INVESTIGATING THE TRADE-OFF BETWEEN MICROFINANCE SUSTAINABILITY AND THE DEPTH OF OUTREACH: A CASE OF ZIMBABWE MICROFINANCE INSTITUTIONS.

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DEDICATION

This document is especially dedicated to my wife Fadzai and daughter Nandi.
DECLARATION

I, Tafara Matanga, do hereby declare that this dissertation is the result of my own investigation and research, except to the extent indicated in the Acknowledgements, References and by comments included in the body of the report, and that it has not been submitted in part or in full for any other degree to any other university.

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Student signature    Date
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ABSTRACT

The purpose of this study was to ascertain whether financially sustainable MFIs can still play their strategic role of poverty alleviation by providing financial services to the poorest and low-income households. This was done by adopting a survey approach where questionnaires were administered to various microfinance institutions. Microfinance is viewed as a mechanism for financial inclusion, that is, it facilitates access to financial services by the financially marginalised segments of the society at an affordable cost. In recent years there has been a paradigm shift towards financially sustainable MFIs. The attainment of self-sufficiency by microfinance institutions is viewed as the necessary conditions for effective poverty reduction. However, it has been observed that too much focus by MFIs on self-sufficiency might lead to a mission drift whereby the extremely poor households are further financially marginalised.

The reviewed literature on MFIs sustainability and the depth of outreach reflects that there are two major schools of thoughts on microfinance, namely, the institutionalist, and the, welfarist whose views are contradictory with regards to the impact of MFIs’ sustainability on the depth of outreach. The literature also revealed that there is an ongoing debate among various authorities on the impact of MFI's sustainability and the depth of outreach.

The findings of the study indicated that the pursuit of financial self-sufficiency does not lead to mission drift. The study concludes that in the process of pursuing sustainability the microfinance institutions still serves their target market that is the poor and financially marginalised.

The study proffers recommendations that would help to ensure that MFIs become an effective mechanism for financial inclusion. Government interventions through the review of MFIs licences and the Moneylending and Rates of Interest Act, and availing of targeted cheaper loans. It is also recommended that MFIs should be innovative and specialise on lending strategies that allows the poorest households to borrow without collateral.
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CHAPTER ONE

INTRODUCTION

1.0 INTRODUCTION

This Chapter outlines the purpose of the study, the background to the study, statement of the problem, objectives of the study, research questions, research hypothesis, justification of the study, and the scope of the study.

1.1 BACKGROUND TO THE STUDY

The purpose of this study is to critically assess the impact of sustainable microfinance institutions (MFIs) in promoting the depth of outreach in Zimbabwe. A microfinance institution (MFI) is an organisation that provides small amounts of credit and potentially other small scale financial services to clients without access to the formal banking system (Morduch, 2000). According to the definition by Conning (1999), the depth of outreach is whereby MFIs extends their financial services to a wider audience, especially towards the poorest of the poor. This entails providing access to financial services for all. Sustainability in the context of this study relates to operational self-sufficiency of an MFI (Sa-Dhan, 2003). It was observed that, once an MFI becomes sustainable, it is capacitated to provide financial services to its targeted market. MFIs' target market includes the poor, low income, micro to medium enterprises, and all the financially marginalised segments of the society (ibid). This research was therefore motivated by the realisation of the strategic importance of MFIs in poverty reduction.

It is also imperative to take cognisance that most of the studies on this subject were undertaken during the time when Zimbabwe was economically and politically stable. During the period, funds to support microfinance were available from the government and donors. The study therefore attempts to fill the research gap that currently exists by focusing on microfinance industry in an economy characterised by liquidity crunch, low fiscal space and declining international aid flow. The international aid in the form of grants to the Non-Governmental Organisations (NGOs) MFIs declined as result of the global economic crisis. In order for MFIs to continue playing their role of promoting financial inclusion, they need to become financially self-sufficient. According to Reserve
Bank of Zimbabwe [RBZ] (2008), sustainable MFIs have the capacity of lowering the poverty levels of the affected households.

The provision of financial services to the poor and low income households is an effective tool of spreading economic opportunities that reduce poverty. Historically, the most commonly known financial service for the poor and low-income households in Zimbabwe was the provision of microcredit (Klinkhaher, 2009). Microcredit refers to the provision of small loans that are accessible to households and entrepreneurs who have been traditionally excluded from the formal financial services market (ibid). Microcredit ranges from group and individual business loans, to personal consumption smoothening loans (Sa-Dhan, 2003). A study by United Nations Department of Economic and Social Affairs [UNDESA] and United Nations Capital Development Fund [UNCDF] (2006) reveal that in most developing economies financial services are available only to a minority of the population. The study highlighted that in Southern Africa about 60% of the population has no access to financial services (ibid). Similarly, a national microfinance survey conducted by the RBZ (2006) also reveal that only 30% of the country’s economically active have access to the formal financial systems.

Halimana and Zwizwai (2004); and Baydas, Graham and Valenzuela (1997) undertook studies to establish the source of reluctance by formal financial institutions in extending their services to the marginalised segment of the community. Halimana and Zwizwai (2004) note that the major reasons for this financial exclusion are attributed to high transactions costs associated with administering small, but many loans in addition to the non-existence of collateral among the recipients. Baydas, Graham and Valenzuela (1997) concludes that commercial banks are reluctant to service poor and low-income segment because their profit maximising shareholders hold a perception that microfinance activities cannot give them a return enough to maximise their bottom line. Secondly, they noted that commercial banks have standards and regulatory requirements that they have to adhere to with respect to unsecured lending and interest rates that are not appropriate for microfinance. Further, they observed that organisation structures, procedures, products and delivery methodologies of commercial banks are not appropriate for microfinance. Finally, they noted that there are cultural barriers that inhibit change as officials and managers often perceive the poor as unbankable.
The absence of the pro-poor financial products within the mainstream financial services sector led to the identification of MFIs as an alternative option of providing financial services to the economically marginalised segment of the society. This was further anchored by the great potential presented by MFIs in welfare enhancement through their special features that enables them to have a broader market reach.

1.1.1 Overview of the microfinance sector in Zimbabwe

In Zimbabwe, microfinance only began to gain significance in the late 1990s (United Nations Development Programme [UNDP], 2009). The country’s financial sector which is among the most competitive in Southern Africa region, is comprised of merchant banks, commercial banks, discount houses, finance houses, building societies, development banks, savings bank, credit unions, housing cooperatives, money lenders, insurance companies, pension funds, and a stock exchange (RBZ, 2008). The emergence of microfinance during the 1990s is mainly explained by the introduction of World Bank/International Monetary Fund (IMF) sponsored Economic Adjustment Programme (ESAP). ESAP introduced financial reforms with a view to liberalise the market and widening the scope of financial services. These reforms facilitated the entrants of new players into the market including the formal and informal MFIs (UNDP, 2009). Halimana and Zwizwai (2004) argue that the rise of microfinance in Zimbabwe in the 1990s was attributed to the deteriorating economic environment. This trend is supported by theories of microfinance which acknowledge a high positive correlation between poverty and demand for microfinance products (Robinson, 2001). This is explained by the fact that when the gap between the affluent and the poor begin to widen, the poor are increasingly excluded from a number of services. In their quest to be economically active, they engage in informal activities using funds obtained from MFIs.

Despite gaining significance since the late 1990s, the microfinance sector in Zimbabwe had a stifled development. According to Klinkhamer (2009), the sluggish development of the sector is attributed to challenges associated with lack of funding, inhibitive legal and regulatory framework, lack of skilled staff, and lack of efficiency. As at the third quarter of 2012, there were 172 registered MFIs suppliers in the country compared to 1,700 in 2003 (RBZ, 2012).
Similarly, UNDP (2009) noted that failure by government to put in place an appropriate microfinance regulatory environment is impacting negatively on the development of the microfinance sector. According to the World Bank (2006) index of Credit Information Depth, Zimbabwe was given the lowest possible score of 0.0. The index evaluates the financial sector in terms of the rules that affect the scope, accessibility and quality of credit information available through either public or private registries. Presently, the regulation of the sector is based on a silo approach whereby regulation is divided along functional lines such as banking, insurances, pension, securities, and microfinance (UNDP, 2009). The silo approach has a limitation in regulating financial groups that operate in several segments of the financial sector, for instance an institution may be into banking, and insurance industries. The application of the silo approach would entail that this single institution would have several regulators. With regards to microfinance sector, a multiplicity of microfinance legislation currently governs the sector. MFIs are registered under various legal instruments such as Money Lenders and Rates of Interest Act, Banking Act, Cooperative Act (Chapter 24:05) of the Registrar of Societies and Private Voluntary Organisations Act (Chapter 7:05).

1.1.2 Zimbabwe Microfinance Service Providers

The market structure in microfinance varies significantly across countries, depending on their stage of financial development, level of economic development, policy environment, and other factors (ADB, 2000). In Zimbabwe, there are a variety of players in the supply of finance to low-income households. The institutional types involved in the supply of microfinance include banking institutions and their subsidiaries, non-bank financial institutions, credit unions and development financial institutions (Klinkhamer, 2009).

Banking Institutions and their Subsidiaries

By the end of third quarter of 2012, Zimbabwe had 18 commercial banks, two merchant banks, four discount houses, and one savings bank (RBZ, 2012). Commercial banks are the largest players in the banking system, in terms of total assets with the broadest range of products on offer. Merchant banks offer a broad range of financial services
except current accounts/check facilities. Discount houses deal mostly in securities. Most banking institutions in Zimbabwe have high minimum balances.

In the past, traditional banks financial services were biased in favour of consumer durables, raw materials for clients in the manufacturing and agricultural sector, and distribution (Mishi & Kapingura, 2012). In recent years, banks have also shown a great interest in providing credit lines to the tobacco industry against the background of its potential to earn foreign currency. With the decline of the major industries and companies due to the adverse macroeconomic environment, several banks, have however, transformed their operations in order to penetrate the lower-end of the market segment. The major providers of microfinance among banking institutions include, Commercial Bank of Zimbabwe (CBZ), Barclays, CABS, Standard Chartered Bank, TN Microfinance and MicroKing Savings and Credit Company (Pvt.) Ltd (Klinkhamer, 2009).

