayments across sectors and across all institutions; and time-bound subsidies for experimental rural branch banking.

- (ii) Bring the clientele closer to the financial system through grassroots training efforts in financial skills and business management, building community associations and institutions, and organizing potential participants in the financial system (smallholder farmers, small traders, and others) into groups that can support improved access to markets and finance. These measures for building up the client base can be complemented by providing institution-building support to specialized private financial institutions that focus on small and medium borrowers through group liability and other techniques--building on and working through indigenous organizations where feasible. If developed correctly, these measures can lead to sustainable, self-financed provision of financial services (especially starting with savings services) and can link eventually to the more formalized commercial system.

- (iii) Link rural finance to non-financial activities in rural areas, in particular to product processing, input supply, and marketing activities. For example, private smallholder-based agroindustry (outgrower cotton, sugar, vegetables, fruits and timber traders) could develop arrangements for passing financing down the line to purchase agents and producers. This approach would also look into ways of providing financing (and increasing cost recovery) through providers of inputs (fertilizers, chemicals, machinery) and marketing entities (auctions, integrated processors and sellers).

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APPENDICES

Appendix 1: Questionnaire

My name is Godfrey Godwin a student from Sokoine University, I am doing research on rural financing, and therefore the purpose of this Questionnaire is to capture data that will reflect the impact of rural financing to the performance of small and medium enterprises. Would you please assist my study by answering the following questions? I assure you that your answers will be kept confidential.

Please write the letter of an appropriate answer or write the appropriate explanation in the space provided.

1. Respondent name

2. Date of interview

3. Marital status

1. Single

2. Married ()

3. Widow

4. Age

5. Education level

1. Completed primary education

2. Completed secondary education ()

3. Completed college education

4. Above college education (please specify).....

6. Does MUCOBA provide efficient services and respect the people who are the owners / proprietors of the bank?

1. Yes

2. No ()

3. Not very much

✓ 7. Is the bank helpful to people with respect to social aspects, that is, education, health and sports? 1. Yes

2. No ()

3. I don't know

✓ 8. Does the bank forcefully confiscate the properties of the clients who get loan from them and do not pay in due time? If so, what is your opinion?

1. Yes

2. No ()

3. I don't know

✓ 9. Are the terms / conditions of getting loans from MUCOBA a bottleneck (obstacle) to the people who want to secure loans?

1. True

2. False ()

3. I am not sure

10. Does the bank favour businessmen with large capitals?

1. True

2. False ()

3. I am not sure

11. Agriculture is among the major economic activities within Mufindi district. Is the bank a help in advancing the activity?

- 1. Yes
- 2. No
- 3. I don't know

12. Does the bank devote to educate clients about proper financial management, both loans and profit obtained from their business?

- 1. Yes
- 2. No
- 3. I don't know

13. Granting loans to people with low income is a great risk to a bank. With your own views do you think that this is it true? What is your opinion in relation to MuCoBa.

- 1. Yes
- 2. No
- 3. I don't know

14. Does the bank support livestock growers in the district?

- 1. Yes
- 2. No
- 3. I am not sure ()

15. Timber business is among the activities done in the district. Does the bank support these business dealers? What is your opinion?

- 1. Yes
- 2. No ()
- 3. I don't know

16. Women play key roles in economic development of any society. Does the bank participate in advancing women economically? Explain briefly.

- 1. Yes
- 2. No
- 3. I don't know

17. Does MUCOBA directly participate in development activities within the district?

If so, in which aspects?

- 1. Yes
- 2. No

18. In your business/farming activities did you get financial support from MuCoBa?

- 1. Yes
- 2. No ()

19. If yes in 18 above what was your initial capital before getting MuCoBa credit?

- 1. Below 5000,000/=
- 2. Between 5000,000 and 10,000,000/=
- 3. Between 10,000,000 and 15,000,000/= ()
- 4. Above 15,000,000/=

✓ 20. Do you think credit has increased your total average profit per month?

- 1. Yes
- 2. No ()

21. If Yes in 20 above what was your total average profit per month before getting credit

- 1. 1-2million
- 2. Between 2 and 3 millions ()
- 3. Between 3 and 4 millions
- 4. Above 7 millions

22. If yes in 20 above what is your average profit per month after getting credit

- 1. 1—3 million
- 2. Between 3—5 millions ()
- 3. Between 5—7 millions
- 4. Above 7 millions

23. Does MUCOBA train or teach entrepreneurship to its clients before and after loan disbursement?

- 1. Yes
- 2. No ()

24. Have you accumulated any assets like cash in the bank, houses, and cars after investing credit you obtained from MuCoBa?

- 1. Yes
- 2. No ()
- 3. No credit

25. Do you think credit has increased your standard of living?

- 1. Yes
- 2. No ()
- 3. No credit

26. Have you ever participated in rural financing programs like seminars, workshops, training or public meetings conducted by MuCoBa or any other financial institution?

1. Many times

2. Rarely ()

3. Never

THANK YOU.

Appendix 2: Frequency Table**Education level of respondent**

	Frequency	Percent	Valid Percent	Cumulative Percent
Primary	10	22.2	22.2	22.2
Secondary	24	53.3	53.3	75.6
College	11	24.4	24.4	100.0
Total	45	100.0	100.0	

Age of respondent

	Frequency	Percent	Valid Percent	Cumulative Percent
20-29	5	11.1	11.1	11.1
30-39	21	46.7	46.7	57.8
40-49	15	33.3	33.3	91.1
50-59	4	8.9	8.9	100.0
Total	45	100.0	100.0	

Marital status

	Frequency	Percent	Valid Percent	Cumulative Percent
Single	9	20.0	20.0	20.0
Married	29	64.4	64.4	84.4
Widow	7	15.6	15.6	100.0
Total	45	100.0	100.0	

Participation in rural financing programs

	Frequency	Percent	Valid Percent	Cumulative Percent
Many times	11	24.4	24.4	24.4
Rarely	20	44.4	44.4	68.9
Never	14	31.1	31.1	100.0
Total	45	100.0	100.0	

MuCoBa loan terms an obstacle to bellowers

	Frequency	Percent	Valid Percent	Cumulative Percent
True	10	22.2	22.2	22.2
False	5	11.1	11.1	33.3
I am not sure	7	15.6	15.6	48.9
Sometimes	23	51.1	51.1	100.0
Total	45	100.0	100.0	

Assets accumulation

	Frequency	Percent	Valid Percent	Cumulative Percent
Yes	31	68.9	68.9	68.9
No	8	17.8	17.8	86.7
No credit	6	13.3	13.3	100.0
Total	45	100.0	100.0	