AN ANALYSIS OF THE CHALLENGES OF THE MICROFINANCE INDUSTRY IN MALAWI WITH A FOCUS ON ITS SUPPLY-SIDE

MASTER OF BUSINESS ADMINISTRATION DISSERTATION

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MASTER OF BUSINESS ADMINISTRATION DISSERTATION

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Submitted to the Department of Management Studies, Faculty of Commerce, in partial fulfilment of the requirements for the award of the degree of Master of Business Administration (MBA)

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DECLARATION

I, Kisa-Mwelefu Kalolokesya, declare that this research report is my own, unaided work. It is submitted in partial fulfilment of the requirements for the degree, Master of Business Administration at University of Malawi, The Polytechnic. It has not, either in whole or in part, been submitted before for any degree or examination in this, or any other university.

Signature : ………………………………….

Date : ……/………/2017

CERTIFICATE OF APPROVAL

We, the undersigned, certify that we have read and hereby recommend for acceptance by the University of Malawi a thesis entitled '*An Analysis of the Challenges of the Microfinance Industry in Malawi with Focus on its Supply-Side'*.

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DEDICATION

To my dad, Douglas and mum, Roseby, who gave me the love of life;

To my wife, Mirriam-Atuswile, who gave me a life to love;

To my daughters, Kimi-Wangu Elizabeth & Miki-Witu Keziah, who give me joy and meaning to my accomplishments;

And to the memory of my late sister, Bahati, who was a natural leader & source of inspiration.

To my only brother, Ipyana, and my four sisters, Njema, Lughano, Anganile & Ofwa, for the moral support.

To all relatives and friends; you have been wonderful.

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May God Bless You All!

ABSTRACT

The research study was carried out in order to analyse the challenges of the microfinance industry in Malawi with a focus on its supply-side. The specific objectives were to; determine the prevailing challenges affecting micro-financing by attempting to; identify the challenges disturbing the industry and generate possible solutions to mitigate the challenges. The afore-mentioned background prompted this research study to be commissioned to analyse the status quo and eventually provide solutions that can lead to the sustainability and growth of the industry.

The study employed an exploratory and a descriptive research design. The target population was all registered and licensed Microfinance Institutions (MFIs) in Malawi totalling 25. In each MFI 3 key managers were targeted. A mixture of Purposive and Convenience sampling was used to determine the sample. This study used both primary and secondary sources of collecting data. Primary data was collected using self-administered questionnaires which were e-mailed, and in some cases, hand delivered to the MFIs. Secondary Data was collected from industry performance reports from 2013 to 2015.

The results of the study exposed that lack of adequate capital, weak legislation and regulatory framework are the severe challenges distressing the growth of the industry. Moderate challenges included; collections, unreliable infrastructure, Information Communication Technology (ICT), theft by staff, double-dipping by customers, customer retention, higher lending rates, Know Your Customers (KYC), education level of customers and staff, high operational costs, poor customer care. Attributes worth noting were; MFIs raise capital through private equity only which is not sufficient, the Portfolio at Risk (PAR) drastically increased to 152% in 2015, the volume of loans declined by 31% in 2015, incapacitated ICT cannot propel increase on coverage and outlets as most MFIs have less than 4 branches and they only cover less than 4 districts.

Some of the suggested solution to the MFIs' situation and its challenges are; availability of soft loans from Government of Malawi (GoM) through Reserve Bank of Malawi (RBM), accessible by registered and licenced MFIs, strengthening the current Financial Services Act (2010) to criminalize defaulters, inculcate the spirit of micro-financing in both staff and customer through training and sensitization initiatives.

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GLOSSARY ACRONYMS AND ABBREVIATIONS

ADD	Agriculture Development Division
APIP	Agricultural Productivity Investment Programme
BCIs	Business Credit Institutions
BRAC	Building Resources Across Communities in Bangladesh
CLB	Central Loans Board
FIs	Financial Institutions
FS	Financial Services
GB	Grameen Bank
GoM	Government of Malawi
LDC	Less Developed Countries
MAMN	Malawi Microfinance Network
MCAs	Microcredit Agencies
MF	Microfinance
MFIs	Microfinance Institutions
MMF	Malawi Mudzi Fund
MRFC	Malawi Rural Finance Company
MSB	Malawi Savings Bank
NDTMFIs	Non-Deposit Taking Microfinance Institutions
NLB	Nyasaland Loans Board
NRDP	National Rural Development Programs
PCIs	Personal Credit Institutions
PAR	Portfolio at Risk
SACAs	Smallholder Agriculture Credit Administration
SACCOs	Savings and Credit Cooperatives Societies
SFIs	Sales Credit Institutions

USAID	United States Agency for International Development

CHAPTER 1-INTRODUCTION

1.1 Background to the Study

Microfinance Act (2010) defines Microfinance Institutions (MFIs) as a licensed provider of Financial Services (FS), to small or micro enterprises, low-income customers, financially undeserved customers including the following-microcredit, deposit-taking, micro-insurance, micro-leasing, transfer and payment services (e-money). The microfinance service provider includes the Microcredit Agencies (MCAs), MFIs or any other licensed Financial Institution (FI) that have been granted approval to offer financial services by the Registrar.

Microfinance services in Malawi have existed for over 50 years, before gaining independence. According to Chirwa (2002) credit outside the formal and informal financial system in Malawi pre-dates the colonial era. In 1958 the Nyasaland African Loans Board (NLB) was established to offer cash or in kind (seeds and fertilizer) to Malawian farmers. In 1964, the Central Loans Board with a secretariat in the Ministry of Finance superseded the Nyasaland African Loans Board. The launching of four Agricultural Development Projects in 1968 and the National Rural Development Programme (NRDP) that led to the creation of Agricultural Development Divisions (ADDs) in 1978 provided the conduit for extending the credit facilities nation-wide as a way of improving agricultural productivity through the provision of input loans. It is within this framework that the Smallholder Agricultural Credit Administration (SACA) was created in the Ministry of Agriculture in 1987.

SACA lending facilities were based on farmers' clubs with an average of twenty-six members with the joint liability concept supplemented by a security fund governing the *modus operandi* of financial services (Buckley, 1996). The SACA was affected negatively by loan repayment defaults because of changes in political landscape from 1992 to 1994 which ushered in democracy. Exit SACA, which was also assumed to focus on better-off farmer, enter Malawi Mudzi Fund (MMF) in 1989 which was to address the credit needs of the rural poor and core poor. However, the coverage of its programs was limited to both its pilot nature and focus on women groups only (Nyanda, Chirwa, & Jones, 1995).

Therefore, the activities of MMF lasted until 1994 and its operations were integrated into a new institution, the Malawi Rural Finance Company (MRFC) as a Mudzi Rural Financial Services Project (MRFSP) in 1995 (Chirwa, 2002). MRFC, now defunct, predominantly offered agricultural credit and state controlled Malawi Savings Bank (MSB), now privately owned, offered both micro-savings and credit. The two parastatals held more than 80 per cent of the microfinance market till the mid-2000. The failure of MRFC gave birth to Agricultural Productivity Investment Program (APIP) which supported the objective of developing a successful credit-in-kind system that could be used as a model to further develop sustainable rural micro-credit schemes. The credit had serious problems regarding default of some major service providers and the slowly delivery caused by beauracratic set-up and was not sustainable (Clifton et al., 2011).

Literature from similar research studies conducted elsewhere, particularly in Ghana, Kenya, Republic of South Africa, Tanzania, just to mention a few countries, has documented a plethora of challenges related to microfinancing. For instance, Boateng (2015) in his examination of microfinancing in Ghana discovered that the key constraints faced by MFIs in Ghana include poor regulatory environment, regular vicissitudes in government policies, paucity of capital, inadequate skills and professionalism, infrastructural inadequacies, socio-cultural misconceptions, corruption, frauds and forgeries and poor corporate governance. The common denominator on the variables is that they have a great impact on the sustainability and profitability of the MFIs.

What is visible is that the microfinance industry in Malawi has been going through a series of evolutions because of myriad challenges affecting sustainability of operations. Therefore, the fundamental point for this research study was to augment knowledge to a specialized area of barat that microfinance institutions are playing a vital role in provision of alternative source of finance to many unbanked people. The global figures are indicative that the number of customers reached out to as at 2007 were 155 million with over 3,000 MFIs in operation (Armendáriz & Morduch, 2010). However, Malawi is burdened by a poor microfinance supply culture created by years of market distortions propagated by public sector involvement in microfinance and supported by donors (Loboyeski, Bagchi, & Chawinga, 2004). Therefore, as the industry metamorphizes, particularly, with the entry of more privately-owned MFIs, it was imperative that a study be commissioned to identify and assess the challenges affecting micro-financing.

1.2 Aim of the Study

The main aim of the study was to analyse the challenges of the microfinance industry in Malawi with a focus on its supply-side.

1.3 Specific Objectives of the Study

The objectives of the study were: -

a) To determine the prevailing performance of MFIs in Malawi based on industry reports.
b) To identify the challenges that the MFIs are facing in Malawi when extending financial services to their customers.
c) To generate solutions to alleviate the established challenges affecting MFI operations in Malawi.

1.4 Research Questions

The study attempted to address the following questions: -

a) What is the prevailing performance of MFIs in Malawi?
b) What are the challenges that the MFIs are facing in Malawi when extending financial services to their customers?
c) What would be the possible solutions to mitigate the established challenges affecting MFIs operations in Malawi?

1.5 Significance of the Study

The study was of importance as it would contribute to the existing body of knowledge and it identifies an existing gap in challenges being faced by privately-run MFIs. The added knowledge would add value to both existing and prospective investors who will have a greater understanding of industry challenges from the supply-side perspective.

The research study has also unearthed area(s) for further research in the field of microfinance in Malawi.

1.6 Chapter Summary

Chapter 1 provides the introduction, background, problem statement, research questions, objectives, significance, limitations and outline of the research report. Chapter 2 provides the literature review fundamentals of microfinance with a specific focus on the supply side. The chapter will also provide a detailed analysis on the background of Malawian MFIs and their operational challenges through to evolution. Chapter 3 provides background regarding the broad methodology, research design and research report activity plan and its budget. Chapter 4 provides a discussion on report findings based on data analysis presentation. Chapter 5 summarises the findings of the research report with a conclusion, and lastly, it also offers some recommendations for the industry and areas for future research.

CHAPTER 2-LITERATURE REVIEW

2.1 Introduction

The literature review has defined the MFIs, their evolution, growth and coverage of their MF industry and finally concluding the chapter with challenges faced by the industry and their mitigating strategies.

2.2 Definition of MFIs

According to Saunders & Cornett (2014) there are three major types of finance companies, and these are; Sales Finance Institution (SFIs), Personal Credit Institutions (PCIs) and Business Credit Institutions (BCIs). Under the stated categories the Microfinance Institutions (MFIs) are considered to be under PCIs. Saunders & Cornett (2014) define the PCIs as a specialized classification in making instalments and other loans to consumers. Under this context, personal credit institutions will make loans to customers that depository institutions will find too risky to lend to (due to low income or a bad credit history). These institutions compensate for the additional risk by charging higher interest rates than depository institutions and/or accepting collateral (e.g., used cars) that depository institutions do not find acceptable (Saunders & Cornett, 2014).

Various authors or authorities have defined MFIs using their corresponding contexts. It is in this regard that to generate reasonable understanding of MFIs, notable definitions have been outlined and a fitting definition for this study was adopted. In Malawi, Microfinance Act (2010) defines MFI as a licensed provider of FS to small or micro enterprises, low-income customers, financially undeserved customers including the following-microcredit, deposit-taking, micro-insurance, micro-leasing, transfer and payment services (e-money). The microfinance service provider includes the MCA, MFIs or any other licensed FI that have been granted approval to offer financial services by the registrar. Ledgerwood (1999) imposes that MF has evolved as an economic development approach intended to benefit low-income women and men. The term refers to the provision of financial services to low-income clients, including the self-employed.

Robinson (2001) refers MF to small-scale financial services—primarily credit and savings—provided to people who farm or fish or herd; who operate small enterprises or microenterprises where goods are produced, recycled, repaired, or sold and provide services; who work for wages or commissions; who gain income from renting out small amounts of land, vehicles, draft animals, or machinery and tools; and to other individuals and groups at the local levels of developing countries, both rural and urban.

Burritt (2006) views MF as provision of the financial and non-financial services to those not included in the formal sector based not only on wealth but also social, cultural and gender barriers. Silvia & Molz (2005) refers MF to the provision of FS to low income entrepreneurs. Silvia & Molz, (2005) share Burritt (2006) understanding that MFIs are hybrid organizations characterized by their combining commercial and social goals.

Bogan, Johnson, & Mhlanga (2007) definition is not far from Burritt (2006) only that they offer a broader and comprehensive picture of the mandate of MFIs and how they are distinctive to MCAs. To begin with, their definition agrees with the basic tenet that MF offers FS to low-income households in developing countries around the world. Bogan et al. (2007) also emphasizes that in the minds of many, microfinance and micro-credit are synonymous. However, microfinance refers to an array of FS that include credit, savings, and insurance while micro-credit is the provision of credit which is usually used as capital for small business development. MFIs can operate as Non-Governmental Organizations (NGOs), credit unions, nonbank financial intermediaries or commercial banks. To cushion themselves from perceived risks due to the target client's lack of collateral as a guarantee against default, MFIs are known to charge very high (30% - 60%) nominal interest rates. The loans are short-term, the average loan size is very small, and only a few programs require borrowers to put up collateral. (e.g., Loans can be as small as $75, repaid over 1 year).

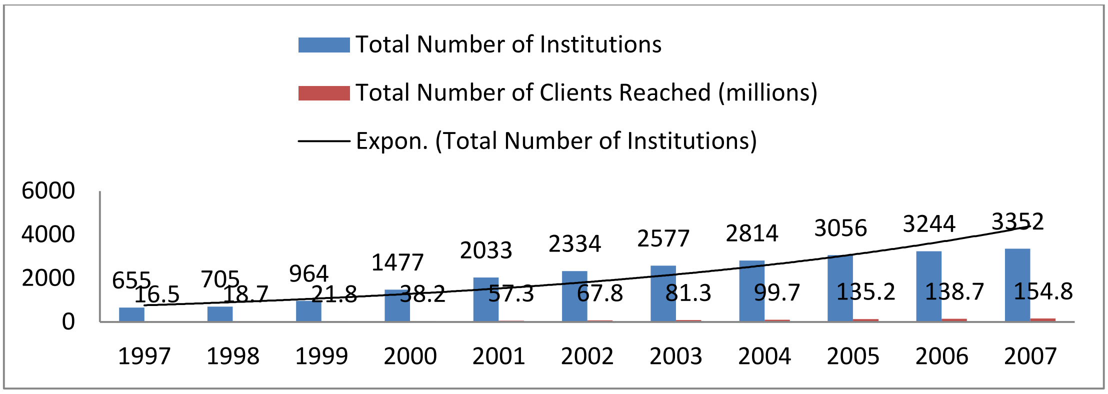
In more or less similar fashion to Burritt (2006) and the Microfinance Act (2010) concept of MF; Nwanyanwu (2011) refers MF to the activity of provision of FS to clients who are excluded from the traditional financial system on account of their lower economic status. They both agree that FS will mostly be in form of loans and savings through some MFI who will offer other services such as insurance and payment services. However, Nwanyanwu (2011) goes a step further to describe three features that distinguish MF from other formal financial sector. They are; the smallness of loans advanced, the absence of collateral and simplicity of the operation. However, for this research study the definition provided by the Microfinance Act (2010) was applied as the standard since it provides a legal persona of the industry.