**Non-Bank Financial Institutions**

The non-bank financial institutions are comprised of four different categories, namely, building societies, asset management companies, moneylending institutions, and development oriented institutions (RBZ, 2012). Building societies offer the largest product menu of the non-bank financial institutions, with a broad range of savings, loans transactions, and investment products. Of the four building societies that were operational in 2007, CABS was the most active in downscaling to lower-income market segments (Klinkhamer, 2009). CABS has a number of products tailored to small and medium-sized businesses and the self-employed (ibid).

In 2008, the number of moneylenders that were operational was close to zero. However, money lenders used to be the largest category of microfinance service providers in Zimbabwe. Many of the moneylenders are family businesses employing less than 10 employees and serving a couple of hundred clients only, with the largest being NISSI Microfinance, which reached some 11,000 clients at its peak (ibid). The service menu of moneylenders is rather narrow, focusing on the provision of 30-day consumer loans; however, as a result of the economic crisis, enterprise financing has been increasing since 2005 (ibid).
Developmental Partners, who include the donor community, are instrumental in the development and implementation of microfinance programmes in Zimbabwe through the provision of grants, subsidized funds and technical assistance (RBZ, 2006). Some of the larger institutions include, Self-Help Development Savings and Credit Company (Pvt. Ltd), which is a wholly-owned subsidiary of Self-Help Development Foundation Trust, Pundutso Microfinance Company which was developed out of a World Vision project, and Zambuko which was one of the first major NGO MFIs.

**Credit Unions / Cooperatives**

In 2008, the number of Savings and Credit Cooperative Societies (SACCOs) that were operational was close to zero. But based on government data this type of provider used to be widespread; it includes SACCOs that are member of the umbrella body, National Association of Credit and Savings Cooperatives (NACSCUZ) and others. Statistics by the World Organization of Cooperative Credit Unions [WOCCU] (2011) indicates that there are 53 SACCOs in Zimbabwe. SACCOs usually operate by mobilising their membership from individuals with similar characteristics such as same geographic location or employers. For instance, the Masvingo Teachers Association Savings and Credit Society reached some 10,000 clients in the mid-2000s. Of the SACCOs in Zimbabwe, 35% are employee-based, 23% enterprise-based, 19% agriculture-based and the remaining 23% are both enterprise- and agriculture-based.

**Development Finance Institutions**

In the early 1980s, the Government of Zimbabwe (GoZ) through a deliberate policy aimed at empowering the previously marginalised indigenous majority, established various financial institutional targeted at providing service to the micro, small, and medium enterprises. The Zimbabwe Development Bank (which is now the Infrastructure Development Bank of Zimbabwe), the Small Enterprise Development Corporation (SEDCO), and the smallholder finance facility at the Agribank are among the established development financial institutions (Hungwe, 2000).
1.2 STATEMENT OF THE PROBLEM

Lack of access to financial resources is one of the major reasons why many people in developing economies remain poor. In Zimbabwe, the majority of the poor have no access to loans and other basic financial services. This is because this group is perceived as not profitable by mainstream corporate banks because they cannot put up acceptable collateral. Another reason is that the costs for banks of screening and monitoring the activities of the poor, and of enforcing their contracts, are too high to make lending to this group financially viable. Since the late 1990s, however, the poor in Zimbabwe have increasingly gained access to small loans from various MFIs. In this regard, microfinance has long been viewed as set of instruments relevant to stimulating entrepreneurship in the country thereby critical in the fight against poverty.

The financial sector development strategies have largely focused on strengthening overall financial stability and increasing the availability of services to major economic actors. This entailed that the financially marginalised households are being further excluded from accessing financial services. It is against this background that MFIs are viewed as the only possible alternative to narrow the gap that exist between the banked and the financially excluded households. However, in order for MFIs to narrow this gap, they need adequate financial resources. Previously, the major sources of funds for MFIs comprised the grants from donors as well as government subsidies. These sources have diminished drastically owing to the current global economic crisis and the low fiscal space respectively. Therefore there is need for MFIs to strengthen their institutional capacity to meet the market demand and effectively absorb the available private funds for on-lending.

1.3 OBJECTIVES OF THE STUDY

The objectives of the study are to;

- Determine whether MFIs in Zimbabwe are sustainable.
- Determine whether the pursuit of sustainability by MFIs will result in increased depth of outreach.
- Determine other factors that may contribute to the depth of outreach.
• Draw some policy recommendations.

1.4 RESEARCH QUESTIONS

To achieve the study objectives, the following questions will be addressed;

• Are MFIs in Zimbabwe sustainable?

• What is the impact of MFIs sustainability on the depth of outreach?

• What are other factors that may contribute to the depth of outreach?

• What are some policy recommendations that can be drawn from the study?

1.5 PROPOSITION OF THE STUDY

The study proposes that sustainable MFIs have a lower depth of outreach, that is, they drift from their mission of providing financial services to the poorest and prefer to services the moderately poor households.

1.6 JUSTIFICATION OF THE STUDY

This research is intended to contribute to the current debate on MFIs sustainability and the depth of outreach. The study would therefore add to the current body of knowledge. Further, government, academia, MFIs, and the general public would benefit from the study as follows;

This study will proffer some recommendations targeted to the policy markers which are expected to assist in the formulation of pro poor policies and the regulatory framework for the microfinance sector. With regards to the academia, the research is intended to add significantly to the available body of knowledge in the field of microfinance particularly on issues MFIs sustainability and outreach in the developing countries. This is on the background that only a few studies have been undertaken on this subject by (Rhyne, 1998; Babandi, 2011; Cull et al 2006; Hartarska and Nadolnyak, 2007; Hao, 2002; Lafourcade et al, 2005; and Lau, 2008). The study will play an important role in bridging the information gap that currently exists. The research will also
provide an analytical perspective on the strategies and recommendations that may be adopted by MFIs. Finally, it is expected that the study findings, conclusions and recommendations will form part of a valuable source of information to the general public.

1.7 SCOPE OF THE STUDY

The research will focus on investigating the trade-off between MFIs’ sustainability and the depth of outreach. The research will also focus on microfinance service providers, and their contribution to the general welfare of the poor and the economic development. The study period is between 2009 and 2011 to allow for a realistic financial comparisons based on the multicurrency regime. The participating MFIs are those that are legally registered under various Acts that govern different types of MFIs.

1.8 ORGANISATION OF THE PAPER

The rest of the document is arranged as follows: Chapter 2 reviews relevant literature. Chapter 3 discusses and justify the research methodology. Chapter 4 presents the analysis and findings while Chapter 5 concludes the study and recommends strategies.
CHAPTER TWO
LITERATURE REVIEW

2.0 INTRODUCTION

This chapter explores both the theoretical and empirical literature surrounding microfinance. The researcher started by providing and discussing the theoretical framework of the study before discussing MFIs’ sustainability and the depth of outreach. A discussion is also presented on the trade-offs between MFIs’ sustainability and the depth of outreach with evidence from previous studies. The review of literature in this chapter is done in relation to the study objectives.

2.1 MICROFINANCE INSTITUTIONS

A microfinance institution (MFI) is defined as an organisation that provides small amounts of credit and potentially other small scale financial services to clients without access to the formal banking system (Morduch, 2000). Microfinance has become a broadly known sector since the pioneering work and success of Grameen Bank in Bangladesh. The bank adopted a simple mission “to alleviate poverty by providing small loans to economically active but disenfranchised people” (Monzurul and Muhammad, 2011). Microfinance institutions provide a variety of products including micro loans, savings and other deposit products, remittances and transfers, payment services, insurance, and any other financial product or service that a commercial bank does not offer to low-income clients in the banking system (Morduch, 2000). Unlike in the traditional commercial banking sector, there is a general understanding that the average microfinance client does not have many assets, thus collateral is usually sought in the form of social capital (Monzurul and Muhammad, 2011). In this respect, microfinance approaches poverty alleviation through the promotion of inclusive financial services to combat exclusion and dependency (Vik, 2010). Through using this approach, microfinance is regarded as a movement, that is, a set of ideas, a way of thinking about development and the poor, a policy and approach to poverty elimination, as well as a set of best practices.
During the foundation of microfinance, services were restricted to the provision of microloans to the disenfranchised (Koveos, 2004). The major source of funds for these loans was mainly from the international aid agencies (Organisation for Economic Co-operation and Development [OECD], 1991). During this era in microfinance movement, the state intervened in the financial sector with the perceived purpose of directing financial resources towards socially and economically desirable activities (Koveos, 2004). The intervention involved government ownership of banks, controls on interest rates, and directed credit towards priority sector at subsidised interest rates (ibid). The outcome of this policy thrust was the misdirected credit towards unprofitable public sector enterprises and politically connected borrowers (Von Pischke, 1991). This led to a rapid increase in the volumes of nonperforming loans, and a weak and non-competitive banking sector (ibid). The few loans that were advanced to the poor took place with little effort towards assessment of creditworthiness or monitoring of loans. More importantly, these loans were implicitly treated as grants by both lenders and borrowers, as a result loan recovery rates were extremely low (Koveos, 2004).

The Grameen Bank of Bangladesh is closely associated with the history of microfinance. The institution recorded an outstanding success with regards to poverty reduction (Hossain, 1988). The idea of the Grameen Bank model was first conceived in early 1970s. The bank was modelled to function as a commercial bank but incorporating a distinguishing aspect of institutionalised group monitoring and group loan accountability (Monzurul and Muhammad, 2011). Initially, the loans were mainly funded by donors and government (Hossain, 1988; OECD, 1991; Monzurul and Muhammad, 2011). The advent of the Grameen Bank model ushered in a new era in the world of microfinance. The innovative group monitoring initiatives resulted in a more than 98% loan recovery rate. A related success story in the history of microfinance is that of Bank Rakyat Indonesia (BRI) (Robinson, 1995). The BRI bank symbolise the revolution of the microfinance industry in the Indonesian countryside through some innovative lending policies (ibid). These two institutions have been the pioneers of the present day microfinance industry.

The case of Grameen Bank and BRI marked a paradigm shift in the history of microfinance. Their operations demonstrated that the market can be used in the allocation and monitoring the use of microfinance resources (Koveos, 2004). Although
these institutions during their formative years depended upon the government support and donor grants, their sustained success was solely depended on their high loan recovery rates (Hossain, 1988). The loan recovery rates were high as a result of continuous monitoring of borrowers. Consequently, the lessons offered by these two pioneering MFIs formed the basis by which microfinance was viewed as strategic tool in poverty alleviation.

2.2 MODELS OF MICROFINANCE INSTITUTIONS

When the concept of microfinance began, MFIs were mainly non-governmental organisations (NGOs) (Schicks, 2007). Their primary sources of funding were international donors, private benefactors and governments (ibid). These original MFIs were not focused on monetary return but merely on creating social benefits through engendering the concept of financial inclusion (Hossain, 1988). The Grameen Bank, a well known MFI bank in Bangladesh was founded on that basis and initially received significant grant funding. However, the current trend with many MFIs points to a situation where there is pursuit for both goals of achieving a social impact as well as financial sustainability.

Lafourcade, Isern, Mwangi, and Brown (2005) notes that microfinance institutions include a broad range of diverse and geographically dispersed institutions that offer financial services to low-income clients, NGOs, non-bank institutions, cooperatives, rural banks, savings and postal financial institutions, and an increasing number of commercial banks. In their study, they identified the following types of MFIs:

2.2.1 Grameen model

According to Lafourcade, Isern, Mwangi, and Brown (2005), the Grameen model emerged from the poor-focussed grassroots institution, Grameen Bank, started by Prof. Mohammed Yunus in Bangladesh. It essentially adopts the following methodology: A bank unit is set up with a Field Manager and a number of bank workers, covering an area of about 15 to 22 villages. The manager and workers start by visiting villages to familiarise themselves with the local settings in which they will be operating and identify prospective clientele, as well as explain the purpose, functions, and mode of operation
of the bank to the local population. Groups of five prospective borrowers are formed; in the first stage, only two of them are eligible for, and receive, a loan. The group is observed for a month to see if the members are conforming to rules of the bank. Only if the first two borrowers repay the principal plus interest over a period of fifty weeks do other members of the group become eligible themselves for a loan. Given, these restrictions, there is substantial group pressure to keep individual records clear. In this sense, collective responsibility of the group serves as collateral on the loan.

### 2.2.2 Association

According to Lafourcade et al (2005), this is a model where the target community forms an association through which various microfinance activities are initiated. Such activities may include savings. Associations or groups can be composed of youth, women and can form around political or religious or cultural issues. Associations usually create support structures for microenterprises and other work-based issues. In some countries, an association can be a legal body that has certain advantages such as collection of fees, insurance, tax breaks and other protective measures (ibid).

### 2.2.3 Credit unions

A credit union is a member-driven, self-help financial institution. It is organized by and comprised of members of a particular group or organization, who agree to save their money together and to make loans to each other at reasonable rates of interest (Lafourcade et al, 2005). The members are people of some common bond, working for the same employer or belonging to the same church. A credit union's membership is open to all who belong to the group, regardless of race, religion, colour or creed. A credit union is a democratic, not-for-profit financial cooperative. Credit Unions due to their nature are owned and governed by its members, with members having a vote in the election of directors and committee representatives (ibid).

### 2.2.4 Community banking

Community banking model essentially treats the whole community as one unit, and establish semi-formal or formal institutions through which microfinance is dispensed
(Lafourcade et al, 2005). Such institutions are usually formed by extensive help from NGOs and other organizations, who also train the community members in various financial activities of the community bank. These institutions may have savings components and other income-generating projects included in their structure. In many cases, community banks are also part of larger community development programmes which use finance as inducements for action (ibid).

2.3 MICROFINANCE AND DEVELOPMENT

Microcredit emerged as a central feature of post structural adjustment development in many development countries. According to Cons and Paprocki (2010) microfinance and its supposed object, micro-enterprise, form the backbone of a turn towards self help development that envisions the poor as untapped, potential economic players. The researchers argued that rather than providing hand-outs which supposedly undermine self-sufficiency, assistance to the poor can only be best delivered through loans. This approach eliminates barriers to market entry and promote the discipline of entrepreneurial economic participation (ibid). Soulama, (2005) also asserts that microcredit programs have a positive impact not only on the micro-enterprise income but also on the female borrowers. Through microcredit, women can achieve multiple productive activities and diversify their sources of income more than men (ibid).

Ledgerwood (1999) identifies three categories of microfinance impact namely, economic, socio-political and psychological. With regards to economic impact, he explained that economic activity may be affected through business expansion in formal or informal sector, consumption smoothing, or other channels. Socio-political impact manifest as the MFI’s activities result in a change in the status of a subsector. Finally, psychological impact results when individuals or groups receiving the benefit of the MFI’s activities feel a greater sense of empowerment.

Microfinance enable clients to break out of the poverty trap by facilitating growth in household income, providing channels for mobilizing savings and through group as well as individual loans help to build up the village’s asset base. Hoff and Stieglitz (1993) elaborates on the role of market interactions in reducing information costs sheds light on the working of MFIs. They argued that interaction between credit markets, microloans enabling access to input and product markets, to complementary inputs, and to new
markets generates externalities that go far beyond the immediate benefits from the loans. The network externalities generated by these loans offer manifold channels for increasing the efficiency of investments at the household level. The obvious benefits are in the form of higher income and wages. Larger sustainable benefits accrue from increases in productivity and productive capacity as credit enables borrowers to use newer technology, intermediate goods, and services, such as marketing and transportation. However, investment in infrastructure, such as transport, communications, schools, drinking water supply, is crucial to the realization of these benefits.

There is also recognition to the effect that providers of microfinance services have the potential to integrate the provision of credit with developmental activities such as community and leadership development, recreation, training in practical skills, entrepreneurship and financial management as well as delivering health education to their clients especially with respect to HIV and AIDS awareness (RBZ, 2008).

**2.3.1 Financial sector efficiency**

Financial sector efficiency is a key factor for economic development and growth (Schaaf, 200). As the poor and marginalised members of the community begin to access credit facilities, they tend to be empowered both socially and economically (OECD, 1991). This is against the background that financial resources that are channelled through credit are crucial for both fixed and working capital, consumption smoothening during periods of seasonal fluctuations of income, and to cushion against uncertainties such as sickness (Ghosh, Mookherjee and Ray, 2000; OECD, 1991). In a broad macroeconomic perspective, financial sector development and efficiency is essential in the enhancement of aggregate growth of the country and changing income distribution in favour of the poorest quintile of the population (World Bank, 2008). On the contrary, inadequate credit can result in persistent income inequality and poverty traps (Beck, Demirgüc-Kunt and Levine, 2007; World Bank, 2008).

Satya and Rupayan (2010), notes that in rural and marginalised regions, credit markets are often inefficient. This credit market inefficiency would inevitably render informal sources such as friends, relatives, and local moneylenders as the only source of credit
to the poor (ibid). However, a moneylender typically exploit the poor as it usually charge interest rates in excess of 75% per annum, and in most cases credit from relatives and friends is inadequate and rarely available (ibid). Therefore, such sources of loans cannot be relied upon as a means to productive purposes but rather for coping with emergencies (Hoff and Stiglitz, 1990). On the other hand, the available formal financial service providers, even if they are prepared, face a number of challenges in their quest to provide credit to the poor (Ledgerwood, 199). These challenges in turn affect their sustainability which in turn affects their outreach to the poor. These two terms, sustainability and outreach are the focus of this study. Kaveos (2004) indicates that there is what is called “Critical Micro-finance Triangle” that is used to evaluate Micro-finance institutions based on their objective of reducing poverty. The triangle can be depicted as (ibid):

![Critical Micro-Finance triangle](image)

**Figure 0.1: Critical Micro-Finance triangle**


According to Figure 2.1, the three corners of the triangle represent outreach to the poor, financial sustainability and welfare impact respectively. The inner circle in the Figure
represents MFI innovations in technology, policies, organization, and management that affect how well each objective is met (ibid). The outer circle represents the environment within which the MFI operates which also affects performance. This environment broadly includes the human and social capital possessed by the poor, the economic policies of the country, and the quality of the financial infrastructure that supports financial transactions (ibid). Improvements in the environment make it easier for MFIs to reach the three objectives (ibid).

2.4 THE SCHOOLS OF THOUGHT ON MICROFINANCE SERVICE DELIVERY

There are various schools of thought on how to deliver financial services to the marginalised segment of the society. Among these various schools of thoughts, there are two which have been adopted by many authorities in the field of microfinance, namely, the institutionalist and the welfarist (Bhatt and Tang, 2001; Brau and Woller, 2004; Woller and Woodworth, 2001). The institutionalist approach centres on “financial deepening” of building sustainability to serve those excluded from services of conventional banks. Achieving financial self-sufficiency and the number of clients are at the heart of the institutionalist approach. Institutionalists do not agree on directly targeting the very poor. They argue that targeting the very poor is very costly and consequently hinder the goal of achieving financial self-sufficiency (Woller and Woodworth, 2001). On the other hand, welfarists argue that it is possible to realize breadth and depth of outreach with poverty targeted services. For welfarists, the net social benefits derived from serving a limited number of very poor clients are better than serving large numbers of not-so-poor clients (ibid). To have the same effect on social welfare, the self-sustainable lender must have 15 to 125 times the breadth of the poverty lender (Schreiner, 2002).

The “microfinance schism” between advocates of “institutionalist” and “welfarist”, even if there are some crossovers among them, leads to various types of policy settings (Morduch, 2000; Bhatt and Tang, 2001). The two divisions of the institutionalist and welfarist approaches have practical inferences on differences in the devise for service delivery, institutional structures and financing, and segregation of the potential clients to be served (Woller and Woodworth, 2001). Their basic difference lies at focusing on the institutional sustainability on the part of institutionalists but social benefits of welfarists. Hence, institutionalists give main concern to the business, while welfarists focus on
clients. According to the welfarists, a change in the life of clients would be brought through the provision of both financial and non-financial services with the aid of subsidies (Bhatt and Tang, 2001). Subsidies, for institutionalists, are start-up fuels and finance new innovations in an effort to enhance efficiency to be sustainable (Morduch, 1999; Schreiner, 2002). Welfarists criticise that MFIs are urged to divert from their mission of serving the poorest of the poor in pursuit of sustainability (Brau and Woller, 2004).