2.3 Microfinance Evolution

Armendáriz & Morduch (2010) assert that one of the most important departures has involved a shift from “microcredit” –which refers specifically to small loans-to “microfinance”. The broader term embraces efforts to collect savings from low-income households, to provide insurance (“microinsurance”) and, in some places, to also help in distribution and marketing client’s output. In order to generate proper understanding and knowledge of the evolution of microfinance Armendáriz & Morduch (2010) argue that the terms microcredit and microfinance have to be implicit.

According to Mendoza & Vick (2010) the past 30 years or so have seen microfinance take off from small group-based lending experiments to several thousand MFIs serving a growing proportion of the developing world today. Nevertheless, the challenge is to improve broad-based access to FS remains going beyond credit and into other products such as savings, insurance, and money transfer services. What is very perceptible is how the MFIs have grown over the years as reported by Daley-Harris (2009) in Microcredit Campaign Report between the years 1997 to 2007. Expectedly, the demand-side of financial services, globally, shows strong correlation with the increased numbers of MF service providers coupled with increased customer uptakes confirmed in Figure 1.

Therefore, the Figure 1 demonstrates that at global level, the demand for microfinance services is on the growth spurt both in terms of customer recruitment numbers and the entry of new MFIs on the market.



Source: Armendáriz & Morduch (2010)

Figure 1 Growth of Microfinance Coverage

According to Lützenkirchen & Weistroffer (2012) for a long time it seemed the microfinance could accomplish social and financial goals simultaneously and without friction. The number of clients climbed steadily, while microfinance became increasingly commercialized and transformed into a more and more financially efficient industry. Sustainability of the industry was rarely questioned during the time. However, they argue that following the international financial crisis and global recession, MF experienced its major setback in 2008. Asset growth slowed markedly, profitability declined and portfolio risk rose.

Lützenkirchen & Weistroffer (2012) conclude that despite all the problems, microfinance continue to grow and managed to remain a profitable business, at least when considering the global aggregate. These sentiments are echoed by Boateng (2015) who touts that there are over 435 licensed MFIs in Ghana alone.

2.4 Challenges of MFI Operations

Abed & Matin (2007) assert that inclusive microfinance is the new mantra, where focus is not only limited to new financial products, but also designing socio-economic processes that create strategic linkages with microfinance. Because the various hitherto un-served groups face different constraints, they may require a wider set of introductory non-microfinance interventions so they can make the best use of microfinance itself. The key challenges here involve packaging and sequencing. Another is how to develop appropriate incentives and management systems that do not distort the process, but instead create synergies. Building Resources Across Communities in Bangladesh (BRAC) has long realized how hard it is to address the needs of the extreme poor using conventional microfinance. In Bangladesh, where outreach to the poor and the poorest has had the greatest influence in shaping the discourse on microfinance, evidence suggests that about 15% of all microfinance clients are among the very poorest (Abed & Matin, 2007). This position is supported by Henry, Sharma, Lapenu, & Zeller (2003) who suggest that MF industry promotes the dual objectives of sustainability of services and outreach to the very poor. This is corroborated by The Consultative Group to Assist the Poor (CGAP) which is committed to similar twin objectives of increasing the financial sustainability of MFIs and deepening their poverty focus—that is, increasing their outreach and impact on the lives of poorer people (Henry et al., 2003).

Additionally, Abed & Matin (2007) established most of the micro and small entrepreneurs operate in the market's informal segment, and lack the kinds of formal documentation that conventional financial institutions typically use for appraisals. These entrepreneurs have little or no access to traditional mechanisms of loan enforcement. Anyone appraising the potential to grow and repay loans has to take the person's financial abilities into account using innovative means, but must also take on social tasks that conventional bank representatives are often not suited to do well. These sentiments are substantiated by Goldberg & Palladini (2010) who suggests that internally determined risk factors include hiring policies, incentive systems, operating policies and procedures, employee evaluations, management information systems and reports, asset and liability management, currency management (hedging), and internal controls and audits.

In African context, another challenge identified to militate against the performance of MFIs is limited support for human and institutional capacity building. The paucity of human capacity in the microfinance sub-sector in Ghana has been an issue. According to Boateng (2015), one of the major problems of the microfinance sub-sector is recruitment of effective and appropriate manpower. This they ascribed to the inability of the sector to adequately compensate personnel. On the same, other human resource problems faced by microfinance institutions include lack of training opportunities and poor conditions of service. The quality of manpower in these institutions is reflected in the poor performance of many of them, inefficiency and high levels of frauds and forgeries. The institutions also suffer from high labour turnover a further indication of low staff motivation and poor personnel practices (Boateng, 2015).

For providers of official remittances, a major constraint is their lack of an outreach network, especially in the rural areas, home to a large majority of those who receive the remittances. This is where microfinance institutions like BRAC, with its network of over 2,000 rural branches, can play a significant role, and it has now partnered with BRAC Bank, a full-service commercial bank. As Bangladesh has no official identification system, one key problem is identifying the beneficiary, which increases transaction costs for both the financial institution and the beneficiary. But BRAC could use its local knowledge; it carried out a survey to register close to 100,000 beneficiaries, providing them with a registration card, unique registration number, and remittance passbook. Through an intranet, the BRAC Bank Head Office in Dhaka is connected with all the branch offices; it can send transfer advice to the relevant branch office overnight. The registered beneficiary comes to the branch office with card and passbook, fills in a withdrawal slip, and gets the money within minutes (Abed & Matin, 2007).

Extending the argument, Goldberg & Palladini (2010) alludes that lack of proper identification can lead to adverse client selection occurs when the MFI agrees to loan funds to a risky client because of incomplete information. Adverse selection can lead to a decline in the quality of the portfolio because the high-risk clients cannot or will not repay the loans. Adverse selection can also lead to moral hazard, which is the possibility that clients who know that they are fully protected from risk will act less responsibly and more speculatively than if they were fully exposed to the consequences of risk taking.

However, not limited to the issue of identification, for Ghana MFIs that operates small branches/agencies which are physically linked by weak transportation and communications infrastructure or susu operators that have several field staff or “mobile bankers”, monitoring branch/agency activities or field officers’ activities to prevent internal fraud and theft is a major challenge. This a clear manifestation that the concept of BRACS in managing its network to counter moral hazards is absent in African context. This challenge has resulted in several fraud cases where field officers under record the actual deposits or repayments of their clients and in some cases, abscond with deposits collected. MFIs with such challenges most often gloss over them. Supervisors and managers of such MFIs most often do not undertake random visits with their field officers to interact with some of its customers and to verify their deposits in the case of Susu clients and the repayment of loans. This is because of MFIs inability to develop an attractive incentive package system to enable it to attract well qualified and motivated staff to support its operations. Inadequate supervision and non-monitoring coupled with poor record keeping contribute to the perpetuation of fraud and cash theft. Another potential problem is a chance that staff with bad track record in one MFI can be recruited to other MFIs and in time will create problems in the new MFI (Boateng, 2015).

Battilana & Dorado (2010:1424) describe collections as the worst part of the job. As a Los Andes' loan officer noted:

> *"It is very hard when you are collecting on a loan and they have put the family sofas and the TV as warranty and you come to pick them up and the kids are crying" (field notes)."*

In addition, Boateng (2015) advances that loan default is a major threat to MFIs' sustainability and growth, it is the deadly 'virus' which afflicts the operation of the institutions. It demoralizes staff and deprives beneficiaries of further valuable services.

Armendáriz de Aghion & Morduch (2005) contend that the high interest rates continue to worry observers today. Singh (1968), for example, surveys seven moneylenders in a village close to Amritsar in the Punjab region of India, finding annualized interest rates from 134 to 159 percent—rates that were far higher than commercial bank interest rates. In Thailand, Siamwalla (1990) finds typical informal sector annualized rates of 60 percent (compared to 12–14 percent from Bank of Agriculture and Agricultural Co-operatives). Siamwalla (1990) also report rates that are as high as 120 percent in Thailand's remote areas. In the market town of Chambar in Pakistan, Aleem (1990) finds interest rates varying from 18 to 200 percent, with an average of just under 70 percent per year; in contrast, local banks in the region charged 12 percent per year. In Ghana, Malawi, Nigeria, and Tanzania, Steele, Aryeetey, Hettige, & Nissanke (1997) find moneylender interest rates at least 50 percentage points higher than formal sector rates.

Furtherance, Jansson (2003) articulates that the issue of funding is crucial to financial institutions, regardless of whether they operate as commercial banks, finance companies, credit unions or non-profit foundations. They all need to refinance their loan portfolio in one way or another, either through debt, deposits or equity. Jansson (2003) goes on to discuss the nature of MFIs and their sources of funds. He argues that MFIs that operate as non-profit foundations generally obtain their funds from donors, retained earnings and, in some cases, from public second-tier financial institutions. Some of the more successful non-profits have managed to obtain funding from commercial banks, but rarely in amounts exceeding their own equity. As for microfinance institutions that have taken the leap and subjected themselves to bank supervisory authorities, they tend to aggressively pursue a range of funding sources to support their continued growth.

McIntosh, de Janvry, & Sadoulet (2005) discovered that wherever two or more institutions are operating, many clients may be taking loans from several lenders simultaneously, or *'double-dipping'*. In interviews with credit officers from several major MFIs, the reasons attributed to borrowers for double-dipping were to smooth the timing of repayment of loans, to maintain cash flow.

On a different note but touching on injudicious competition, Boateng (2015) argues that the prevalent problem among MFIs is the copying, competing and mimicking the practices of universal banks. Many MFIs managers and other management staff were universal banks' staff who were either retired or sacked by their former employers. To these staff, MFIs is just an extension of the conventional universal banking they know. They also come with their organizational orientation, philosophy and culture. They refuse to understand that microfinance is not micro-universal banking but a different kind of banking requiring a different methodology, philosophy and client base. This may be why many MFIs spend colossal sums on office complex, glamorous vehicles and the walk-in wardrobe of their staff. They also engage in inordinate competition with the universal banks. This class of staff lack orientation as to the essence of microfinance.

Ssewanyana (2009) in his Uganda MFI research findings, found that MFIs are always often faced with high operating costs to provide financial services to the poor people and Small and Medium Enterprises. On the same note, but in a different context, Goldberg & Palladini (2010) impose that source of MFI operations risk includes the processes, practices, and information systems used to track the loan portfolio. A management information system tracks individuals, groups, sectors, and branches to identify quickly any threats to strong portfolio performance.

Caudill, Gropper, & Hartarska (2009) underpin that MFIs play a key role in many developing countries. Utilizing data from Eastern Europe and Central Asia, MFIs are found to generally operate with lower costs the longer they are in operation. Robinson (2001) concurs with the notion of time based cost-effectiveness of an MFI by proving that over time common elements of sustainable microfinance institutions are firmly established. The common elements shared by self-sufficient institutions can be broadly grouped into five categories: knowledge of the commercial microfinance business and its clients' characteristics of institutional ownership, priorities in organization and management, development of human resources, and corporate philosophy. Many of the shared elements are found in other kinds of microfinance programs as well, but they are common in aggregate to sustainable microfinance institutions operating on a large scale. The common denominator to what Robinson (2001) and Caudill, et al. (2009) are saying is that management experience developed over time is critical to MFI cost-effectiveness. In the African set up, cost-effectiveness of MFIs with time does not dominate as advanced by European counterparts. However, the realistic picture and most fundamental challenge is high operational/transaction cost. The operational costs include payment of rent, utility bills, salary of employees, travel and transportation, administration, depreciation etc. Electricity and water tariff hikes coupled with epileptic nature of supply forces MFIs to provide themselves with electricity and water at exorbitant costs resulting in high operational costs, thus threatening their survival. Other operational costs include mobile service, door to door service which is the most used medium for advertising MFIs products. In sum, small units of services, pose the challenges of high operating cost, several loan applications to be processed, numerous accounts to be managed and monitored, and repayment collections to be made from several locations especially in rural communities (Boateng, 2015).

2.5 Strategies to Mitigate Challenges

Burritt (2006) came up with benchmarks for successful MFIs which are eight of them in total. He argued that as a way of expanding financial access, MFIs should use innovative lending technology that balance the needs of low income borrowers at the same time minimizing risk to the institution. The MFIs should be located closer to the borrowers which works well for both disbursements and collections of loans. Their pricing of products should make sure that revenue covers the full cost of running operations to enable profitability within reasonable period of time, usually between 5 to 10 years. Operation efficacy was also alluded to, where MFIs should manage highly efficient operations to reach very large number of people, generally between 200 and 500 which ensures that operating costs as a percentage of the loan outstanding portfolio are minimized. Sustainability model relative to operating cost practice should be adopted in order to mitigate cost control as global benchmarks for sustainable institutions peg operating costs at 15 to 20 per cent of the outstanding portfolio. Marketing should also be modelled on attracting customers rather than target them; MFIs in this sense, are to design products that draw from broad population rather than narrowly targeting a particular group.

Related to marketing, MFIs should provide financial services exclusively, the general rule being that successful MFIs do not provide both financial and non-financial services. Finally, and a critical benchmark, MFIs should have multiple sources of funding to support long-term growth. they should be able to access commercial sources of funds including savings from the public, bank loans, debt markets; for instance, by issuing bonds or other forms of commercial paper. The world Microcredit summit Campaign, as cited in Shil (2009), outlined the nine best practices for MFIs originally developed by Jammeh (2002) which are presented in Table 1. They are considered as an extension to the Burritt (2006) strategies.

Table 1 The Nine Best Practices for MFIs

No.	***Best Practices***
a)	Ensuring loan repayment.
b)	Moving towards institutional sustainability.
c)	Targeting the poorest and covering costs.
d)	Sustainability in industrialized countries.
e)	Empowering women.
f)	Establishment and use of poverty measurement tools.
g)	Measuring impact on the lives of clients.
h)	Mobilizing savings and ensuring their safe use.
i)	Recruiting, training and retaining excellent staff.

Source: adapted from Shil (2009)

According to Shil (2009), the combination of these best practices in appropriate proportions is useful in poverty alleviation and other development plans. However, since MFIs deal with both business and human relationship, which involve a lot of risk-taking, the risks taken need to be managed properly. In furtherance, Burritt (2006), as explained earlier, stresses that successful MFIs have developed new, cost-effective business models and innovative lending technologies. Lending technology covers the range of activities carried out by an institution relating to developing products that respond to clients' needs, marketing products, and developing delivery channels, minimizing risk to the institution, and enforcing repayment of loans.