2.6 FINANCIAL SUSTAINABILITY

Microfinance institutions’ sustainability has been defined in various ways by different authorities, however they all recognise the importance of the institution’s ability to cover its costs (Thapa, 2006). The existence of a myriad of measures or definitions of sustainability reflects in essence that the industry is maturing (Ledgerwood, 1999). During the early stages of microfinance movement, the sustainability of a microfinance institution was considered as its ability to cover its operating costs by its income, regardless of its source (ibid). This definition entails that, as long as the institution could attract enough donations to cover its expenses, it was considered financially viable. Later, sustainability was viewed in terms of the institution’s ability to generate enough income from the services it offers to cover its expenses (Ledgerwood, 2001). In other words, the operations of the MFI should be sustained by the revenue from its clients, rather than grants from the donors. Once an MFI operates at this level of sustainability, it becomes operational self-sufficiency (OSS). The Consultative Group to Assist the Poor [CGAP] (2006) defines OSS as the extent to which an MFI is able to create sufficient revenue to cover its costs. However, institutions that are operationally self-sufficiency do not charge high interest rates that are enough to cover for inflation and commercial costs of capital. This entails that they could only sustain their operations for some period of time without resorting to subsidies and donations, but they cannot sustain forever. Further, with this level of self-sufficiency, they can only attract a limited amount of commercial funding (Christen, 1997).

According to Morduch, (2000), a higher level of self-sufficiency can only be achieved when the institution is in a position to cover the costs of inflation and other non-cash expenses, as well as to operate entirely without subsidised inputs, that is, concessionary loans or grants. Any MFI operating at this level of sustainability is said to
be financially self-sufficient (FSS). In contrast to an MFI which is operationally self-sufficient, an MFI that is financially self-sufficient can sustain its operations without donations or subsidies since it is in a position to cover its costs of capital at market rates (Christen, 1997; Morduch, 2000).

Ledgerwood (2001); CGAP (2006), prescribes specific measures that can be used to calculate an institution’s self-sufficiency. The most used measures of sustainability are the Financial Self-Sufficiency ratio (FSS), Operational Self-Sufficiency ratio (OSS), and Subsidy Dependence Index (SDI). The FSS ratio is calculated using the following formula: \[ \text{FSS} = \frac{\text{adjusted financial revenue}}{\text{adjusted financial expenses} + \text{adjusted loan loss provisions} + \text{adjusted operating expenses}}. \] The OSS ratio is calculated using the following formula: \[ \text{OSS} = \frac{\text{operating income}}{\text{operating expenses} + \text{loan loss provisions}}. \] Another common measure that is used in addition to FSS and OSS is Return on Assets (ROA). According to Schaaf (2010) ROA relates profits to the size of the institution. In this regard ROA differs from the other cost-recovery measures, namely, OSS and FSS because it allows for comparisons between the profitability of microfinance as an investment with that of other possible investments. On the contrary, OSS and FSS are based on a donor mentality, that is, they indicate whether the target MFI is in need of more subsidies or not.

### 2.6.1 Increasing attention to financial performance

During the early 1970s, the existing microfinance initiatives were successful in ensuring high repayments rates and this trend was sustained into the late 1980s (Monzurul and Muhammad; 2011). This evidence shows that microfinance has a potential of reaching significant numbers of poor clients, who are able and willing to repay the loans and the costs of credit (ibid). According to Christen (1997), this led to a new realisation by donors of the significance of this industry thereby motivating them to increase their resources towards microfinance. Although microfinance has proved to be a solution to overcome the shortage of financial resources to the poor, (MFIs) are still typically unable to reap profits from their operations and as a result they have to rely heavily on subsidies (Wright, 2006).
The view that MFI’s sustainability is of critical importance did not receive much attention from the practitioners in the beginning of the microfinance movement. However, when the industry started to show signs of growth in the 1980s and 1990s, there was a paradigm shift as policymakers and donors started to advocate for MFIs self-sufficiency (Cull et al. 2007). The major factor was the increasing criticism for failed subsidised credit programs (Koveos, 2004). Armendáriz de Aghion and Morduch, 2005; Zeller and Johannsen, 2006 argues that the financial self-sufficiency is necessary condition for the development sustainable MFIs. International donor organisations and microfinance networks adopted this view and began to advocate for the sustainability ideology (Cull et al. 2007). The first and notable transformation from a non-profit MFI to a commercial bank was done by BancoSol, a Bolivian MFI (Bruck, 2006).

The evolution of the microfinance industry was also driven by the radical change in the services portfolio offered by MFIs. Ledgerwood, (2001), notes that the earlier microfinance programs of the 1970s were more focused on welfare projects that were heavily reliant on subsidies and donor grants. However, in the late 1980s the focus shifted towards the provision of diverse financial services. This shift was further given the impetus by the perception of some microfinance providers who viewed donor funding as only temporary given the unpredictability of donor periodical changes in priorities (Morduch 2000). As a way to mitigate against the perceived risk of ‘donor fatigue’, the MFIs shifted from being donor dependent towards commercialisation through mobilising commercial financing and mobilising resources from clients' savings (Christen, 1997; Ledgerwood, 2001). The need to access more commercial funds compelled many MFIs to be financially sustainable. This requirement led to the development of a ‘financial systems’ approach to microfinance. The success of this approach was premised on the institutionalist principle that poor people are able to pay high interest rates that cover the lender’s transaction costs (Ledgerwood, 2001; Robinson, 2001; Morduch 2000). By the mid-1990s, some leading programs had proven that commercial funding could be mobilised to serve poor customers and contribute to MFI’s institutional self-sufficiency (Christen, 1997).

In this, study the terms profitability, sustainability, financial self-sufficiency, financial sustainability and self-sufficiency are used interchangeably to refer to an institution’s sustainability.
2.7 OUTREACH

According to Conning (1999), outreach is the effort by microfinance institutions to extend loans and financial services to an ever-wider audience (breadth of outreach) and especially toward the poorest of the poor (depth of outreach). Navajas, Schreiner, Meyer, Gonzalez-Vega, and Rodriguez-Mega (2000) define outreach as the social value of the output of a microfinance organization in terms of depth, worth to users, cost to users, breadth, length, and scope. The definition by Conning (1999) is more appropriate for this study. It implicitly recognizes that microfinance institutions have a niche market, which is primarily the low-income section of the population, who have no or limited access to financial services from the traditional formal financial sector under free market-driven conditions.

There numerous indicators and measures of microfinance institutions outreach. In the past, the main measures of microfinance institutions’ depth of outreach in developing countries was the extent to which most policies of government are achieved. The concern at the time was more on outreach than sustainability (Schreiner, 2002). The result of these policies were assessed in terms of outreach, using measures such as the number of loans made, tons of fertiliser sold, number of tractors purchased, acres of land irrigated and of crops financed by loans, and number of cattle purchased. Adams and Fitchett (1992), for example, argue that these measures did not adequately capture the ultimate objectives of the stated policies. The recent recognition of microfinance institutions, the concept of outreach begun to be widely used in microfinance and other measures developed. Yaron (1992) further argues that the traditional quantifiable measures of institutional success based on profit presented in standard financial statements provide only partial, often meaningless information with respect to financial self-sustainability.

For this reason Yaron (1992) suggests alternative sets of measures that would be far more revealing not only in terms of actual cost of continued institutional operations, but the extent to which formal financial services are accessible to the low-income earners. These include: (i) the value of outstanding loan portfolio and the average value of loans extended, (ii) the number of borrowers, (iii) credit methodology, (iv) the number of branches and village posts/units, (v) percentage of the total rural population served, (vi)
the annual growth of microfinance institution assets over recent years in real terms, and (vii) women's participation. These measures have either been broadened, refined or categorised. Ledgerwood (1999) broadened outreach measures and classified them under three groups: (i) clients and staff outreach, (ii) loans outreach, and (iii) savings outreach. Under each of these groups, a number of specific measures were proposed to capture the extent to which the microfinance institution is reaching out to clients with its services, and whether or not the clients reached could be described as poor. One example of these measures used by Valenzuela (2002) is the number of active loans.

There have also been discussion on the worth, cost, breadth, scope and dimension of outreach in literature. These concepts stand to put clear usage and understanding to microfinance outreach. Following Schreiner (1999), the consensus in the microfinance industry appears to be that all the above proposed measures can be conveniently and exhaustively grouped into two categories: scale and depth of outreach. Similarly, Ledgerwood (1999) argues that currently most people in the microfinance industry refer to only two levels of self-sufficiency: operational self-sufficiency and financial self sufficiency. Ledgerwood (1999) further argues that the scale of outreach is a straightforward measure, but less nebulous than the depth of outreach, because it captures the total number of clients served by microfinance institutions without taking into account their poverty status. A more nebulous measure is one that captures the characteristics of the poor clients served. This argument, however, ignores the fact that it is not only the poor who are denied access to financial services in the formal financial sector. There are millions of non-poor people who are also denied access to financial services in the formal sector, those who can access financial services from the formal sector, leaving out mainly those who are unable and have to turn to microfinance institutions for financial services (Ledgerwood, 1999; Barres 2006). The depth of outreach, which is considered a more nebulous measure of outreach, is also very contentious because of its roots in poverty indicators.

Some authorities advocates for the use of loan size. The loan size assumes that only the poorest individuals are willing to take the smallest loans, and that wealthier individuals require larger ones (Christen, Rhyne and Vogel, 1995; Morduch, 2000; Fransico, 2001). This assertion is based on the view that people with small incomes have only sufficient cash flow to make very small debt service payments. Therefore, small loans will be closely related to low incomes (Christen et al., 1997). Armendáriz de
Aghion and Morduch (2005) suggests that loan size can be related to national income levels as way to differentiate between individual countries’ interpretations as a certain number of dollars can have varying meanings in different countries. In their study they propose a loan size less of than 20% of GDP per capita of a country as a poverty threshold. Cull et al. (2007) also supports this view on the basis that income distributions vary significantly from country to country, hence relating the loan size to the income of the poorest, for example, the poorest quintile can be even more helpful when making international outreach comparisons.

The use of such simple measures as average loan size as an indicator of an institution’s depth of outreach has received criticism (Hatch and Frederick, 1998; Schreiner, 2001; Wilson, 2011). The loan size proxy has however been criticised of being an exceedingly crude and inaccurate measure that fails to take into account other important aspects of the MFI’s business practices (ibid). For example, an MFI might choose to always disburse loans of the same size to first-time borrowers. In order to mitigate against this shortcomings of the loan size proxy, it is necessary to use additional information alongside loan sizes. However, as extensive data is often hard to find, loan size is still largely used in the study of microfinance.