Basically, Table 1, demonstrates the type of MFI practice and its explanation, vis-à-vis, how an MFI can be a successful player on the market. The same concept is corroborated by Burritt

(2006) who attempts to divulge mitigating strategies or solutions that should make MFIs sustainable and profitable in their operations.

However, the envisaged nine best practices cited by Shil (2009) and further extended by Burritt (2006) do not mean that the MFI industry is complete and well-functioning relative to stakeholders' expectations. Criticisms to MFI operatives have strongly emerged against the backdrop of outlined best practices. Notable antithesis to MFIs operatives is advanced by Sharma (2005) who has categorically stated that, paradoxically, the so-called exploitative moneylender has been replaced with an army of moneylenders. Though the motive was to drive the exploitative moneylender away, in effect exploitation has been legitimized through the neo-institutional mechanism of micro-credit. With interest rates exceeding the repayment capacity of the poor, a debt-trap has been laid. Micro credit has been designed to create an illusion, much like electoral promises. At the cost of the poor in Bangladesh, GB has grown to sky-scraping heights.

2.6 Chapter Summary

The chapter has highlighted the definition of MFIs, evolution of the MF industry, operational challenges affecting micro-financing and envisaged strategies to mitigate some of the challenges. The literature has provided scenarios from a global perspective on how the industry has performed amidst challenges and some interventions being pursed to keep MFIs sustainable and profitable.

CHAPTER 3-RESEARCH METHODOLOGY

3.1 Introduction

Walter, (2010) states that methodology is the theoretical lens through which research is designed and conducted. This chapter presents the methodology that was used to carry out the research study. This includes; the study design, target population, data collection tools, data collection techniques, data analysis methods.

3.2 Research Design

Research design stands for advance planning of the methods to be adopted for collecting the relevant data and the techniques to be used in their analysis, keeping in view the objectives of the research and the availability of resources (Kothari, 2004).

The study employed exploratory and descriptive research design. M. Saunders, Lewis, & Thornhill (2007) define an exploratory study as a valuable means of finding out what is happening; to seek new insights; to ask questions and to assess phenomena in a new light'. Additionally, it is particularly useful if one wishes to clarify their understanding of a problem. On the other hand, descriptive design portrays an accurate profile of persons, events or situations (Saunders et al., 2007). The rationale for mixing the research designs hinges on the fact that social research does not fall neatly into one category of research or another. Rather, exploratory research was used to describe the social phenomena under investigation and also develop tentative explanation for what was found (Walter (Ed.), 2010).

3.3 Data Collection Strategy

This area covers the approach that was employed to collect data for the research study, from study population, techniques and methods in data collection.

3.3.1 Study Population

The population for registered MFIs in Malawi is 25. Out of the total number 16 are Microcredit Agencies (MCAs) while 9 are Non-Deposit Taking Microfinance Institutions (NDTMIs) (Reserve Bank of Malawi, 2015).

3.3.2 Population Sample and Sampling Technique

The target population was all 25 registered and licensed MFIs in Malawi under the Financial Services Act of 2010 (Refer to appendix 1), the rationale being that there are few official players on the market.

A census was carried out on key designations in MFI management which according to the Microfinance Act (2010), Section 27 (1) are the Chief Executive Officer, Chief Financial Officer and Chief Operations Officer. These key officers are considered to have satisfactory record of managing a FIs since they are only appointed after vetting from RBM. Based on stated reason the three officers were deemed as essential in provision of research data.

Purposive sampling was used to determine the sample since it enabled the researcher to use personal judgement to select cases that will best enable answer the research questions and to meet the objectives (Saunders et al., 2007). Additionally, it was appropriate method available since there were only limited number of primary data sources who could contribute to the study (Saunders et al., 2007).

3.3.3 Methods of Data Collection

Walter (2010) defines methods as a research technique or practice used to gather and analyse the research data. Documentary secondary data are often used in research projects that also use primary data collection methods (M. Saunders et al., 2007). This research study used both primary and secondary sources of collecting data.

3.3.3.1 Primary Data

Primary data was collected using self-administered questionnaire which were e-mailed, and in some cases, hand delivered to the MFIs. The questionnaire for MFI key managers was adopted from Goldberg & Palladini (2010) (Refer to appendix 2).

The self-administered questionnaire was opted based on Bryman (2008) assertions that it is both cheaper and quicker to administer. It also eliminates issues of absence of interviewer effects and interviewer variability.

3.3.3.2 Secondary Data

Documentary secondary data include written materials such as notices, correspondence, minutes of meetings, reports to shareholders, diaries, transcripts of speeches and administrative and public records depending on whether one has been granted access to an organisation's records (Saunders et al., 2007). Prior approval, using a University of Malawi introductory letter (Refer to Appendix 6), was sought to get broad historical industry performance quantitative data of MFIs from RBM. Consent to collect the data was granted by RBM on 10th March 2016 (Refer to Appendix 7).

3.4 Data Analysis

Data analysis is the process of analysing the evidence that is produced from the research (Walter, 2010). Descriptive statistics was used in analysing research data from the self-administered questionnaires for MFI Managers. Data collected was described through the use of frequency tables, frequency distribution and graphic presentations as prescribed by Lind, Marchal, & Wathen (2010). Qualitative data was also collected on the suggestions to mitigate industry challenges and was presented in the conclusion and recommendation in their original presentation.

3.5 Research Ethics

Based on ethics in business research, developed by Greener (2008), participants to the research study were given written introductory consent letter bearing information on; the researcher, aim of the research study, confidentiality (commercial and personal), anonymity, what it involves, and their freedom to participate or not (Refer to Appendix 6).

3.6 Limitations

The population sample for the study was limited to only the licensed MFIs in Malawi. The institutions that were included were limited to the officially published list by RBM as at December 2015. All the informal MFIs were excluded from the population sample. Therefore, this research is devoid of information on micro-financing challenges from other MFIs not listed in the official RBM annexure (Refer to Appendix 1).

3.7 Chapter Summary

The chapter described the research design, data collection strategy, study population, population sample and sample technique employed. It also gave focus to data analysis procedure, the research ethics followed and the limitations of the study.

CHAPTER 4-DATA ANALYSIS, FINDINGS AND DISCUSSION

4.1 Introduction

This chapter discusses the data analysis and findings from 75 self-administered questionnaires sent to managers of MFIs. A total of 41 questionnaires were responded to by the MFIs' key managers representing a response rate of 55%.

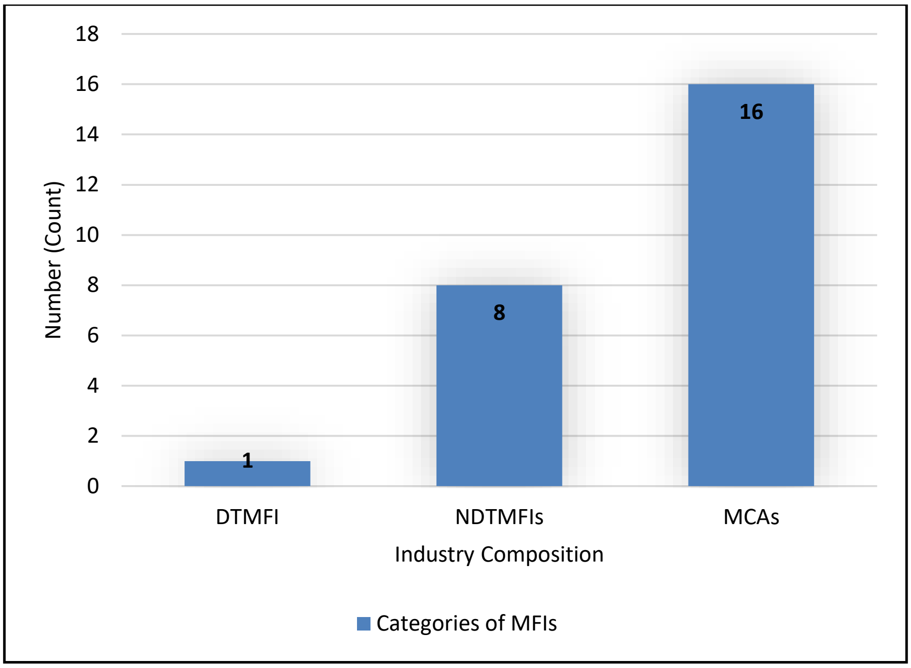
The secondary data determines the prevailing performance of MFIs in Malawi based on industry reports. The primary data identifies the challenges that the MFIs are facing in Malawi when extending financial services to their customers, and finally, provides solutions to alleviate the established challenges affecting MFI operations in Malawi.

4.2 Performance of Microfinance Sector in Malawi

This part presents the findings on the industry composition and its growth reports, the position of values and number of loans disbursed, increase or decrease in numbers of Loan/Credit Officers and the consolidated portfolio quality and management reports.

4.2.1 Industry Composition

According to Reserve Bank of Malawi (RBM), as illustrated in Figure 2, the list of licensed market players as at 31st December 2015, there are a total of 25 MFIs. Out of the 25, 16 are MCAs, 8 are NDTMFIs, and 1 is a DTMFI. Indicatively, there are more MCAs in operation followed by NDTMFIs. MCAs are considered as an entry level to the MF market. The market players, all things being equal, are supposed to graduate to NDTMFIs or DTMFIs over time. This is suggestive that the MF industry is still at an infancy stage, struggling to grow amid a myriad of supply-side challenges that affect their sustainability and profitability in the long run.



Source: Reserve Bank of Malawi (2015)

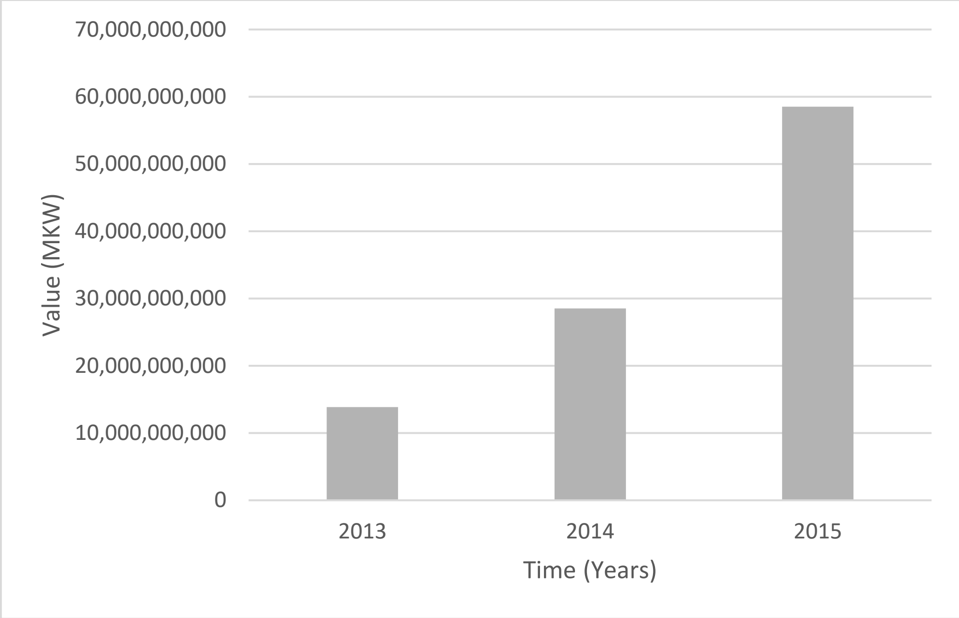
Figure 2 Registered MFIs in Malawi by Classification

Comparatively, our neighbouring countries have more MFIs than Malawi. For instance, Zambia has a total of 46 (Bank of Zambia, 2016). The Bank of Tanzania (2016) indicates that Tanzania has 41. Data from Mozambique shows that in 2000 they had 29 and in 2009 the figure rose to 32 despite civil war ravaging the country (Fion, 2006).It can be concluded that our neighbouring countries have registered more success in having more licenced MFIs which is suggestive of an existing conducive environment for both entry on the market, sustainability and profitability of the enterprises.

4.2.2 Value of Loans Disbursed

Figure 3 presents data of the loans disbursed by MFIs from 2013 to 2015. The disbursements show a high-pitched growth in the value of loans expended over the stated period. For instance, in January 2013 only MK13.8bn was disbursed followed by 28.5bn in 2015 and then MK58.5bn. The figures indicate an annual loan portfolio growth of 205% each financial year. Therefore, for 2 years running, the industry's loan value disbursed increased by 410%. This is a typical example of consistent industry growth relative to value of the loan book.

However, Figure 4 presents further analysis on the industry disbursement trends over the same period based on quarterly and yearly average disbursement movements.

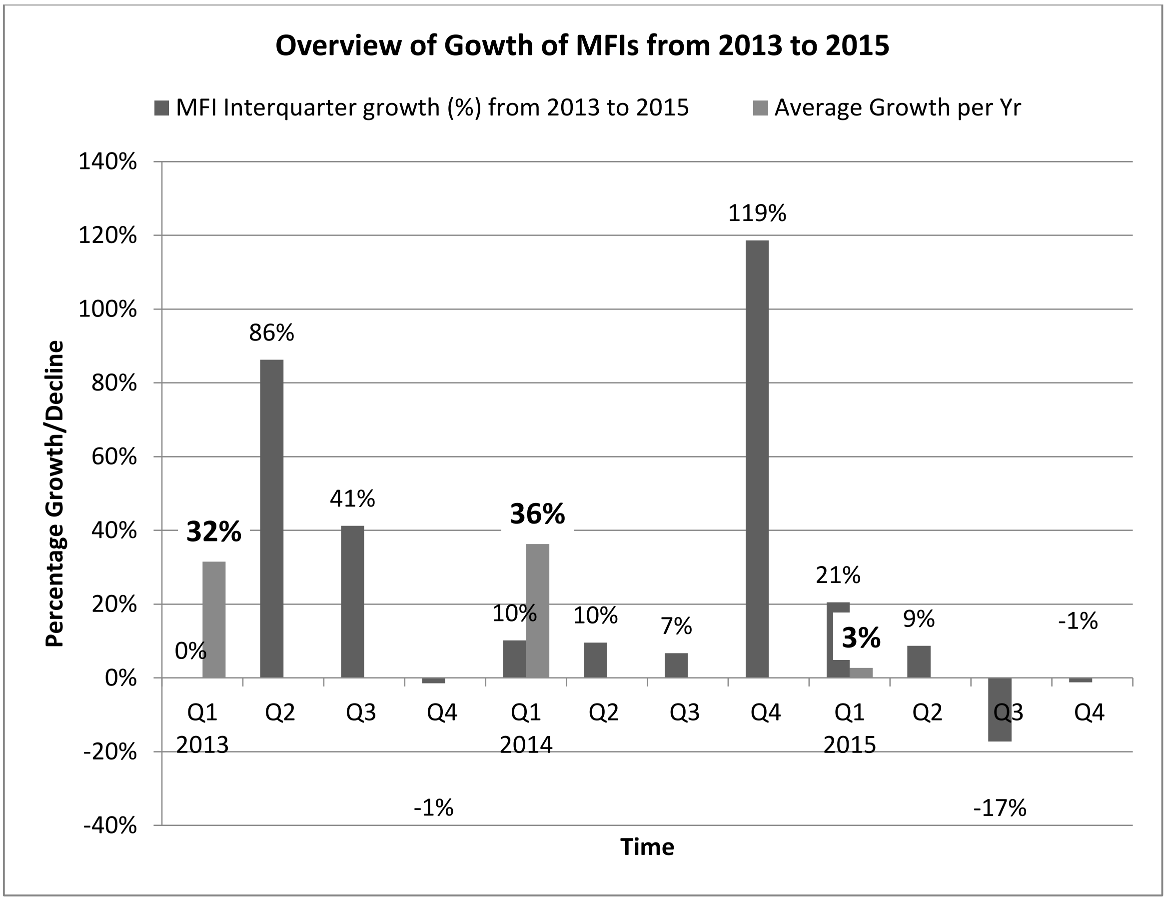


Source: Reserve Bank of Malawi (2016)

Figure 3 Total Value of Loans Disbursed by MFIs

Further analysis of industry disbursement movements in Figure 4 is indicative of an industry that has very asymmetrical trends. It is also symptomatic of an industry that is making inconsistent disbursement values. Results of yearly average growth trends, for instance, in it 2013 registered 32% growth, 2014 it was at 36% and 2015 dropped abruptly to 3%.

The same experience is corroborated by quarterly disbursements results on the same scatter graph (Figure 4). Q1 of 2013 starts with robust disbursements (86%) that rapidly declines to negative (-1%) at the end of the year. Q1 of 2014 starts picking up slowly and maintains a 10% growth and then registers a massive 119% inter-quarter growth at close of the year. Finally, going to 2015, the inter-quarter growth declined rapidly to negative growth where Q3 registers -17% and finally closing 2015 at a rising -1% inter-quarter growth. The rhythm, in terms of loan disbursement is still unpredictable, an indication of an industry that has not attained full stability.



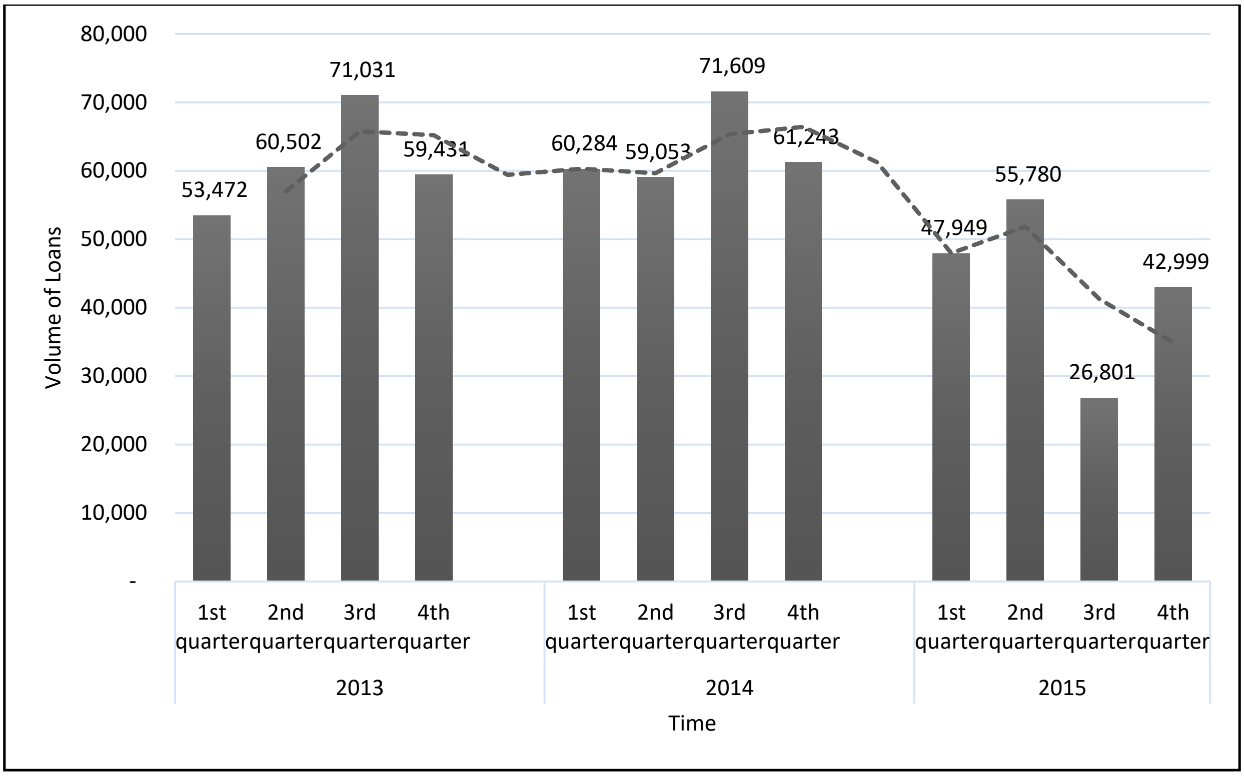
Source: Reserve Bank of Malawi (2016)

Figure 4 Average Loan Disbursement Movements-Quarterly and Yearly from 2013 to 2015

In summary, Figure 4 presents a picture of a business portfolio that is fighting to grow on the basis that there is no negative growth registered over the period if we base the argument on average growth per year. Additionally, ultimate sales values are potentially achievable if reference is made to both the 86% and 119% inter-quarter growth in 2013 and 2014 correspondingly.

4.2.3 Volume of Loans Disbursed

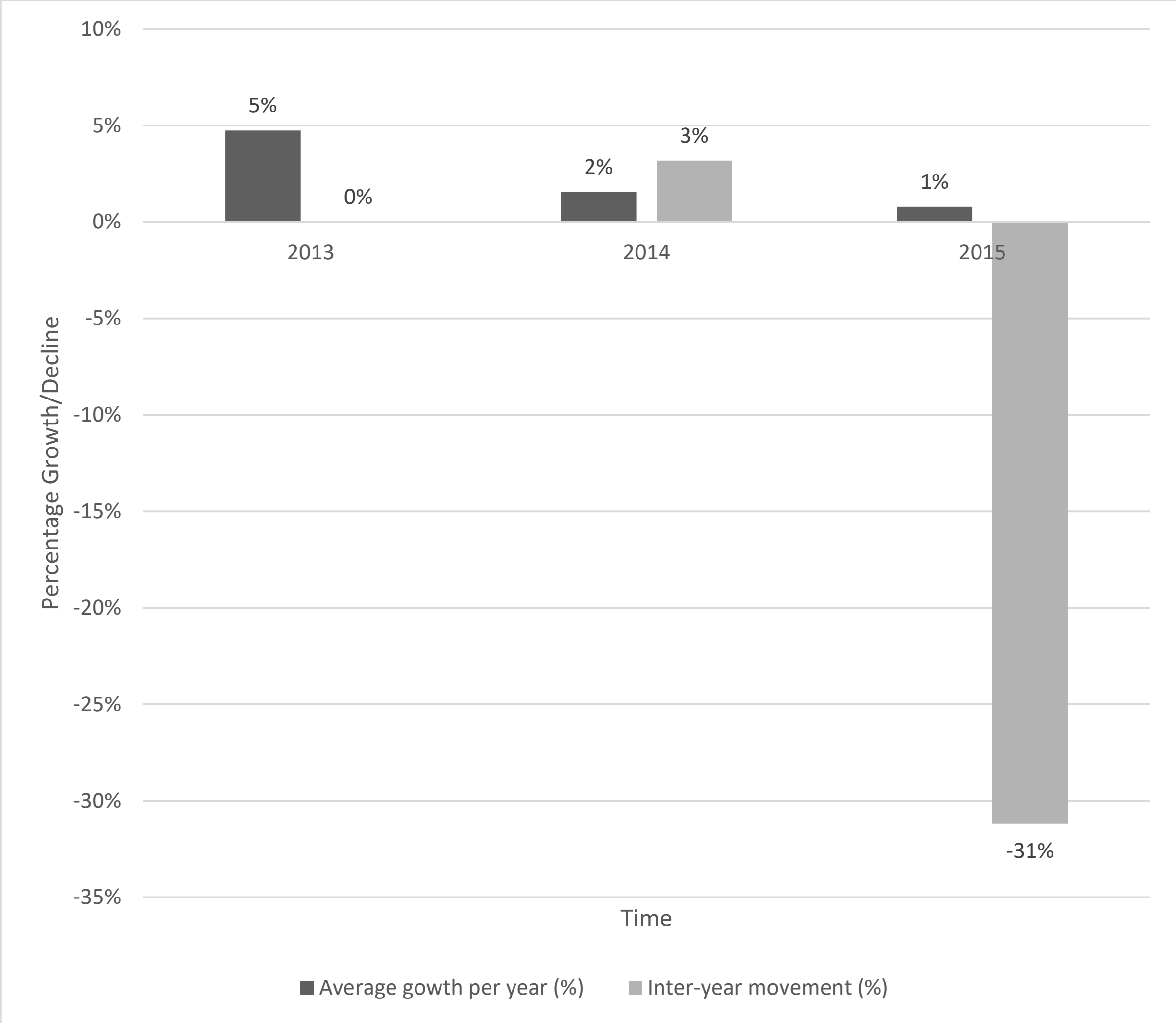
Figure 5 illustrates that the volume of loans disbursed over the period showing moving average trend line of growth and stability. It is prominent to notice strident growth in both Q3s of 2013 and 2014. However, the direction of the trend in 2015 is very different as it portrays declining loan applications. Q3 of 2015 registers an unparalleled deep fall compared to the increased volumes of the immediate past 2 years.



Source: Reserve Bank of Malawi (2016)

Figure 5 Number of Loans Disbursed from 2013 to 2015

The results in Figure 6 illustrates that on average the number of loans disbursed grew by 5% for 2013, 2% in 2014 and 1% in 2015. In terms of inter-year movement 2013 cannot be measured because data for 2012 was not available. However, from 2013 to 2014, 3% growth in the number of loans was registered. 2014 to 2015 there was a sharp decline to -31%. The findings of this analysis are an indication of a radical decline in recruitment of customers by the MFIs. The Malawi trend is in sharp contrast to the robust global trends presented by Armendáriz & Morduch (2010) which show an inclined growth of total number of cumber reached for a period between 1997 to 2007 (Refer to Figure 1).

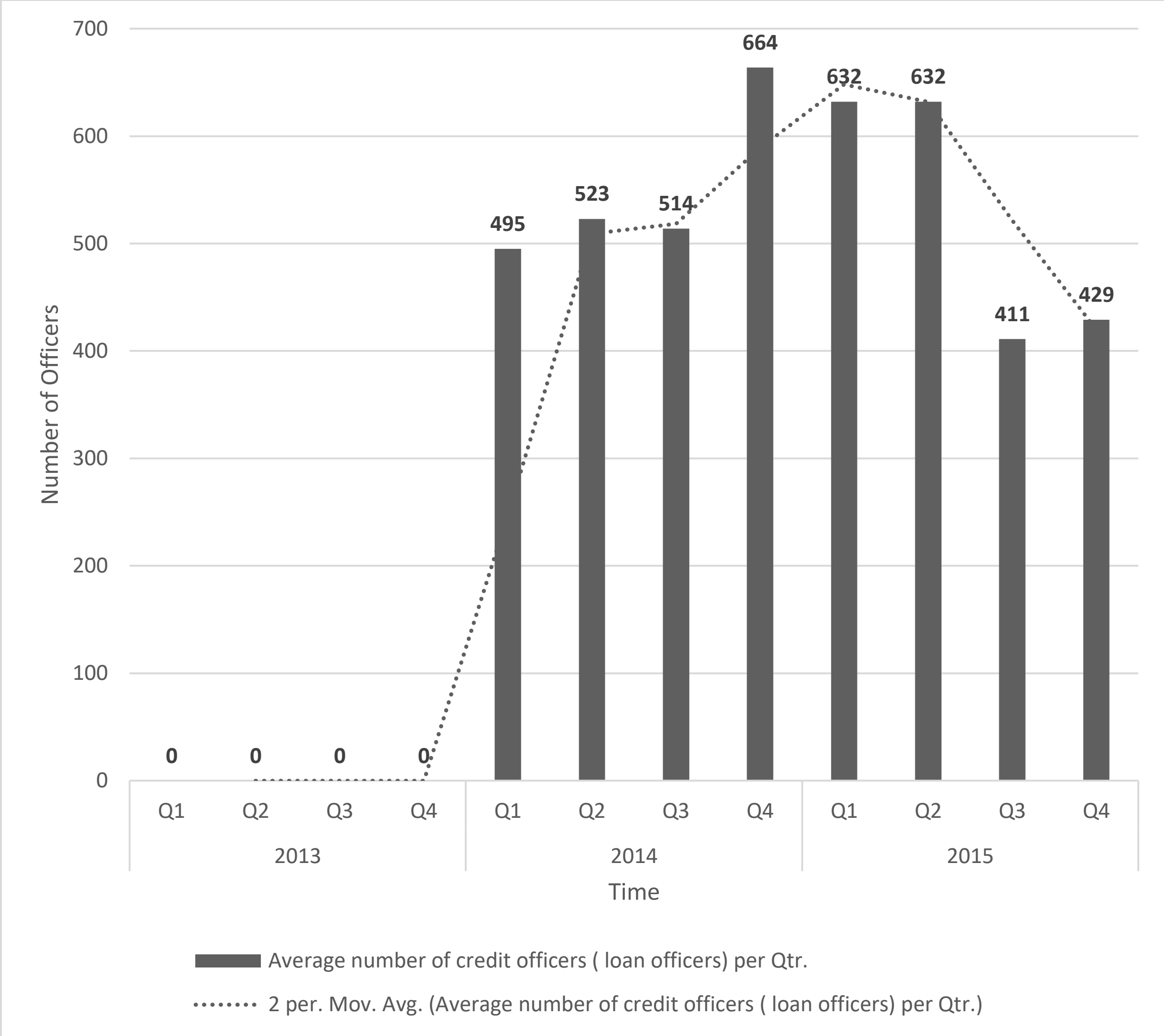


Source: Reserve Bank of Malawi (2016)

Figure 6 Loan Volumes Average Growth Rate from 2013 to 2015

4.2.4 Average Number of Loan/Credit Officers

Figure 7 presents data only available for 2014 and 2015. Nevertheless, for 2014 on average, the number of Credit Officers grew by 8% and in 2015 there was a drop to -9%. In actual figures, the number of Credit Officers declined from 549 to 526 and the moving average trend-line reflect the same.