**2.8 TRADE-OFFS BETWEEN MFI SELF-SUFFICIENCY AND DEPTH OF OUTREACH**

With the advent of commercialised microfinance, which also resulted in a number of NGOs MFIs being transformed into commercial banks, some pro-poor microfinance advocates have been sceptical about the ability of MFIs to sustain their original mission, which is offering financial services to the very poor and marginalised members of the community (Cull et al., 2007). This view by this particular section of microfinance practitioners, has resulted in an escalating debate on whether there are trade-offs between MFIs’ self-sufficiency and depth outreach, which could possibly lead to a mission drift. Cull et al. (2007) defines mission drift as a shift in the composition of new clients, or a re-orientation from poorer to wealthier clients in pursuit of financial sustainability. However, the term mission drift as measured by loan size should be interpreted with caution as it might be misconstrued with other similar phenomena. As an illustration, an MFI can experiencing a natural rise in loan size because the clients who have shown prudent repayment performance are able to reach larger loans.
because of progressive lending practices; and in successful microfinance programs the clients might have been able to develop and expand their businesses with earlier loans, which leads to increased income and also a need for larger loans (Cull et al., 2007; Armendáriz and Szafarz, 2009). As can be noted from this illustration, an MFI can be compelled to increase the loan size but this behaviour does not imply a mission drift. However, these similar occurrences can make it difficult to identify actual mission drift, and also accentuate the need to examine the depth of outreach more accurately than by using mere loan sizes (Hatch and Frederick, 1998; Schreiner, 2001; Wilson, 2011).

Some MFIs practitioners have however expressed their scepticism on whether mission drift is a justified concern given that some various discussions points to the fact that the poorest population has never been a target client group of microfinance, as they are considered less able to benefit from financial services as well (Hulme and Mosley, 1996; Morduch, 2000; Zeller and Johannsen, 2006).

The advocates of MFIs’ sustainability view those microfinance institutions that follow the principles of good banking as the best candidates for the alleviation of poverty. However, it can be revealed that this win-win proposition focuses on the importance of breadth of outreach rather than its depth. According to, Robinson (1995), many microfinance oriented organisations such as ACCION International, the Consultative Group to Assist the Poor [CGAP], the US Agency for International Development [USAID], UNCDF and the United Nations Development Programme [UNDP]) have also joined the debate advocating for the sustainability ideology. These organisations have advocated for subsidies to be limited to the start-up phase of microfinance institutions and pushing for a more commercial orientation once operational. On the other hand, the ‘poverty camp’ fears that the intensified advocacy towards MFIs’ financial sustainability would further widen the gap of financial exclusion for the poorest client. This “camp” view commercialisation of microfinance as a major factor that consequently lead to a major shift from the original mission of microfinance, that is sustainability promotes the breadth of outreach at the expense of depth (Morduch, 2000).

Aghion and Morduch (2005) summarize the differences between the sustainability and poverty camps concisely:
Those who oppose subsidisation tend to assume a relatively flat distribution of social weights, low sensitivity of credit demand to interest rates, positive impacts of interest rates on returns, very low returns to investments by poorer households, and negative externalities of subsidized credit programs on other lenders. Those who are open to strategic subsidization, on the other hand, tend to put greater social weight on consumption by the poor, assume highly sensitive credit demand to interest rates, low impacts (or perhaps negative impacts) of interest rates on returns, moderately high (but not extremely high) returns to investments by poor households and small or beneficial spillovers onto other lenders. (p.244)

Despite representing diverging views on MFI operations, the sustainability and poverty camps do however share something in common. The two camps both subscribe to the concept that the ultimate goal of microfinance is to provide financial services to the poor people who are otherwise excluded from them. This concept is premised on the fact that almost all MFIs, inclusive of those operating on operational or financial self-sufficiency, do have a social objective in addition to the economic. “…there is in fact only one objective, depth of outreach; sustainability is but the means to achieve it” (Rhyne, 1998: 7). According to Rhyne (1998), the only different between the two camps is only the perceptions on the means to deliver that goal that are different. Robinson (2001) also agrees with Rhyne (1998), when he emphasises that “Thousands of clients can be served through either method (sustainability or poverty-focused).

2.8.1 The problem with interest rates

The achievement of MFIs’ self-sufficiency, although it has been overemphasised by many practitioners, it has proved to be a very difficult target to attain in practise (Schicks, 2007). The current level of subsidies and donor grants in the industry is enough evidence that points to reality that most MFIs are still dependent (ibid). According to Koveos (2004), MFIs are still highly dependent on subsidies in spite of the recent innovations in lending methods and achievements in narrowing down organisational forms. He notes that there are exorbitant transaction costs associated with lending small amounts to many people as compared to lending large amounts to
just a few. In addition, Christen (1997) and Morduch (2000) also observes that microfinance by its nature, more often than not, extends credit to rural and poor areas, which is another factor that increases operating costs. These high transactional costs associated with lending to the poorest would inevitably compromise MFIs as they seek to attain self-sufficiency (ibid). In order to attain financial self-sufficiency, an MFI is faced with two options, either to adjust its income upwards, or to revise downwards its operational expenses or loan losses (Koveos, 2004). A Cull et al. (2007) studying a sample of 124 MFIs also finds that cost cutting measures play a critical role in determining the sustainability of the MFI, regardless of its lending methodology (individual or group contracts, or village banking).

Consistent with A Cull et al. (2007) and Koveos (2004), operational costs and loan losses can be reduced when an MFI adopts more efficient ways of operations. The Bancsol case offers a good example of an MFI which managed to successfully contain its administration costs through the development efficient and simpler ways of managing loan contracts, which resulted in reduced labour costs (Morduch, 2000).

Apart from reducing the operational costs, it is also essential for MFIs to come up with revenue generation strategies to ensure that the institution’s income is sufficient enough for it to be financially sustainable. In respect of microfinance, the most obvious source of income is the interest rate charged on loans advanced (Christen, 1997). The subject of adjusting the interest rates as a strategy to generate sufficient income for the achievement of financial self-sufficiency and the view that this would not affect the demand is a central claim in the proposition that “the poor are able to pay high interest rates, to the extent that higher interest rates would not curb demand” (Robnison, 2001). The proponents of this proposition argues that by charging higher interest rates, MFIs becomes less dependent on donations and subsidies and in addition they would be able to make profit which would allow them to access commercial lending (ibid). Christen et al. (1995) studying 11 leading MFIs finds that the most financially self-sufficient MFIs have managed to adjust their interest rates at levels that would fully recover costs, while those which are still subsidy dependent have kept their interest rates below the cost recovery level.
Although the subject of adjusting the interest rates has been advocated by some authorities such as Robnison (2001) and Christen et al. (1995), the view that the costs of borrowing must be subsidised because micro-borrowers are too poor to pay the full cost still prevailed. According to Morduch (2000), not all of the poor individuals have the capacity and willingness to pay these high interest rates. In to the views against the proposition that the poor are able to pay high interest rates, Stiglitz and Weiss (1981) make use of the theory of asymmetric information to argue against raising interest rates too high. Consistent with the theory of asymmetric information, charging of high interest rates can result to adverse selection and moral hazard problems (ibid). This entails that the high interest rates would screen out the most reliable borrowers and as a consequence, undermining the loan repayment rates (ibid). This claim has also been supported by Cull et al. (2007) when they finds out that if a typical microfinance lender increases interest rates, the increase is positively related with increased financial self-sufficiency, but only up to a certain point, which they call a “60% critical threshold”. An additional increase in interest rate beyond this threshold would result to a more than proportional decrease in demand and hence the financial self-sufficiency (ibid).

The argument that views the poor as relatively interest-insensitive is also countered by empirical evidence. Dehejia, Montgomery and Morduch (2005) analyse this assertion through an experiment of two operational branches of a credit cooperative in Dhaka, Bangladesh, with one branch unexpectedly changing its credit contract terms. They find out that the branch which had relaxed its interest rates recorded a significant number of new applicants. In contrast, the branch that had not changed its credit contract terms had no notable change in clientele base. They conclude that, poorer clients are indeed interest sensitive and they are willing to borrow at low rates. Karlan and Zinman (2007) also argues that interest rates are inversely related to loan demand. In their study, they find out that the take-up elasticity to the interest rate offered is -0.28 and when interest rates are raised above the standard rates, an increase in the rate offered decreased loan take-up by six times more than at standard rates.

As MFIs realise that they cannot easily raise interest rates without adversely affecting the loan demand, some started to implement alternative options aimed at subsidising the costs of small loans to the poorest clients by extending services to better-off clients. According to Morduch (1999), the principle behind the cross-subsidisation was
premised on the argument that by making a profit in the high-end services, the MFI can cross-subsidise between the poorer and wealthier clients, as the case with Grameen Bank.

2.8.2 Customers’ cost differentials

The cost differential between various microfinance clients is one of the major courses of the trade-off between MFI’s sustainability and the depth of outreach (Hao, 2002). Customers’ cost differentials is associated with the existence of two groups of clients, namely, the poorest; and moderately poor. The poorest clients are likely to default in repayments as compared to the moderately poor, and they are also likely to be illiterate and needs the assistance from credit agents when signing loan contracts, hence the cost of providing microfinance services to them becomes higher (ibid). This view has persuaded many MFIs to prefer serving the moderately poor since it is relatively it is easier and cheaper (Aubert, de Janvry and Sadoulet, 2009). Conning (1999) also support this view by arguing that the poorest customers require intense monitoring against the background of inadequate collateral, which increases the relative cost of lending to them. Further, Jaini (2009) cites that the transaction costs associated with smaller loans are much higher relative to costs for larger loans. In addition, Cull et al. (2007) finds that larger loans, that is, loans that are normally required by moderately poor clients, gives rise to lower average costs for individual lenders.

The cost differentials between these two groups of clients could therefore entail that those MFIs whose objectives is to serve the poorest segment of the society could have serious challenges in achieving self-sufficiency as compared to those MFIs focused on serving the moderately poor clients. Also in their later study, Cull et al. (2009) suggests that institutional characteristics, that is lending methodology and institutional type, can have a significant impact on the depth of outreach and financial sustainability. As an example, a financially unsustainable NGO MFI can achieve satisfactory depth of outreach compared to a financially sustainable microbank. This is because NGOs typically make use of group lending contracts rather than microbanks that charge higher interest rates. As a result smaller loan sizes in NGOs’ group lending schemes increase fixed costs per dollar lent, even though they are able to keep their total operational costs
down. In this sense, the social mission of reaching the poorest with small loans can be in contradiction with the pursuit of sustainability, and vice versa.

Chaia, Aparna, Tony, Maria, Jonathan and Robert (2010), suggests that customers’ cost differentials can also emanate from region-specific parameters, that is, the proportion of the poorest clients usually varies between rural and urban areas and between countries, resulting in different limits for the MFI’s outreach. The authors observe that there number of poorest microfinance clients in the South Asian countries is more than in Latin America. This, they explain, would have an impact on the cost to South Asian MFIs of reaching out to a large number of the very poor.

### 2.8.3 Empirical evidence of sustainability and depth of outreach trade-offs

There are a number of empirical studies that have been undertaken regarding the trade-offs between the MFIs’ sustainability and the depth of outreach. However, it seems that these studies still offers varying the conclusions equivalent to the same debate discussed in the theoretical analysis above.

Using a dataset of 124 leading MFIs in 49 countries, Cull et al. (2007) finds that some sampled institutions had achieved both satisfactory outreach depth as well as sustainability. The correlation between average loan size and sustainability measures was not statistically significant, that is the simple correlations for the whole sample did not provide evidence of mission drift. However, when sustainability and depth of outreach objectives were disaggregated by lending type, the study reveals a trade-off. The FSS and OSS were found to be on the higher side for individual lenders and lower for village banks. On the other hand, village banks performed better in depth of outreach than the individual lenders. Overally, Cull et al. (2007) finds no trade-off between MFI’s sustainability and the depth of outreach.

Reviewing the phases and driving forces of a shift towards achieving sustainability by MFIs in Latin America, Christen (2001) concludes that there is no compelling evidence that the push towards MFI’s sustainability leads to lower depth of outreach. His conclusion is however contradictory, because although it claims that there is no trade-off between depth of outreach and MFI sustainability, the same study accepts the
possibility that the MFIs tend to cut down the poorer clients once they transform into sustainable institutions.

Analysing 11 MFIs, with loan sizes ranging from 6% to 36% of GNP per capita, Christen et al. (1995) finds that interest rates rather than the loan size was the major determinant factor of sustainability, which reflected the commitment to achieve the goal of financial self-sufficiency. The conclusion the authors make reflects their position in the mission drift debate: “These results show no evidence of a direct trade-off between outreach, either deep or extensive, and financial sustainability. The two goals are clearly not in opposition.” (Ibid, 27).

It is however important to realise that the studies cited above used a very special data of MFIs which reports to a premier microfinance organisation, MIXmarket. Although the results from these studies proffer some empirical evidence with regards to the studying of depth of outreach and sustainability patterns in larger datasets, there is need to make cautious inferences using their findings as they hardly represent a generality of the entire microfinance industry. As an example, Christen et al. (1995), carefully chose a sample of MFIs explicitly based on their known record of outreach and self-sufficiency, thus, it is impractical to try and make some inferences on such a biased and small sample size. In this regard, the failure to observe any clear pattern with regards to the trade-off between depth of outreach and self-sufficiency in such a study can be simply attributed to the sample size rather than to the actual lack of any relationship. On the other hand, one of the major problems of a case study is that it also falls short to give a representative generalisation of the population due to the limited number of cases under study.

The other setback with the Cull et al. (2007); Christen (2001); Christen et al. (1995) is that they are not time sensitive, that is they are all static. In this regard they disregard time period which is one of the most important aspect when analysing mission drift. Mission drift by definition takes place over a period of time, hence the use of static data could not adequately capture its pattern. In this regard, although the analysis done for example by Cull et al. (2007) can proffer some important relationships between sustainability and depth of outreach, it is not possible to make some actual inferences with regards to the occurrence of mission drift. Mersland and Storm (2010); Olivares-
Polanco (2005); and Makame & Murinde (2006) address this problem by make use of a panel dataset.

Mersland and Strom (2010) using a panel data set of 379 MFIs from 74 countries, covering years 2001 through 2006. Unlike Cull et al. (2007), their analysis is not based on disaggregation by lending methodology. Using average costs per credit client as regressors, they concluded that cost efficiency is important in determining the depth of outreach.

Olivares-Polanco (2005) investigates the determinants of outreach in terms of the loan size of MFIs, using data for 28 MFIs in Latin America for the years 1999-2001. Using the simple Ordinary Least Squares method, the study confirms the existence of a trade-off between sustainability and depth of outreach. In a related study, Makame & Murinde (2006) analyse the outreach versus sustainability trade-off using a balanced panel dataset for 33 MFIs in five East African countries for the period 2000-2005. Using loan size as the proxy measure for the depth of outreach, they find strong evidence for a trade-off between depths of outreach and MFI’s sustainability.

CHAPTER SUMMARY

The chapter reviewed literature on MFIs sustainability and the depth of outreach. The literature looked at both theoretical and empirical of microfinance. The literature showed that there are two schools of thoughts on microfinance, namely, the institutionalist, and the, welfarist whose views are contradictory with regards to the impact of MFIs’ sustainability on the depth of outreach. The literature also revealed that there is a debate among various authorities on the impact of MFI’s sustainability and the depth of outreach.
CHAPTER THREE

METHODOLOGY

3.0 INTRODUCTION

This Chapter gives an overview of the study methodology used to collect data, analyse it and present the results. The population and sample selection for the study are also discussed. The chapter includes the research design, population, sample, data collection methods, data analysis strategy and ethical considerations.

3.1 RESEARCH DESIGN

Polit & Hungler (1999) defined the research design as an outline for conducting the study in such a way that maximum control will be exercised over factors that could interfere with validity of the research results. The study was conducted using a Survey Research Design where questionnaires were sent out to participating organisations. Denzin and Lincoln, (1994) defines surveys research as a systematic gathering of primary data through the use of structured questionnaire. According to James (1993), no single research design is more superior to others. In this regard many researchers use a combination of designs. Given the nature of the research problem and that information on MFIs’ outreach and financial performance could be only gathered from individual institutions since it not made public, the researcher selected this design as the most appropriate for this research. The method was also appropriate for the study because same type of information was collected from various MFIs. This quality allowed the researcher to have a standardised measurement.

3.1.1 Justification of the research design

The author selected the survey design because of the following advantages;

• Data can be standardised allowing for easy comparison.
• It allows for economical usage of large amount of data.
• It allows for more of the research.
Polit & Hungler (1999) however states the survey has the following disadvantages;

- It is time consuming in designing, pretesting and distributing the questionnaires.
- There is heavy reliance on questionnaires.
- Quantitative techniques make data collection narrow.

In an effort to mitigate the shortfalls of the survey, the author designed the questionnaire in such a way that data collection was not narrow through the use of more straight questions that is those questions that only allow the responded to be objective.

3.2 RESEARCH PHILOSOPHY

There are two major categories of the research philosophy, namely, positivism (quantitative) and phenomenology (qualitative) (Leedy, 1997). According to Keogh (1999), quantitative research involves use of numbers. On the other hand, qualitative research implies an emphasis on process and in depth understanding of perceived meanings, interpretations and behaviours (Denzin and Lincoln, 1994). This study is undertaken using a quantitative research paradigm. The quantitative approach was appropriate for this study because it is investigative in nature, that is it seeks establish whether is trade-off between MFIs sustainability and the depth of outreach. Deductions were made from the data available and graphs to explain some trends on the indicators of depth of in relationship to MFIs. The use of this approach also made the statistical analysis of data easy. It is important to note that quantitative approach can be used to test the predetermined proposition and produce generalised results. The researcher had proposition given in Chapter One.

3.2.1 Justification of the research philosophy

Positivism research methods were employed in this study in order to maintain objectivity. The use of questionnaires was done to gather numerical information the indicators of the depth of outreach. It was also used in order to minimise the costs.
3.3 TARGET POPULATION

According to Burns and Bush (1998), population refers to the aggregate of all cases under study as specified by the objective of the research. The target population for this study comprised of the total number of 172 MFIs registered by RBZ registered. This target population was considered to be appropriate for the study because unregistered MFIs do not usually keep correct and updated records and therefore may not provide the required data appropriate for the study.

3.4 SAMPLE

A sample is defined as a systematically and strategically selected set of the population with the objective of drawing conclusions about the population (Miller and Wilson, 1983). The research is based on a sample population of 35 MFIs composed of banking institutions MFIs, RBZ registered MFIs, credit unions, and development which were in operation at least by 2009.

3.5 SAMPLING METHODS

A non-probability sampling technique was used for this study in the form of purposive sampling technique was used in determining the sample size. Purposive sampling is a form of non-probability sampling where the researcher selected the sample in a deliberate and non-random fashion to achieve certain goals. With this type, the sample is "hand-picked" by the researcher (Polit & Hungler, 1999). The main goal of purposive sampling is to focus on particular characteristics of a population that are of interest, which will best enable you to answer your research questions (ibid). This sampling method was appropriate for this study because the researcher only wanted a sample of sustainable MFIs upon which the trade-off with the depth of outreach was investigated. Although there are marked differences in terms of ownership structure, market niches and strategies among the broad MFIs categories, some balance was ensured to capture the diversity. The sampling technique was also adopted after the researcher took into account that some MFIs were unwilling to provide information on their outreach and financial performance. In this regard, the researcher identified those MFIs who were likely to cooperate. Consideration of these factors consequently led to the selection of this method. If the researcher was to apply any other sampling technique, the study
could have lacked a true representation thus the research conclusions and recommendations could have been misleading.

3.6 DATA COLLECTION TECHNIQUES

3.6.1 Questionnaire

The researcher used a questionnaire to obtain data from the sample of MFIs. The A questionnaire was chosen as the most appropriate instrument for the study because of the following strengths:

- It enabled the researcher to gather quantitative information about the MFIs. Polit & Hungler (1999) suggested that a questionnaire is the appropriate research tool when gathering quantitative information that can be generalised to a whole population.
- The questionnaires are less subject to researcher bias (Walsh 2001), thus improving the reliability and validity of the study.
- The instrument was also used because it was appropriate for the study which required a wide range of information, and if any other tool was used, the researcher could not have borne the financial requirements.

However, the major weakness of the questionnaire was it was impersonal, that is, it provides no option for clarification of responses. For example the participant would only be required to provide the outreach summary without giving any explanation to the pattern of the observed changes in the outreach. In an effort to mitigate this weakness, the researcher included only relevant questions derived from the research objectives.