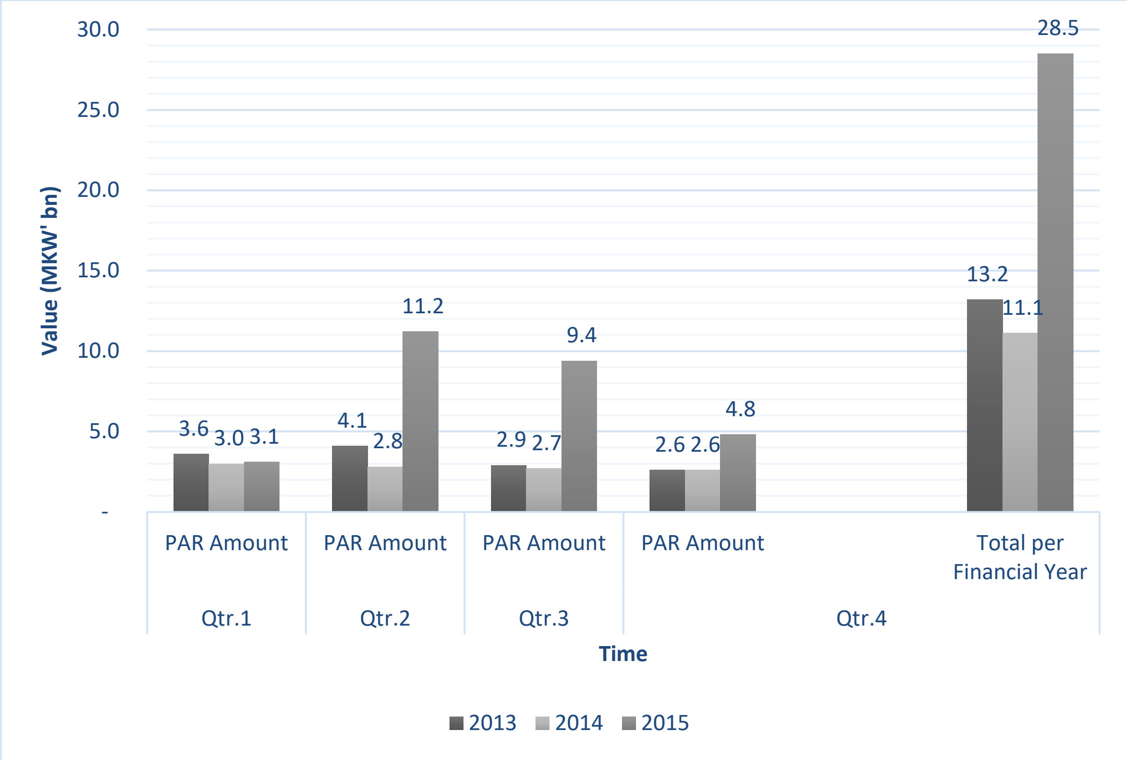
Source: Reserve Bank of Malawi (2016)

Figure 7 Average Number of Loan Officers

Comparatively, at global stage, the number of loans disbursed between 1996 and 2008 have increased by 512% (to 3352 from 655) (Armendáriz & Morduch, 2010).

4.2.5 Portfolio Report Quality and Management Reports

This part presents the findings of outstanding principal loan balances for each quarter from 2013 to 2015 in terms of Portfolio at Risk (PAR).



Source: Reserve Bank of Malawi (2016)

Figure 8 Portfolio at Risk (PAR)

The findings presented in Figure 8 illustrate a stable to alarming situation on the rise of PAR. In 2013 the PAR was at MK13.2 billion. The following year it declined to MK11.1 billion, and in 2015 the figure rose to MK28.5 billion. As a measurement of a percentage, in 2014 the PAR dropped by -15% and only to increase sharply to 152% in 2015.

Separately, the second quarter for all the years, especially for 2013 and 2015, recorded the highest values of PAR. This must have been a tough period for normal loan recoveries. Challenges in on time loan recovery can be attributed to so many factors and one of them Goldberg & Palladini (2010) allude to adverse selection of customer because of lack of proper identification precludes completeness of information.

4.2.6 MFI Growth Reports

The findings on the condition of growth of the industry are based on assets value and the number of registered industry players from 2012 to 2015.

Table 2 indicates that in 2013 the MFI assets grew by only 8%. Thereafter, there was phenomenal increased growth in 2014 to 172%. The growth trend drastically declined in 2015 when it registered a -3.8%.

The decline in growth of the asset size in 2015 directly correlates with the higher PAR value (MK28.5bn) of the same year presented in Figure 8. Reduction in the value of the MFIs is a derivation of high loan impairment figures caused by defaulting customers. Impairment in this instance, in part, can be attributed to fraud as alleged by Meki, N. (2015, July 28) which caused a loss of millions of kwacha to some MFIs.

Table 2 Growth of MFIs by Assets and Registration

Assets	**2012**	**2013**	**2014**	**2015**
K'bn	10,8	11,6	31,7	30,5
Growth Rates (%)	-	8,0	172,1	(3,8)
Number of MFI's	11	19	25	27
Of which				
Micro-Credit Agencies (MCA's)	*6*	*14*	*16*	*17*
Non deposit taking MFIs (NDTMFI's)	*5*	*5*	*10*	*9*
Deposit Taking MFIs (DTI's)	*0*	*0*	*0*	*1*
Banks with microfinance window	2	2	2	2
SACCOs				
Number of SACCO's	45	48	49	30
Of which				
Provisionally Licensed	*30*	*45*	*49*	*5*
Fully Licensed	*15*	*3*	*0*	*25*

Source: Reserve Bank of Malawi (2016)

RBM has conflicting figures on the number of registered MFIs for 2015. Reserve Bank of Malawi (2015) in its golden jubilee documentary indicated 25. In its official press release Registrar of Financial Services (June, 2015) gives a the total as 26.

However, the findings in Table 2 disclose an increase in industry players for 2013 and 2014 only. As for 2014 and 2015 the growth appears to have stalled completely, as the movements registered were negligible.

4.3 Attributes of MFIs

This section presents the findings and discussion on the attributes of MFIs with a focus on areas of governance, operations, marketing capitalization and staff related issues.

4.3.1.1 Governance of MFIs

The Board of Directors (BODs) composition as illustrated in Table 3 shows male dominance (78%) at strategic decision-making level, and women constituted a meagre 22%. Research studies by Randøy, Mori, & Golesorkhi (2015) suggest that BODs with specific attributes may help MFIs to attain social objectives. For instance, female Board Members may have unique competencies and knowledge with respect to specific needs of female customers. Malawian women are bound to be financially excluded by the MFIs since they are not well represented at strategic level for their needs to be taken on board.

In terms of professional background 49% have business related qualifications followed by 31% with accounting feat. Commerce which is closer of business registered 16% and finally legal qualification was last at 4%. In a nutshell, it can be pronounced that the MFIs' BOD have the requisite qualifications to competently run the industry to register positive results.

Table 3 Board of Directors Composition

MFI	Male	Female	Accounting	Legal	Business	Commerce
MFI 1	4	1	3	0	2	0
MFI 2	5	1	2	1	3	0
MFI 3	4	0	1	0	2	1
MFI 4	5	1	1	1	4	0
MFI 5	11	1	4	4	4	0
MFI 6	1	1	0	0	1	1
MFI 7	3	1	2	1	1	0
MFI 8	3	1	1	1	2	0
MFI 9	1	2	0	0	3	0
MFI 10	2	3	1	1	2	1
MFI 11	3	2	2		3	0
MFI 12	6	0	2	1	3	0
MFI 13	5	1	2	1	3	0
Total	**53**	**15**	**21**	**11**	**33**	**3**
Average	**78%**	**22%**	**31%**	**16%**	**49%**	**4%**

Table 4 exhibits attributes of MFI governance system. The finding established that most MFIs (83%) have well established mechanisms for internal controls in place which include organizational structure, established systems and policies. The results of the attribute of availability of internal controls correlates with further findings of existence of competent Boards and leadership in place (66%) that follows code of conduct when discharging their duties (66%), the issues of existence of strategic plans and being implemented also registered (66%). The feeling of equity holders having capacity to provide capital was given a confidence of 63%. The BODs are thought of being independent in discharging their duties (59%). The final positive response was on the existence of sound regulatory framework for equity holder (54%). Encouragingly, the above positive attributes may have been enabled by the introduction of legislation on microfinance operations in Malawi which only came into effect in July 2010. The above results are in contrasts with findings in Ghana where corporate governance in many MFIs is very poor in terms of internal controls. BODs are known to misuse their positions to obtain facilities way above the regulatory limit for insider related loans and worse still with no intention of repaying such facilities. They also use their position to influence and manipulate the recruitment process on favour of their cronies (Boateng, 2015).

However, the MFIs in Malawi also have their weaker-side on corporate governance practice. Areas that are challenges are on; Instruments to specify rights and responsibilities of equity holders, the separation of responsibilities of Board Chairperson and Chief Executive Officer (CEO), existence of term limits for BODs and existence of independent Board committees. All these areas generated results of less than 50% backing. If research findings of Randøy et al. (2015) in East Africa which endorses the issue of independence of the BODs guarantees understanding of customers' needs and provides strong linkages to the providers of resources that are important to MFIs' mission, is to go by, then Malawi MFIs are at higher risk of veering away from their vision and mission. According to Randøy et al. (2015) Malawi MFIs will in the end fail to achieve higher outreach performance. Additionally, the findings of Goldberg & Palladini (2010) established that the CEO and Board Chairperson must not be the same person as it results into control of the institution being concentrated in one person, later on producing the veering off consequences suggested by (Randøy et al., 2015).

Table 4 Attributes of MFIs Governance System

Governance Attributes	Not Applicable	No %	Yes %	Total %
Existence of mechanisms for internal controls including organization structure, systems, policies and procedures.	10%	7%	83%	**100%**
Existence of a competent Board and leadership	17%	17%	66%	**100%**
Existence of code of conduct for the Board of Directors	10%	24%	66%	**100%**
Existence of strategic plan indication clearly the mission and objectives	10%	24%	66%	**100%**
Existence and implementation of a framework for setting objectives, ensuring objectives are met, assessing performance and for rewarding performance	10%	24%	66%	**100%**
Existence of clear equity holders and their capacity to provide more capital	10%	27%	63%	**100%**
Existence of independent Board of Directors	10%	32%	59%	**100%**
External factors that include the existence of sound and regulatory framework for equity holders	12%	34%	54%	**100%**
Existence of instruments specifying rights and responsibilities of equity holders	7%	44%	49%	**100%**
Separation of responsibilities of Board Chair and Chief Executive	10%	46%	44%	**100%**
Existence of term limit for Board of Directors	10%	54%	37%	**100%**
Existence of independent Board Committees	10%	56%	34%	**100%**

4.3.1.2 Operational Issues

The findings in this area relates to the number of years an MFI has been in operation. The results are linked to expected performance indicators linked to experience in the industry.

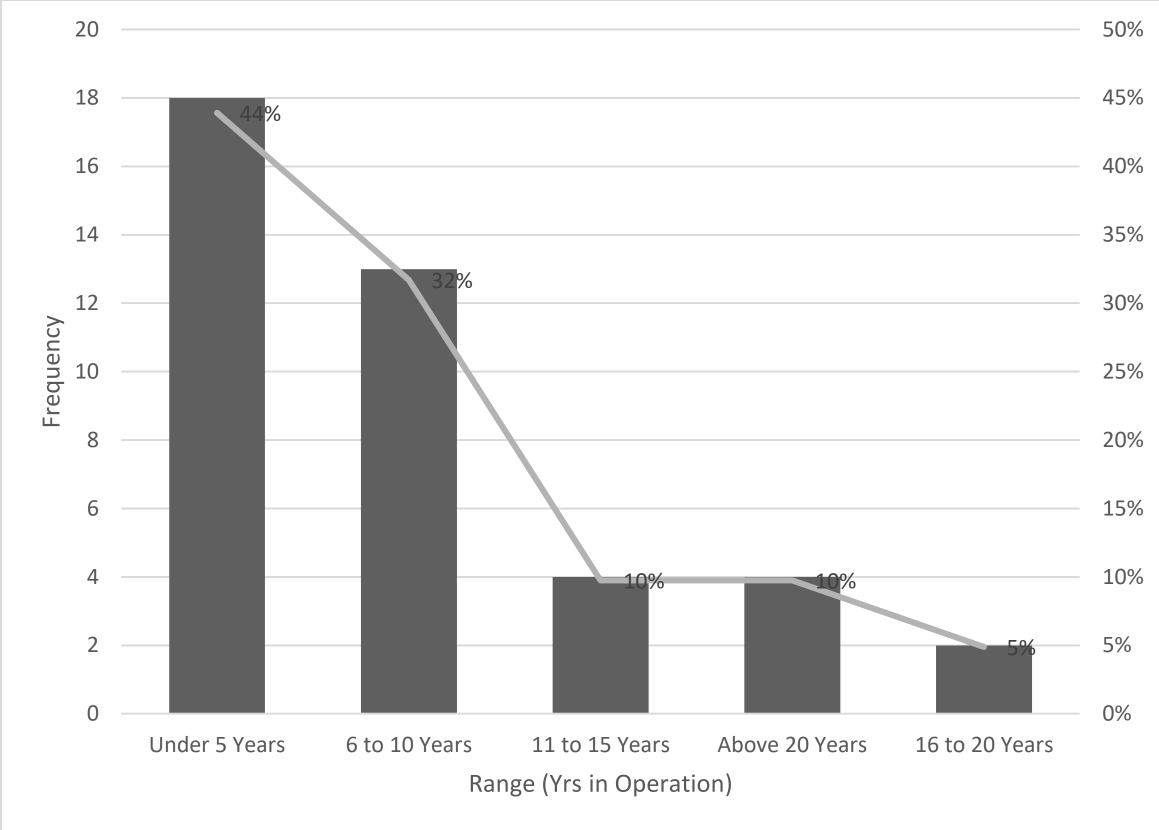


Figure 9 MFIs Years in Operation

The results in Figure 9 suggest that most MFIs are under 5 years in terms of number of years they have been operational in Malawi. This was endorsed by 44% of the respondents. Then, 32% declared that most MFIs are 6 to 10 years old. On MFIs, above 10 years of operations, 25% of the respondents consented.

Caudill et al. (2009) emphasized that management experience developed over time is the critical common denominator for MFI cost-effectiveness and their sustainability. The same notion is underpinned by Robinson (2001) who utilizes research data from Eastern Europe and Central Asia to assert that MFIs are found to generally operate with lower costs the longer they are in operation. Using the philosophies asserted by Caudill et al. (2009) and Robinson (2001), it can be determined that MFIs in Malawi are at a position of higher operating costs which are a direct threat to their business longevity. The findings of Lafourcade, Isern, Mwangi, & Brown (2005), also underpin that efficient institutions minimize costs of delivering services which is achieved through considerable years of experience.