3.6.2 Covering letter

The researcher attached a covering letter to the questionnaire outlining the purpose of the survey and requesting the cooperation of the respondents. This decision was made after realising the importance of informing the respondents about the research objectives and research topic. A sample of the covering letter is attached as Appendix I.
3.6.3 Questionnaire construction and pilot testing

In constructing the questionnaire, the researcher made use of the research objectives, available literature and personal experiences. During various stages of construction, the resultant drafts were analysed and discussed with the research supervisor and other professionals. A first final draft was agreed and pre-tested at eight MFIs seeking comments and any suggested improvements. The pre-testing was in line with the suggestions of Polit and Hungler (1999) that content validity of a questionnaire represents the tool’s credibility. In addition, the pre-test also took into account the views of Parahoo (1997) who stated that pre testing helps ensure that the assessment tool is clear, unbiased and elicits the type of response required for the research, thus demonstrating the credibility of the tool and adding to the validity of data.

The major finding of the pre-testing was that all the MFIs were unwillingly to disclose their financial sustainability ratios. Since the knowledge of these ratios was critical in determining whether the MFI is sustainable or not, the author had to revise the questionnaire. The revised questionnaire did not require MFIs to state their financial sustainability ratios but only to indicate whether they are sustainable or not. Only the financially self-sufficient MFIs could proceed and complete the rest of the questionnaire. This did not affect the results of the study since the author was merely concerned with investigating the trade-off between MFI sustainability and depth of outreach, hence only a sample of sustainable MFIs was required.

3.6.4 Structure of the questionnaire

The questionnaire includes two sections. The first section outlines the instructions to the participants while the second section contains the questions. The sequencing of questions in the questions section is as follows: the institutional background; sustainability, depth of outreach indicators and type of collateral required. A sample of the questionnaire is attached as Appendix I.
3.7 DATA COLLECTION PROCEDURE

The research questionnaire was sent to the identified respondents by hand or through the e-mail. The questionnaire contained questions aimed at capturing data and information of interest to the researcher. The questionnaire consisting of both closed and opened ended questions was pre-tested by conducting a pilot survey on members of the sampling frame which has resulted in the elimination of ambiguities and clarification of certain questions. Responses were collected by hand or through the e-mail.

3.8 DATA ANALYSIS STRATEGY

The depth of outreach was measured based on four indicators as suggested by Yaron (1992): total number of borrowers, number of women clients, number of rural clients, total amount of group loans and types of collateral required. The data was grouped under various sections outlined on the questionnaire. The sections included in the analysis are, response rate, demographic, outreach, and loans activities. The study used quantitative method for data analysis because all the indicators of the depth of outreach could be measured numerically. The Microsoft Excel 2007 was used to perform data analysis. A template of the results was presented in the form graphs and charts for easy understanding and comparison over time. Finally, pie charts were also used to provide a pictorial illustration on responses from the questionnaires.

3.10 ETHICAL CONSIDERATIONS

There are ethical dilemmas that are faced by institutions in their day to day operations. As a result researchers need to exercise due care to ensure that the rights of institutions and individuals are safeguarded (Pollit and Hungler, 1999). Certain behaviours in research may cause harm to individuals, breach confidentiality, and introduce bias that are considered unethical in any profession. The researcher was therefore guided by the following ethical consideration:
3.10.1 Seeking consent

In any discipline it is considered unethical to collect information without the knowledge of participants and their expressed consent to participate. Informed consent implies that subjects are made adequately aware of the type of information the researcher want them to provide and why the information is being sought. In this regard, permission to conduct the study was sought and granted by all respondents.

3.10.2 Providing incentives

The researcher did not attempt to offer any form of incentive in order to obtain information from respondents. All the respondents participated in the research after having realised the importance of the study.

3.10.3 Possibility of causing harm

Some of the study's information requirements were sensitive, particularly the financial and outreach information. The researcher assured the participating MFIs that the data obtained will not be passed to third parties.

3.11 SUMMARY

This chapter has discussed the research design used in the study and the reasons for choosing the design. The chapter also discussed how research instruments were developed, methods of data collection, data entry, data processing and analysis explored how the researcher carried out the research the research design, how data was actually collected and the data analysis strategy. The findings and analysis of the results are discussed in the next chapter.
CHAPTER FOUR
RESULTS AND DISCUSSIONS

4.0 INTRODUCTION

The present chapter presents the study findings from data gathered through the research questionnaire. The findings of the study are compiled in a quantitative form and are linked to the reviewed literature for discussions. The approach implies the use of graphs to show the trend analysis and pie charts for pictorial illustrations of responses. The indicators of depth of outreach total number of borrowers, number of women clients, number of rural clients, total amount of group loans and types of collateral required.

4.1 RESPONSE RATE

As explained in the methodology, questionnaires were used in data collection. A total of fifty (50) questionnaires were sent to the sampled MFIs. Forty-five (45) questionnaires were successfully completed and returned to the researcher representing a 90% percent response rate. The response rate was high enough to warrant the validity and reliability of the research findings.

DEMOGRAPHIC ANALYSIS

4.2.1 Position of the respondent

Figure 4.1 represents the position of the participants to the research.
Figure 4.1 Positions of respondents

Figure 4.1 shows that 12% of the participants were general employees at the analyst’s level, 43% were managers, and 45% were managing directors. The results indicate that the majority of the participants were managers. Management constituted the highest number of participants because of the sensitiveness of the questions asked. The questionnaire required disclosure of some market sensitive information such as the type of products, number of clients, and the financial performance of the institution. This type of information can only be disclosed to outsiders at the discretion of management hence the majority of participants were from this category.

4.2.2 Experience of the respondents

Figure 4.2 represents the experience of the participants.
Figure 4.2 shows that 24% of the participants had an experience of between two and five years, 64% had an experience of between six and 10 years and 12% had an experience of above 10 years. This indicates that the majority of the respondents had experience of between six and ten years. The results shown by the above analysis implies the existence of a close linkage between experience and positions of the respondents. This is attributable to the fact that, experience is usually one of the major factors considered by institutions when recruiting managers. In most cases, a minimum of five years experience is usually the standard benchmark for managerial positions.

4.3 DEPTH OF OUTREACH

4.3.1 Total numbers of borrowers

Figure 4.3 represents the total number of borrowers for year the 2009, 2010 and 2011.

![Figure 4.3 Total numbers of borrowers](image)

Figure 4.3 shows that there was an increase of 221.25% in the number of borrowers from 2009 to 2010. Between 2010 and 2011, the number of borrowers increased by 74.5%. This indicates any increasing trend in the number of borrowers serviced by sustainable MFIs. However, the number of borrowers is increasing at a decreasing rate.

4.3.2 Number women clients

Figure 4.4 represents the number of women clients for the year 2009, 2010, and 2011.
Figure 4.4 Number of women clients

Analysis of Figure 4.4 reveal that in year 2009, 46% of the MFIs clients were women, in year 2010 they increased to 49% and in year 2011 they constituted the majority of 51%. The findings indicate that women are now the major clients of MFIs of sustainable.

4.3.3 Number of rural clients

Figure 4.4 shows the number of rural clients for the years 2009, 2010, and 2011.

Figure 4.5 Number of rural clients
Figure 4.5 reveals that of the total MFIs clients, 2% of them were located in rural areas in 2009, 15% were located in rural areas in 2010, and 19% were located in rural areas in 2011. The results indicate an increasing trend in the proportion of MFIs clients located in rural areas.

4.3.4 Amount of group loans

Figure 4.6 shows the total amount of group loans for the year 2009, 2010, and 2011.

![Figure 4.6 Total amounts of group loans](image)

Figure 4.6 shows that total amount of group loans increases by 389% between 2009 and 2010, and increased by 156% between year 2010 and 2011. This indicates an increasing trend in the number of group loans issued by MFIs.

4.3.5 Types of collateral required

Figure 4.7 shows kind of collateral required by institutions.
Figure 4.7 Types of collaterals required

Figure 4.7 shows that 60% of the collateral required is assets based while 40% constitute other forms of collaterals such as group and salary guarantees. The results indicate that asset collateral is the most commonly used form of collateral.

4.4 DISCUSSION OF RESULTS

The results above suggest that there is no trade-off between MFI’s sustainability and depth of outreach. What can be interpreted from these results is that there is no evidence to suggest that sustainable microfinance in Zimbabwe moving away from providing financial services to the poorest of the poor, that is, the sampled MFIs are still serving the very poor although they are operating self-sufficiently. The findings show that for period under study (2009-2011), the institutions have recorded any increasing depth of outreach as depicted by the increasing number of borrowers, increasing percentage of women clients, increasing number of rural clients, and the increasing amount of group loans.

These results are similar to those of Christen et al. (1995); Cull et al. (2007). Christen et al. (1995) analyzed 11 leading microfinance institutions and find no evidence of a direct trade-off between outreach, either deep or extensive, and financial viability. They conclude that the two goals are clearly not in opposition. Cull et al. (2007) using a
dataset of 124 MFIs in 49 countries find that some institutions in the sample have achieved both satisfactory depth of outreach as well as financial sustainability, and that simple correlations for the whole sample do not provide evidence of mission drift.

However, the results are in contrast with those of Olivares-Polanco (2005); Makame & Murinde (2006). Olivares-Polanco (2005); investigates the determinants of outreach in terms of the loan size of MFIs, using data for 28 MFIs in Latin America for the years 1999-2001. The study confirms the existence of a trade-off between sustainability and depth of outreach. In a related study, Makame and Murinde (2006) analyse the outreach versus sustainability trade-off using a balanced panel dataset for 33 MFIs in five East African countries for the period 2000-2005. They find strong evidence for a trade-off between depths of outreach and MFI's sustainability.

Even though the results from this study are similar to those of Christen et al. (1995); Cull et al. (2007) and contradict those of Olivares-Polanco (2005); Makame & Murinde (2006), the observed high depth of outreach recorded by sustainable MFIs may not be entirely attributed to their financial performance alone. The trend of depth of outreach indicators tends to be affected by other factors as discussed in the reviewed literature.