4.3.1.3 Marketing Issues

The findings relate to the attribute of financial products offered, the target markets, inclusive microfinance targeting the poor, loan book threshold targeting the poor, and the income bracket of most MFI customers.

Table 5 Financial Products Offered by MFIs

Products	Count	% Responses
Credit	37	90%
Credit & Insurance	4	10%
Grand Total	**41**	**100%**

Table 5 illustration clearly asserts that MFIs in Malawi are providing financial products that constitute 90% credit services and 10% combining insurance and credit. By description, most MFIs in Malawi are not operating in the broader sense of the definition of microfinance which is supposed to offer other financial products in form of ; savings, micro-leasing, electronic money transfer and payment services, among other areas, as defined by Microfinance Act (2010). MFIs in Malawi focus primarily on one segment of the market which is micro-credit provision. This on its own is problem the industry should work on if the MFIs are to remain relevant on the market and sustain themselves in the long run. The same findings are in agreement to research results by Legadima (2012) in South Africa which determined that none of the MFIs offered savings as a service, most MFIs offer credit. The same findings were established in Ethiopia by Kereta (2007) which concluded that all the MFIs focused on loan provision and saving product and very few provide micro-insurance, leasing, pension, money transfer and consultancy.

Table 6 Target Market for MFIs

No.	Target Market	Count	Response %
1	Only Employed	11	27%
2	Only Employed & Small Businesses	7	17%
3	All Except Larger Businesses	6	15%
4	All Categories	5	12%
5	Small & Larger Businesses	4	10%
6	Individuals & Business	3	7%
7	Only Women & Small Businesses	2	5%
8	Individuals	1	2%
9	Small Businesses	1	2%
10	Unemployed	1	2%
11	**Grand Total**	**41**	**100%**

Table 6 presents the target markets by category of market segment. The findings revealed that most MFIs target only the employed financial consumers (27%). Following this was the category of the employed and small businesses (17%). Already this category augments the employed category bringing the preference for the employed consumers at 44%. Small and larger businesses market category was supported by 10% response. Individuals and small businesses constituted 7%; only women and small businesses was supported by 5%. To a lesser extent, markets targeted at equal proportions are for individuals (2%), small business (2%) and unemployed (2%). From the above findings, what is substantive is that; the employed category is the much sought-after market segment. By compounding; small businesses market segment cross-cuts as a complementary targeted market segment with 68% agreement.

However, the global fundamentals of MFIs market segmentation are an anti-thesis to what is happening in Malawi. Shil (2009) asserts that MFIs must target empowerment of women. However, the findings show that only one MFI does deliberately target women. Furthermore, the maxim of targeting the poorest and measuring the impact on the lives of customers as advanced by Burritt (2006) does not exist in the product offerings.

Table 7 Prevalence of Inclusive Microfinance Targeting the Poor

Inclusive Microfinance	**Count**	**% Response**
No	22	54%
Yes	19	46%
Grand Total	**41**	**100%**

Table 7 illustrates that most the MFIs (54%) suggest that inclusive microfinance targeting the poor is still a problem. MFIs response to the ultra-poor segment of the market is an area that needs to be considered strategically if inclusive finance is to be attained. The Malawi results are a deviation from client targeting methodologies in practice across the globe. Kereta (2007) advances that one primary targeting issue is poverty targeting which is interpreted as lending to the very poor and poor versus lending to the marginally poor and non-poor.

Table 8 Loan Book Threshold Targeting Inclusive Microfinance

Threshold	**Count**	**% Response**
NA	22	54%
Above 20%	8	20%
11% to 20%	7	17%
6% to 10%	4	10%
Grand Total	**41**	**100%**

Extending the argument of prevalence of inclusive microfinance targeting the ultra-poor, Table 8 illustrates what threshold of the loan book is reserved for the financial inclusion of the ultra-poor segment. Overwhelmingly, 54% of the respondents registered that the targeting of ultra-poor market segment does not exist in their market preference.

On the other hand, 20% agreed that above 20% of their loan book targets the ultra-poor. Additionally, 17% agreed that 11% to 20% of the book targets the ultra-poor. To a lesser extent, 10% agreed that 6% to 10% of the loan book targets the same segment of the market.

Profoundly, the above findings are in sharp contrast to the Consultative Group to Assist the Poor (CGAP) twin objectives that are aimed at increasing financial sustainability and deepening their poverty focus. Under this context, the latter means, increasing their outreach and impact on the lives of the poorer people (Henry et al., 2003). The above situation is reflected in Bangladesh where targeted outreach to the poorer people has shaped the discourse of MF with evidence based results indicating 15% of all MFIs customer coming from this segment (Abed & Matin, 2007).

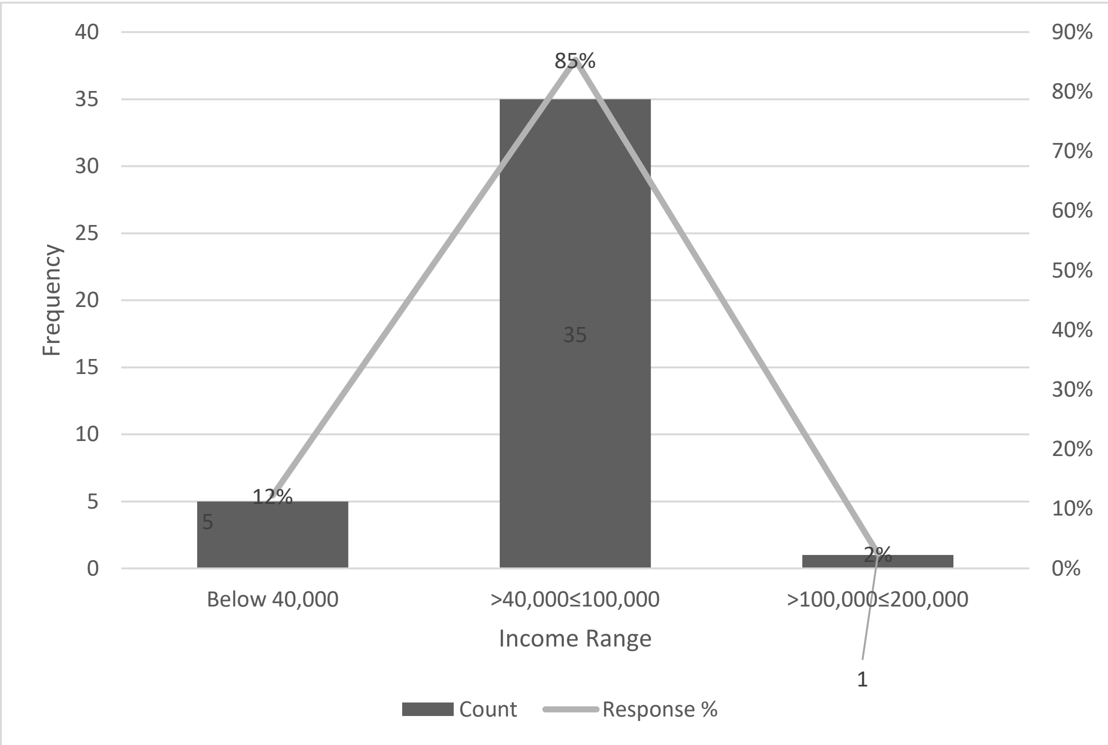


Figure 10 Monthly Income Bracket of Customers

Figure 10 shows results of the monthly income groups in which most of the customers fall into. The MFIs responses (85%) agreed that the income range of most of their customers fall in the bracket of greater than MK40,000 equal to or less than MK100,000. Next category, 12% of the respondents suggested that their customers earn below MK40,000; and finally, the high-income bracket of greater than MK100,000 equal to or less than MK200,000 was endorsed by 3% of the respondents.

These finding corroborate the challenge of MFIs failing to achieve inclusive finance in their marketing. MFIs are targeting financial consumers that already have some formal or stable incomes.

4.3.1.4 Capitalization Issues

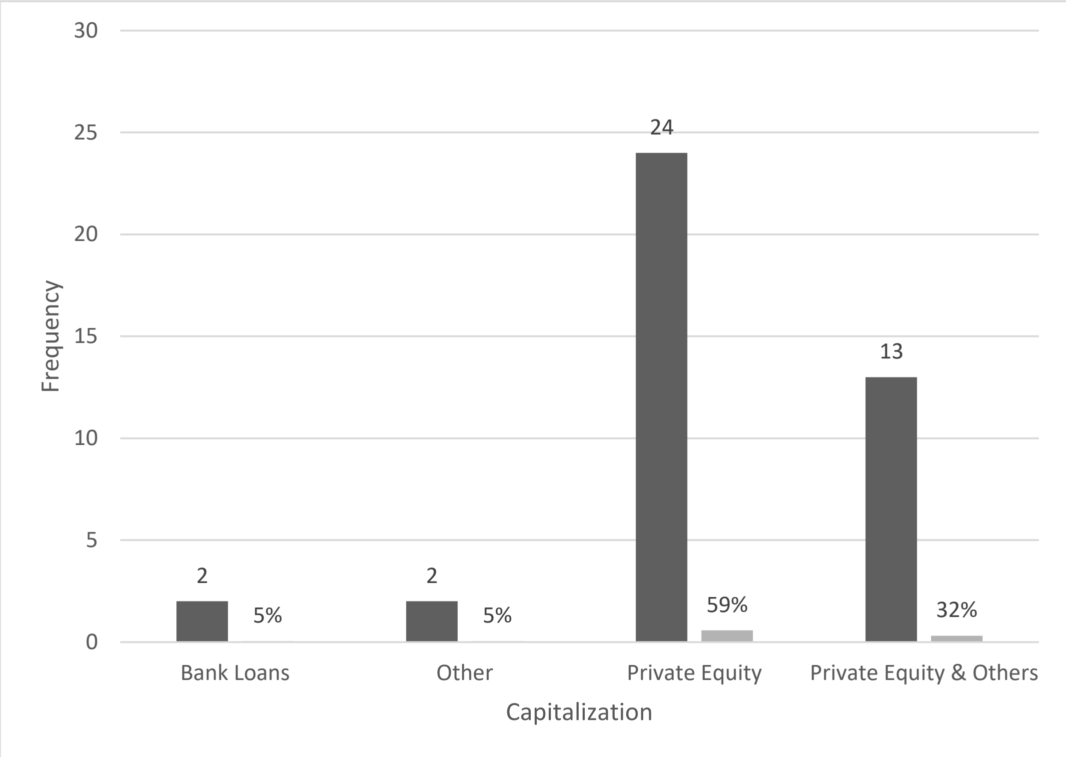


Figure 11 Capitalization of MFIs

The findings in Figure 11 shows the proportions of how or where the MFIs access capital for their enterprise. Resoundingly, 90% (37) declared that they get their funds from private equity holders. A smaller proportion of 5% (2) is sought from debt-financing in form of bank loans. The other 5% (2) of the funds are generated through other means that were not described. However, gurus in MF propose that moving towards institutional sustainability and to support long-term growth, MFIs should be able to access commercial sources of funds including savings from the public, bank loans and other debt market (issuing bonds and commercial paper, as some examples) (Burritt, 2006). Jansson (2003) further supports the idea on how critical the issue of funding is to MFIs. He argues that re-financing loan portfolios for MFIs should be aggressively pursued to fund and support continued growth. He mentions securing debts and deposits as some notable sources of funding.

4.3.1.5 Staff Related Issues

The findings presented in Table 9 suggest that most members of staff in the MFIs have Diplomas as education level qualification; 88% of the responded stated this position. On staff with University Degree, 10% of the respondents assented. Finally, 2% of the respondents were not sure of the attainment levels of education in their staff.

Under the best practices and benchmarks of successful MFIs, Burritt (2006) and Shil (2009) advocate for recruiting, training and retaining excellent staff. This in their understanding brings about operational efficacy where they manage highly efficient operations to reach very large number of people. Typical of operation efficiency, each officer manages a significant number of customers, between 200 and 500 and operating costs as a percentage of the outstanding loan portfolio are minimized.

Table 9 Educational Level of Staff

Staff Education Level	**Count**	**% Response**
Diploma	36	88%
University Degree	4	10%
NA	1	2%
Grand Total	**41**	**100%**

The industry professionalism in terms of higher qualification is still in formative stages. Most staff have entry-level basic qualifications defined as diplomas.

Table 10 Staff Turnover in MFIs

Staff Turnover	**Count**	**% Response**
Low	23	56%
NA	10	24%
Moderate	5	12%
High	3	7%
Grand Total	**41**	**100%**

Table 10 shows the results of the past 12 months on how high, vis-à-vis, the staff turnover was in MFIs. Most of the respondents (56%) agreed that staff turnover was low which in this context means 20% and less. Others felt that this did not apply (24%) at all in their MFIs. Moderate turnover was agreed by some (12%), this meant greater than 20% and less than 50%. Finally, 7% of the respondent felt turnover was high, greater that 50% staff left their organizations.

Table 11 Ranges of Staff Numbers Employed by MFIs

Range of Staff Employed	**Count**	**Response %**
Less than 20	17	41%
21 to 30 Employees	16	39%
31 to 40 Employees	4	10%
Above 40 and more	4	10%
Grand Total	**41**	**100%**

Findings in Table 11 illustrate that most of the respondents declared that most MFIs have less than 10 members of staff. Next to that, 39% said that most MFIs have between 20 to 30 employees. The 30 to 40 employee categories were agreed by 10% of the respondents. Greater than 40 employees, was also agreed by 10% of the respondents.

With the numbers of staff in MFIs in Malawi being on the lower side, coupled with not so robust academic credentials, the MFIs are quite challenged on staff related issues to bring about the much-needed operational efficacy for the growth and sustainability of the industry.

4.4 Challenges Encountered by the MFIs

This section presents the findings from the self-administered questionnaire responded by key MFI managers. The findings thereof are also discussed in detail simultaneously.

The key managers of MFIs acknowledged that they experience all the 26 general challenges in their operations as presented the questionnaire for manager (Refer to Appendix 2, pages 76-77). They ranked the challenges, vis-à-vis, to what extent they affect operations of their FIs using scale of 1 to 4; (small problem-1), (minor problem-2), (moderate problem-3) and (severe problem-4). Remarkably, the same issues were raised by similar studies by Abed & Matin (2007) who identified matters of identification (ID), education levels of staff, poor communication infrastructure, collections, as some of the notable bottlenecks. Boateng (2015) corroborates the same details in subsequent research findings.

Table 12 below summarizes the findings of the extent of MFI challenges. Only 2 challenges were beheld as being severe in nature with a mean score of 4. The most responses were that most MFIs face moderate challenges in their operations, and 15 of those got a mean score of 3. The minors which were deemed as inconsequential were 9 with a mean score of 2. The small ones had no response/result.