4.4.1 Total numbers of borrowers

The increase in the number of borrowers between 2009-2010 can also be attributed to the general improvement in market liquidity. The improved supply of funds, other things being constant, led to the fall of interest rates to the levels afforded by many poor and low income households resulting in increased number of borrowers. Lower interest rates have a positive effect on loan demand and thereby contribute to the increasing number of borrowers (Morduch, 2000). It is also critical to highlight that in pursuit of financial self-sufficiency, MFIs might have the incentive to shift their focus towards wealthier borrowers who can absorb larger loans, at the expense of outreach to the poorest clients (Cull et al., 2007). Finally, the phenomenal increase in the number of borrowers can also be attributed to the general increase in the salary levels of the low income group who constitute the largest proportion of the formally employed in the country. The salary increases allowed them to borrow as they could afford the repayments (Ghosh et al., 2000).
4.4.2 Number of women clients

The analysis of the results indicates that sustainable MFIs in Zimbabwe are increasingly focusing on providing financial services to women. Although these findings are similar to those of Cull et al. (2007), it is however suggested that they should be interpreted with caution. The enhanced access to financial services by women may also be linked to other factors other than MFIs’ financial self-sufficiency. Through microcredit, women can achieve multiple productive activities and diversify their sources of income more than men (Soulama, 2005). In this regard, sustainable MFIs might be targeting women not with the intention of empowering them but rather due their high loan repayment rates, hence less risk of default risk.

4.4.3 Number of rural clients

The observed increasing outreach in rural areas by financially self-sufficient MFIs may not be directly attributed to financial performance. The study by Sharman (2011) concludes that innovations in microfinance resulted in wider outreach and lower transaction costs and much lower risk costs. He cited the Self Help Group Approach (SHGs), Kissan Credit Card (KCC), and the use of Business Facilitators and Correspondents models as some of the outstanding innovations in India’s microfinance sector. These innovations increased MFIs rural outreach. The innovativeness rather their financial performance, might be the major driver of the increasing outreach to the rural clientele. These innovations are largely driven the human and social capital possessed by the poor, the economic policies of the country, and the quality of the financial infrastructure that supports financial transactions, for example reliable mobile network (Zeller and Meyer, 2002). An improvement in these aspects makes it easier for MFIs to reach the three objectives (ibid).

4.4.4 Total amounts of group loans

The results may indicate that the increasing trend in the number of group loans is largely driven by other factors other than MFIs’ sustainability. (Cull et al., 2009) indicates that financial sustainability can be influenced by different cost structures of the institutions. They show that NGOs who typically employ group-lending schemes have
higher fixed costs per dollar lent. In this sense, the social mission of reaching the poorest with group loans can be in contradiction with the pursuit of profitability, and vice versa.

However, Cull et al. (2007) suggest that MFIs stand to benefit substantially through higher loan recovery rate if they use group-lending method. There is evidence that the innovative group monitoring initiatives of the Grameen Bank and Bank Rakyat Indonesia models resulted in a more than 98% loan recovery rate supports this (Hossain, 1988; OECD, 1991; Monzurul and Muhammad, 2011; Robinson, 1995). In this regard, the need to achieve higher loan recovery rates might be the major contributing factor for the increasing trend of group lending other than the financial performance of the sampled institutions.

4.4.5 Types of collaterals required

The findings show that sustainable MFIs in Zimbabwe’s require asset collaterals. However, the average microfinance client does not have many assets, thus collateral is usually sought in the form of social capital (Monzurul and Muhammad, 2011). In this regard, the prevalence of asset collateral maybe attributed to the fact that the sustainable institutions would attempt to reduce their losses in the event of default as assets can be easily disposed. Conning (1999) also argues that the poorer the customer, the more monitoring effort and cost is needed because of their lack of collateral. In this regard, MFIs prefer asset collateral to reduce their relative cost, in order to remain financially sustainable.

4.6 SUMMARY

The chapter presented and discussed the research findings in relation to the reviewed literature. The findings presented and discussed include the demographic analysis, and depth of outreach indicators. The findings clearly show that microfinance could achieve both the depth of outreach and financial sustainability. The following chapter presents the conclusions and recommendations of the study.
CHAPTER FIVE

CONCLUSIONS AND RECOMMENDATION

5.0 INTRODUCTION

The chapter presents the major conclusions and recommendations of the study. These are drawn from the research findings in chapter four. Area of further research is also suggested in this chapter.

5.1 CONCLUSIONS

The research presents the following conclusions:

5.1.1 Total numbers of borrowers

The study concluded that sustainable microfinance institutions are associated with the increased the number of borrowers, thus indicating high depth of outreach. However, given the liquidity challenges that the country has faced over the years, it was found out and concluded that other factors such as lower interest rates and general increase of disposable income have also contributed to the increased number of borrowers.

5.1.2 Number of women clients

The study found out that women are now the dominant MFI clients. This shows that in their pursuit of sustainability MFIs have not drifted away from serving this segment of the financially excluded. It was therefore concluded that MFIs could attain long term sustainability, if they increase their focus on providing financial services to women. This is against the background that women can achieve multiple productive activities and diversify their sources of income more than men, hence less risk of default risk.

5.1.3 Number of rural clients

The research concluded that sustainable MFIs have not changed their mission of serving the rural poor. However, financial sustainability was not the only factor that led
to increasing outreach in rural areas. The study also concludes that other factors such as innovations can also have a significant impact in wider outreach for the rural clients, that is, the innovativeness rather the financial performance of MFIs, was the major driver of the increasing outreach to the rural clientele.

5.1.4 Total amounts of group loans

It was found out that sustainable MFIs are increasingly advancing group loans to their clients. The study concluded that, in order to remain sustainable MFIs use group as a way of attaining higher loan recovery rate from their poorest clientele.

5.1.5 Types of collaterals required

The study established that sustainable MFIs in Zimbabwe prefer asset collaterals as compared to other forms of collaterals. The study therefore concluded that asset collateral reduce MFIs losses in the event of default as assets can be easily disposed, that is, in order to remain financially sustainable, they need to mitigate against default risk.

5.1 PROPOSITION TESTING

The proposition that sustainable MFIs have a lower depth of outreach, that is, they drift from their mission of providing financial services to the poorest and prefer to services the moderately poor households is not adopted basing on the conclusion given in this study.

5.3 RECOMMENDATIONS

In order to enhance the capacity of MFIs in promoting financial inclusion in Zimbabwe, the following recommendations were proposed;

It is recommended that government should review MFIs licences to allow them to mobilise deposits which have a potential to become a major and sustainable source of funding as opposed to the commercial loans. In addition, the government should also review the Moneylending and Rates of Interest Act that controls interest rates. If the Act
is reviewed and MFIs allowed to set market interest rates commensurate with the transaction cost of servicing the rural areas, the financial inclusion goal would be attained.

The study also recommends that government and donors should avail cheaper funds towards lending to the targeted poor who are engaged in agricultural activities. This is critical because agriculture is the major income generating activity for the majority of the poor household. MFIs are hesitant to extent significant loans in this sector because of the high risk associated with weather uncertainties that ultimately affect the cash flows of the clients.

The government should proactively promote financial inclusion by offering fiscal incentives to MFIs to that operate exclusively in rural areas. The incentives can be in the form of tax reliefs and subsidised lines of credits.

It is also recommended that MFIs should be innovative in order to achieve a significant depth of outreach. As more numbers of people in rural and economically marginalised areas begins to have access to the mobile internet, technology can be used to promote financial inclusion. Further, MFIs should enter into strategic alliance with formal banks in order to have access to their infrastructure which is critical for online transactions. The use of online methods of payment and receipting can reduce the transaction costs involved in servicing the remote areas.

With regards to loan products, it is recommended that MFIs should issue small, short-term and repeat loans and gradually build to larger amounts as relationship with clients becomes stronger. This would lower the risk exposed to MFIs in the event of default by clients.

MFIs should emphasise on lending strategies that would allow the poorest households without asset collateral to have access to loans for income generating activities. In coming up with these strategies, lessons from the successful MFIs such as Grameen bank should be utilised.
5.3 AREA OF FURTHER STUDY

It is suggested that a further study in the same field be undertaken to assess the role of government in the promotion of financial inclusion.
REFERENCES


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APPENDIX I: LETTER OF INTRODUCTION AND QUESTIONNAIRE

The SERA
First floor, Cecil House
95 Jason Moyo Avenue, Harare
0712 876210

30 August 2012

To whom it may concern

Dear Sir/Madam

RE: QUESTIONNAIRE COMPLETION ON MICROFINANCE SUSTAINABILITY AND OUTREACH

My name is Tafara Matanga (R016240T) and I kindly seek your assistance in the completion of my questionnaire. I am a University of Zimbabwe Graduate School of Management (U.Z. G.S.M) student and as part of the requirements of the institution for the completion of the Master of Business Administration program, I am carrying out a research entitled; Investigating the Trade-off Between Microfinance Sustainability and the Depth of Outreach: A case of Zimbabwe Microfinance Institutions. It is against this background that I kindly seek your opinions by completing the attached questionnaire.

Please feel free to say out your honest opinion and I assure you that all the information you provide will be treated in strict confidence. For any clarifications, please contact me on the details provided above.

Yours sincerely

Tafara Matanga
G.S.M STUDENT
QUESTIONNAIRE FOR MICROFINANCE INSTITUTIONS

Instructions

a) Please respond to all questions

b) Respond by ticking the applicable in questions where responses are provided and briefly explain where spaces are provided

c) Please note that all your responses will be treated with strict confidence and the study will be used for academic purposes only

SECTION A: DEMOGRAPHIC INFORMATION

1. Name of Institution _____________________________________________

2. Position of respondent __________________________________________

3. Type of institution

   a) NGO [ ]
   b) Private microfinance institution (Non bank) [ ]
   c) Bank microfinance unit [ ]
   d) Savings and credit co-operative [ ]
   e) Other (Specify) ...........................................................

SECTION B : SUSTAINABILITY

4. Is your institution sustainable, that (Operating income/Operating expenses) is equal or greater than 1.

   a. Yes [ ]
   b. No [ ]

*NB* You can only proceed and fill the questionnaire, if the answer to this question is yes
SECTION C: DEPTH OF OUTREACH DATA

5. Please complete the following table as accurate and exhaustive as possible.

<table>
<thead>
<tr>
<th></th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
</tr>
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<tbody>
<tr>
<td>Total number of borrowers for the year</td>
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<td></td>
<td></td>
</tr>
<tr>
<td>Percent of women clients</td>
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<td></td>
<td></td>
</tr>
<tr>
<td>Percent of rural clients</td>
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<td></td>
<td></td>
</tr>
<tr>
<td>Amount of group loans</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

SECTION D: Collateral Required

6. What kind of collateral do you require?

   a. Asset collateral [ ]
   
   b. Other forms of collateral [ ]

END OF QUESTIONNAIRE

Thank you for your time