Table 12 Mean Score Summary of MFIs' Challenges and their Extent

No.	Extent	Number
1	Severe	2
2	Moderate	15
3	Minor	9
4	Small	0

Detailed analysis and discussion of findings on the challenges of MFIs and their extent are illustrated further in Tables 13 and 14. Table 13 combined the findings on severe and moderate challenges while Table 14 presents the minor challenges affecting micro-financing.

Table 13 Severe and Moderate Challenges Faced by MFI Challenges

No.	Challenges	SM %	MI %	MO %	SV %	Mean Score
1	Lack of adequate capital to lend to customers	20%	3%	3%	75%	4
2	Legislation & regulatory framework	55%	13%	21%	11%	4
3	Theft by staff	49%	12%	10%	29%	3
4	ICT usage in MFI	32%	2%	12%	54%	3
5	Double-dipping by customers (multiple borrowing from other MFIs)	49%	12%	12%	27%	3
6	Collections gimmick and late payments	5%	37%	0%	56%	3
7	Retaining existing customers (building customer loyalty)	54%	17%	10%	20%	3
8	Inadequate funding /or capital financing (funding hitch)	17%	2%	5%	78%	3
9	Higher lending rates	5%	2%	46%	44%	3
10	Customer identification (IDs & KYC)	41%	15%	20%	24%	3
11	Education level of staff	41%	17%	22%	20%	3
12	Unreliable loan repayment systems (i.e., bank debit orders, mobile money operations, government procedures etc.)	27%	5%	51%	17%	3
13	High operational costs	17%	15%	20%	49%	3
14	Educational level of your customers (effect on understanding the financial products)	41%	22%	29%	7%	3
15	Unreliable infrastructure (Poor transport, communication, IT, etc.)	12%	15%	15%	59%	3
16	Service quality to customers (attracting new customers)	2%	20%	78%	0%	3
17	Small and irregular cash flows	12%	17%	20%	51%	3

Firstly, reference to Table 13 suggests that the challenge of lack of capital adequacy and legislation shortfalls are severe problems affecting the operations of MFIs in Malawi as they got a mean score of 4. And Focusing on capital issues, 75% of the respondents felt that this was a giant issue that is seriously affecting the operations of MFIs. Linked to the same, 78% of the respondents felt that inadequate capital financing was a severe problem. The findings concur with those of Volschenk, Fish, & Mukama (2005:53) which concluded that lack of capital is the biggest inhibitor of growth in the MFI sector; the below quote summarises their findings in relation to inadequate capital: *"A lack of capital to lend to clients could lead to loan applications that are processed on a queuing basis, favouritism in loan allocations and fraud. Such a MFI cannot expand microfinance services/products. With inadequate funds to afford reliable infrastructure, research for clients' information, education, skills and incentives to employees, the result is poor quality of loan books, low morale among employees and poor selection practices."*

Nasir (2013) research findings in India also allude to the fact that lack of access to funding is a big challenge. This has massively contributed to the lack of growth of MFIs as concerned agencies (banks) and government have not supported them to meet their capital requirements as demanded. In Nigeria, One of the critical problems facing microfinance institutions is the lack of finance needed to expand financial services to clients; this primarily arises from low capital base of the institutions (Nwanyanwu, 2011).

Secondly, the challenge of legislation and regulatory framework was also emphasized as a severe challenge with a mean score of 4. This is not a surprise because the Malawi Microfinance Act (2010) only came into force in 2012. The Credit Reference Bureau Act (2010) with a further amendment in 2015 only came into effect in the last quarter of 2016. The absence of these two pieces of legislation meant that MFIs were acting outside a licenced context which was failing to legitimizes their status (Loboyeski et al, 2004). In Ethiopia for instance, Kereta (2007) confirmed that the legal environment is not conducive enough in enforcing the loan contract. When loan contract cannot be reinforced the cases of default rise leading to high PARs affecting sustainability and growth of the industry. The same result is corroborated by Volschenk et al. (2005) who argue that legislation and regulatory framework is not conducive to allow sound MFIs to emerge and grow in Tanzania.

4.4.1 Moderate Challenges

According to Table 13, moderate challenges have a mean of 3. Firstly, theft by staff, was determined as a moderate challenge. In Ghana, according to research findings of Boateng (2015), the same situation is prevalent, as monitoring branch/agency activities or field officers' activities to prevent internal fraud and theft is a major challenge. This challenge has resulted in several fraud cases where field officers under record the actual deposits or repayments of their clients and in some cases, abscond with deposits collected. MFIs with such challenges most often gloss over them. Research findings by Legadima (2012) also confirms that theft by staff is a moderate challenge that need to be cautioned.

Secondly, ICT usage was also viewed as a moderate challenge according to study findings. Burritt (2006) also confirms the same challenge when he was looking at easing access to financial services in Malawi. He determined that Information technology has the potential to reduce high transaction costs that discourage financial sector development. Information technology can be used to create new delivery channels, and widen the range of financial services including payment and transfer services. The rationale given by Burritt (2006) justifies why the issue of ICT has to be advanced to solve a myriad of challenges which are affecting the growth of the industry.

Thirdly, double-dipping by customers, which in some circles is referred to as multiple borrowing was conceived as a moderate challenge. In Malawi, it is common practice for MFI customers to borrow from several FIs as there is no legal framework to deter them from doing so. On the part of the MFIs they do not have prior information to check if the customer is financially distressed due to several loan repayment commitments. In the interim, MFIs that are subscribers to Payment Solution Malawi can only vet civil servants loan liabilities to curb double-dipping, but the private sector customers are devoid of such check. The same observation was in existence in Kenya, Mwangi (2014) found out that the earlier MFIs in their country did the screening and trained the new borrowers but the new arrivals skipped those steps. These practices contributed to the loan repayment defaults due to multiple borrowings that exceeded the borrowers’ capacity to service the loans. In Malawi where MFIs predominantly offer credit products as presented in Table 5; the challenge of double-dipping will remain outstanding. Mwangi (2014) argues that client-lender relationship is weakened as the borrower can sever relationship with one lender and still retain relationships with other lenders. Savings by borrower and provision of other financial services with a single MFI leads to deepening of ties between the lender and the borrower.

Additionally, Collections gimmick and late repayment was revealed by the findings as a moderate challenge. In Malawi, the procedures for pursuing unpaid debt obligations are well structured. But, even though legal procedures are in place for exercising the right of collateral, collection is difficult. There are few incentives for processing claims and capacity in the judicial system is stretched. Recognizing these limitations in pursuing unpaid debts, the Chamber of Commerce and professionals in the banking and legal industries have created a new mechanism to speed up the process of civil proceedings related to unpaid debts. Where possible to avoid a lengthy court proceeding, mediators will work with parties to develop legally binding agreements to resolve disputes (Burritt, 2006).

In Nigeria, research finding by Nwanyanwu (2011) established that about 70% of micro credits given to micro enterprises via government microfinance scheme were not recovered. Some people see the loans as their own share of the national cake and do not see any need for the repayment. Reference to the study by Loboyeski et al (2004), the same challenge was experienced in Malawi on public-owned MFIs which most of them collapsed due to the ever growing book of non-performing loans. Loboyeski et al (2004) concludes that the sustainable provision of microfinance services requires dedicated professionals whose job security depends on how well they perform; and this is extremely difficult to instil such feelings in bureaucrats from government or quasi-government institutions.

Furthermore, retaining existing customers which is also referred to as building customer loyalty was also determined to be a moderate challenge. Customer retention is an issue that creates a problem in growing an MFI. Research study by Churchill (2000) discusses the impact of customer loyalty and concluded that customer loyalty is key to MFI success. Customer loyalty was perceived as the primary driver of long-term financial success. If an MFI can retain a strong cadre of loyal repeat customers, it will be well on its way toward profitability. Research findings in India determined that there is only 28% customer retention in MFIs. This occurs because customers are not properly informed and educated about services and products (Nasir, 2013). From the findings of this research study the issue of customer retention cannot be understated in this industry.

The higher lending rates was also a challenge that is affecting the operations of MFIs in Malawi. Burritt (2006) concurs that high real interest rates in Malawi resulting from inefficiency in the banking sector and instability in the macroeconomic environment discourage financial sector development. High real interest rates lead to an inefficient use of productive resources in the economy and discourage the participation of low-income populations, particularly smallholder farmers, from taking advantage of productive opportunities that lay dormant. Generally, the position of higher interest rates has a bearing on the growth of MFI business in Malawi. It is a fact that the higher real interest rates are passed on in the value chain proposition. In concurrence, Kereta (2007) alludes that excessive interest rates may lead to MFI losses as borrowers cannot pay.

High operational costs were also determined by the research study as a moderate challenge. This is driven by small and irregular cash flows from customers. Nasir (2013) in his research study in India also found that high transaction cost is a big challenge for microfinance institution, for instance, volume of transactions is very small, whereas the fixed cost of those transactions is very high. The same findings were confirmed in Namibia by Mulunga (2010) where high operational cost impacted negatively on the efficiency of the MFIs, specifically, cost recovery was particularly constrained by the imposition of the Usury Act that stipulates the interest rate ceiling which is not the case with Malawi.

Low educational level of staff, which was also assessed as moderate challenge in this study reverberated with the Nigeria experience. Nwanyanwu (2011) attributes this to; low capacity and low technical skills on micro-financing as most staff recruited in the microfinance institutions, particularly at management level, have little or no experience in microfinance banking and practice. He argues that management of micro finance institutions would require a pedigree of knowledge on micro-financing to successfully operate in the industry. On the same note, Table 9 findings presents that most employees in the sector hold a diploma qualification which validates the existence of challenge in human resource quality.

Lack of proper identification and Know Your Customer (KYC) procedures was also indicated as a moderate challenge. In Malawi, there is no national identification system in place to define its citizenry. However, the national ID cards were launched in October 2016 with a pilot of 5,000 cards processed and printed. Finally, on the moderate side findings, there were also several challenges which included the issue of; unreliable loan repayment systems, unreliable infrastructure, poor customer service, and small and irregular cash flow.

4.4.2 Minor Challenges

All the findings in Table 14 present the minor challenges that are affecting the MFI operations in Malawi.

Table 14 Minor Challenges Faced by MFIs

No.	Challenges	SM%	MI%	MO%	SV%	Mean Score
1	Increased competition among MFIs	29%	27%	27%	17%	2
2	Poor selection & recruitment practices	32%	22%	41%	5%	2
3	Appropriate staff incentives/remuneration schemes	12%	29%	12%	46%	2
4	Lack of information about customers (adverse selection en-route to moral hazard)	10%	2%	78%	10%	2
5	Delivering what customers want (Customer focus)	39%	10%	51%	0%	2
6	Fraud	20%	5%	76%	0%	2
7	Skills development of staff (in microfinance)	12%	56%	20%	12%	2
8	Profit performance	10%	63%	7%	20%	2
9	Quality of loan book (risk delinquency & repayment default risk)	15%	17%	37%	32%	2

The challenge of competition is virtually absent and this is confirmed by research findings of Loboyeski et al (2004) as he argues that MFIs are concentrated in urban or peri-urban areas as compared to rural areas. The same applies to selection and recruitment and staff remuneration which are viewed as minor challenges. It can be argued that staff do not complain because most of them are diploma qualification holders and the income to qualification ratio is satisfactory. However, in Ghana the situation is different; Boateng (2015) cites that one of the major problems of the microfinance sub-sector is recruitment of effective and appropriate manpower. This they ascribed to the inability of the sector to adequately compensate personnel. Other human resource problems faced by microfinance institutions include lack of training opportunities and poor conditions of service. The quality of manpower in these institutions is reflected in the poor performance of many of them, inefficiency and high levels of frauds and forgeries. The institutions also suffer from high labour turnover a further indication of low staff motivation and poor personnel practices. In India, Kumar & Singh (2015), their findings concur with human resource challenges raised by Boateng (2015).

Lack of information about customers leading to moral hazard was also assessed as a minor risk to MFI business. Gyamfi (2012) study concluded that most of the techniques used for the management of credit risk by MFIs in Accra within the period (2004-2007) were not quite effective. It was also concluded that the best technique for determining the credit worthiness of clients was to study their character, savings and cash flow. It can be argued that if the Malawi case of adverse selection is not managed properly it can easily graduate into the Accra case of 2004 to 2007. There is also a despondent side to absence of proper information about customers. Customer related problems refer to problems relating to the target segment of an MFI. Volschenk et al (2005) argues that the success of MFI growth is higher where service quality to customers is good. Lack of information about clients affects MFIs' focus that is necessary for development of financial products attractive to low-income clients as well as retaining of the existing clients. Tanzania MFIs were failing to grow because of lack of information about their customers.

The other minor challenges include; skills development of staff, quality of loan book, fraud and profit performance. The challenge of skills development of staff corroborates with the findings in Table 9 suggestive of low education levels of MFI staff. According to Chambo (2004), on quality of loan book, fraud and profit performance, as cited by Volschenk et al (2005), they contend that, failure to maintain good quality of loan books lead into delinquency risk, credit risk and payment default risk. Frauds such as corruption, embezzlement, misappropriation and theft of assets emphasized by Otero & Rhyne (1994) as performance challenges have resulted into high administration costs detrimental to MFIs' growth. These MFI challenges though found to be small in nature can easily affect the growth of MFIs in Malawi.

4.5 Solutions to MFIs Challenges

Table 15 presents the findings on suggested solutions to MFIs' prevailing challenges. These resolutions were sourced from the key managers of MFIs.

Table 15 Suggested Solutions towards MFI Challenges

Count	Suggested Solutions to MFI Challenges	Frequency	Percentage
1	Availability of loans from Reserve Bank of Malawi like what it does with banks.	33	81%
2	Availability of National IDs to mitigate the problem of identifying customers.	31	76%
3	Greater support from the banking industry to access finance.	23	56%
4	Setting of credit reference bureau which will help in identifying defaulting customers and check their character/credit history before disbursing a loan	22	54%
5	Intervention of the Malawi Government in creating an enabling environment where there are reliable loan repayment systems in the financial industry; this can be a catalyst for fast industry growth and achievement of financial inclusion.	20	49%
6	Employer character reference check before offering a recruit a job; this will help reduce theft by staff within the MFIs.	19	46%
7	Setting strong internal controls to help in reducing the rate of fraud.	17	42%
8	More control must be invested in customer selection process to mitigate issues of adverse selection which creates the risk of moral hazard (diligent customer scrutiny).	15	37%
9	A more efficient Government of Malawi payroll system that collates MFI deductions to ensure comprehensive total payment information.	12	29%
10	A vibrant and strong macroeconomic environment should be built by Malawians with government of Malawi providing clear direction and drive and political will	10	24%
11	There is need for a financial services hub which will help MFIs source information about customers and the market they are operating in. This will help a lot in addressing issues of adverse selection and moral hazards.	5	12%
12	Sensitization of the public on issues concerning attitude change towards MFIs and their operations.	4	10%
13	Media to sensitize members of the public to appreciate the importance of repaying loans.	2	5%
14	Proactive and selfless cultures in organizations focused on creating more customer oriented services.	1	2%

In the findings on the extent of the MFI challenges, lack of adequate capital was pronounced as a fundamental problem (Refer Table 13). Corroboratively, in Table 15; the respondents (81%) alluded that there is need for an organized fund (loan pool) to be managed by the central bank that can be accessed by MFIs. One of the severe challenge facing microfinance institutions in Malawi is the lack of finance needed to expand financial services to clients. The same situation has not spared Tanzania. Volschenk et al (2005) provides the problem itself and the solution. He contends that, the lack of enough capital to lend to clients is globally one of the most severe problems inhibiting the growth of MFIs. To some extent MFIs can use the deposits by clients to increase its loan book, but this option is often limited in poor communities. In order to expand programs, MFIs need access to a stable and an ongoing source of funds for MFIs to achieve sustainable growth.

Following this; the issue of introduction of national identification (IDs) was raised (76%) as a direct mitigant to formalizing the documentation of customers which presently is very tricky. Even in South Africa, Legadima (2012) reasons that to process loans and to complete transactions with clients, MFI requires identification documents and information like proof of address from clients. Most of the time the customers do not have access to services for obtaining these documents, which eventually leads to customers being denied credit. This is caused by the lack of a reliable address system, which is another hindrance to MFI services and work. In Malawi, the key MFI managers lobby for quick rolling out of the national registration system which will give birth to national identification cards.

The concept of establishing Credit Referencing Bureaus (CRBs) was supported by 54% weight of key managers of MFIs as they assumed that it can greatly assist in identifying delinquent customers before approving a loan (managing adverse selection). This point was linked to creation of National Information System (financial processing hub) which would house a database for all MFIs in Malawi (12%). Mwangi (2014) deduces that competition among MFIs signifies major institutional factor influencing over-indebtedness especially where there are no credit bureaus. The need for CRBs in this case cannot be overstated.

The MFI players (56%) also felt that the commercial banking sector has a role to render support to the MFIs by providing access to capital debt financing. Under capitalization issues presented in Figure 11, the finding confirmed that 90% of MFIs are funded through private equity and other means. MFIs also felt that GoM has a fundamental role to play in creating an enabling environment for the operations of MFIs (49%). This was in direct connection to reliable infrastructure in loan repayment system, a more efficient government payroll system (29%).

Other solutions raised were; awareness or sensitization campaigns to change mindsets of customer towards their negative attitude on MFI operations (10%). This was linked to the background to MFIs in Malawi which is primarily dominated by state-run MFIs. Such attitudes have led to the winding up of Development of Malawian Enterprise Trust (DEMAT), Small Enterprise Development Organization of Malawi (SEDOM), among others, due to high delinquency levels. Kereta (2007) pointed out that loan repayment (measured by default rate) could be another indicator for financial sustainability of MFIs; because, low default rate would help to realize future lending.

Finally, the challenge of shifting industry culture to incline towards customer-orientation or market-driven was also proposed as a progressive idea (2%). This according to MFIs' key managers, this could be resolved through staff trainings or orientations regarding the essence of micro-financing and its best practices. Such intervention could avert the Ghanaian situation explained by Boateng (2015) which is infested with copying, competing and mimicking the practices of universal banks. These are hangover effects of managers and management who were universal banks' staff who were either retired or sacked. Such staff look at MFIs as an extension of conventional banking they know, so they refuse to understand microfinance.

4.6 Chapter Summary

This chapter has presented the findings and discussion of the research study in which a number of issues have been exposed. Notable areas being the performance of the microfinance sector in Malawi covering a 3 years' period (2013 to 2015). Industry composition has only 25 licensed MFIs. The value of loans disbursed has been steadily increasing year on year representing 410% increase in the period under study. The average number of loan officers has declined amidst an increase in PAR. The rise in the PAR value correlated with the negative industry growth rate in 2015 of -3.8%. Attributes of MFI functionality in terms of governance, operations, marketing, capitalization and staff related issues have also revealed problems affecting micro-financing. Severe challenges affecting microfinancing bordered on inadequate capital and weaker legislation/regulatory framework. Other challenges were rated as moderate, minor to small. Finally, suggested solutions to MFIs' challenges included availability of loans from central bank to be accessed by licenced MFIs.

CHAPTER 5-CONCLUSION AND RECOMMENDATIONS

5.1 Introduction

The objectives of this research were to determine the prevailing performance of MFIs in Malawi based on industry reports, to identify the challenges that the MFIs are facing in Malawi when extending financial services to their customers and to generate solutions to alleviate the established challenges affecting MFI operations in Malawi.

5.2 Conclusion

The conclusion section presents the findings from the set objectives of the study.

5.2.1 Prevailing Performance of the MFIs in Malawi

Malawi has a total of 26 MFIs which is a smallest number as compared to her neighbouring countries; for instance, Tanzania has 41 and Zambia has 46. Generally, Malawi has a long way to go to increase the number of registered MFIs. However, the value of loans has quadrupled over the three-year period of 2013 to 2015 to MK58bn from MK13bn.

Nevertheless, the volume of loans disbursed over the same period does show growth. The figures have just been stable, but at the same time showing a sharp decline in 2015. This is indicative of an industry that is not recruiting new business but rather focusing more on existing customers through issuance of re-loans. The average number of Credit Officers or Loan Officers also imitate the same trend which appears on volume of loans. In 2015 the numbers of these officers are on the decline as compared to 2014.

The industry’s portfolio quality and management report depict a rising Portfolio at Risk (PAR) to MK28.5bn in 2015 from MK13.2bn in 2013. This is distressing as it is sending the signal to potential investors and the regulator that there is a general challenge on on-time repayment. The levels of defaulting customers are on the rise. If the PAR is not prudentially managed, MFIs’ sustainability of operations will be remote.

The growth of MFIs by assets has grown to MK30.5bn in 2015 from MK11.6bn in 2013. The year-on-year growth rates have been very positive 8% in 2013, 172% in 2014 to -3.8% in 2015. However, 2015 has presented a picture of negative growth which corroborates with the issue of growing PAR which is not healthy for the industry. In the MF sector if the PAR increases there is a rise in impairment which eats into the capital investment of the shareholders. A rise in loan impairment negatively affects the growth pattern of industry assets.

5.2.2 Challenges encountered by MFIs

It can be concluded that the microfinance industry in Malawi is severely affected by two critical challenges. These are; lack of adequate capital to lend to its customers and legislation and legal framework. Hear it is envisaged that if Malawi can have conducive legal instrument that are reinforced; issues of fraud, default, theft among others will be controlled. The same can be said of access to soft loans (using the base rate) facilitated by GoM, through RBM, for debt-financing can address the challenge of capital adequacy. From the composition of MFIs in Malawi, it is very clear that most of them are NDTMFIs (Refer to Appendix 1), meaning that they cannot mobilize capital through deposits.

The research study also found out that most challenges in the industry are moderate in nature and direct off-shoots of the severe challenges. Where an MFI is faced with challenges related to; financial constraints, weaker legislation and legal instruments; poor ICT, loan collections gimmick, high lending rates, customer retention, quality of staff, high operational costs, unreliable transport and communication infrastructure, recruiting new customers, among other areas; their sustainability and profitability will continually be challenged. The verdict is that if the moderate challenges are left unaddressed they can negatively affect the growth of the MF industry.

The study also concluded that there are minor challenges which if left unattended they can also graduate into inhibitors for the growth of MFIs. Among them are competition, human resource factor related to skills development, poor selection and recruitment, adverse selection of customer and customer care, fraud and quality of loan books. Research studies in Ghana, Kenya, Ethiopia and Nigeria have alluded to the same challenges as being detrimental to the growth of MFIs.

5.2.3 Solutions towards the Challenges

Unequivocally, concerted efforts are required from all stakeholders including; government, the MFIs, customers, media, the regulator (RBM), among others, to make the industry more robust. Some of the solutions raised were; availability of cheaper loan from RBM to MFIs, institutionalized national ID system to ease customer identification, setting up of CRBs to check creditworthy of potential customers, enhanced loan repayment systems, employee character check before recruitment, strengthening internal control in MFIs, establishment of a one-stop virtual financial processing hub for all MFIs, positive use of the media to raise awareness about MFI operations, and orientation of the business towards customers and the essence of micro-financing (market-led MFIs).

5.3 Recommendations

The following are some of the recommendations made by the report: -

The Financial Services Act (2010) which is a father legislation to all financial institutions in Malawi should be amended to criminalize defaulting customers. The same should be enforced at all levels in order to ensure that customers take their full responsibility for not honouring contractual loan servicing. High levels of loan delinquency scare off potential investors in MFIs.

The government through RBM should hasten the establishment of the National Financial Services Hub which will house all registered MFIs' Information Systems (IS) though integration. According to Mattacks (2005), strategically and operationally, such an enhanced IS platform improves the ways products and services are supplied to customers.

MFIs should adopt entrepreneurial ways of sourcing funding other than predominantly relying on private equity of their shareholders. A typical American Finance Company has assets and liabilities comprising; bank loans, Commercial Paper, Debt-both Short-and Long-term (Saunders & Cornett, 2014). Provision of debt instruments allows the MFIs to operate in a more sustainable and profitable way. Room for growth and expansion of MFIs is guaranteed beyond the equity of shareholders.

MFIs in Malawi should establish solid Corporate Governance (CG) structures within their set-up if they are to achieve sustainability. Numerous studies conclude that well-governed companies worldwide perform better in commercial terms. Adopting corporate governance best practices has the potential to improve access to external financing, lowers the cost of capital, improves operational performance, increases firm valuation, improves share performance, reduces the risk of corporate crises and scandals (International Finance Corporation, 2008).

In terms of risk management, the GoM must speed up the issue of introduction of national IDs. If this is distant, as a short-to-medium term measure, Civil Service should have officially-employer-issued identification cards with relevant security features.

The MFIs have a task of widening their product offering to their customers. Investment in new products research and development can answer both the impasse of poor customer service and absence of customer centricity approach emanating from lack of broad-based approach to the microfinance market. Some financial products fit for exploration could be customer savings (deposit-taking), micro-insurance, financial advisory, micro-leasing, transfer and payment services (e-money).

Alternative innovative distribution channels should be explored by MFIs. The prospective networks should be ones that are inter-operable, scalable and sustainable in both medium to long term. The Mobile Network Operators (MNOs), for example, can play a crucial role in expanding outreach of MFIs. The design of virtual platform can allow customer to access financial services in the remotest (hard-to-reach) locations through appropriate technology.

Staff related issues should be given a strategic position in the growth and development of MFIs. Staff should be paid competitive remuneration and incentives, human resource development should be administered through; up-skilling, refresher training and conference training. Such trainings will ensure that intellectual capital of the organization is advanced, effectively utilized and retained.

5.4 Issues for Further Research

Some of the issues that can be explored for further research are: -

Explore the demand-side challenges faced by customers in their pursuit to access financial products from MFIs (Financial Inclusion).

Critical assessment on the role of Corporate Governance in MFIs in Malawi relative to sustainability and profitability.

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APPENDICES

Appendix 1. List of Registered MFIs in Malawi as at 31st April 2015

Category	**MFIs**
A	**MCAs**
1	Business Finance Solutions
2	Saile Financial Services
3	Umunthu Microfinance
4	Greenroot Finance
5	Moyowathu Financial Services
6	TEECs
7	DF Agency
8	GetBucks Malawi
9	National Association of Business Women
10	FEDOMA Microfinance Project
11	Fountain Microfinance
12	Citizen Microfinance
13	EPIK Finance Limited
14	Ecological Research and Outreach Initiative Ltd.
15	Green Gold Finance Ltd.
16	Foundation for Irrigation and Sustainable Development
B	**NDTMFIs**
1	Pride Malawi
2	Greenwing Capital Financial Services
3	Microloan Foundation
4	CUMO Microfinance
5	Blue Financial Services
6	Easy Loans
7	Select Financial Services
8	VisionFund Malawi
9	Foundation for International Community Assistance (FINCA) Ltd.

Source: adapted from Press Release; The Daily Times, Monday June 1, 2015

Appendix 2. Questionnaire for Managers

Questionnaire for MFIs	
Respondent:	***Position:***
Organization:	***Date:***

Purpose of the study: *This is strictly an academic study by Kisa Mwelefu Kalolokesya (Tel. 0999659680), a student at the University of Malawi, Polytechnic. The data being solicited shall be used strictly for academic purposes and will be treated with utmost confidentiality. Your kind and very valuable response shall be highly appreciated.* ***Thank you.***

1. Type of Microfinance service provider (Tick √ the appropriate service)

NGO ☐
SACCO ☐
NDTMFI ☐
MCA ☐
Commercial Bank ☐
Other ☐

2. Years the MFI started operations in Malawi (Tick √ the appropriate service)

Under 5 Years ☐
6 to 10 Years ☐
11 to 15 Years ☐
16 to 20 Years ☐
Above 20 Years ☐

3. Which financial products do you offer? (Tick√ the appropriate service)

Credit ☐
Savings ☐
Insurance ☐
Other ☐

4. Does your organization provide a service to? (Put a tick√ in the appropriate block):

Only Women	☐	Only Men	☐	Both	☐
Only Groups	☐	Only Individuals	☐	Both	☐
Only Employed	☐	Only Unemployed	☐	Both	☐
Small business	☐	Larger business	☐	Both	☐

5. What is the source of your financing? (Tick√ where applicable)

Donors ☐
Private Equity ☐
Member Savings ☐
Government ☐
Others ☐

6. Number of borrowers (clients)/individuals and groups who had received loans to-date?

Individual ☐ Groups ☐

7. Number of Branches/offices/outlets providing Microfinance services (put the figure)

1-4 ☐

5-10 ☐

11-15 ☐

16-20 ☐

Above 20 ☐

8. Number of Districts covered

1-4 ☐

5-10 ☐

11-15 ☐

Above 20 ☐

9. (a) Do you have new products/services that support inclusive microfinance targeting the socio-economically unserved groups (the ultra-poor). Please indicate <u>"Yes" or "No"</u>

Yes ☐

No ☐

(b) If the answer if <u>"yes"</u>, what threshold of your loan book is reserved for the financial inclusion of the ultra-poor segment?

1%-5% ☐

6%-10% ☐

11%-20% ☐

Above 20% ☐

10. Indicate in which monthly income group the majority of your clients fall in? (Tick only one)

Below MK40,000 ☐

>MK40,000≤MK100,000 ☐

>MK100,000≤MK200,000 ☐

Above MK200,000 ☐

11. Describe the <u>characteristics</u> of your MFI governance system?

Characteristics/attributes of MFI governance system	(Tick √ where in place, and put **X** where not in place)	Year when put in place
a) Existence of clear equity holders and their capacity to provide more capital		
b) Existence of instruments specifying the rights and responsibilities of equity holders		

c) Existence of competent Board and leadership		
d) Existence of independent Board of Directors		
e) Existence of independent Board committees		
f) Existence of term limit for Board of Directors		
g) Existence of Code of Conduct for the Board of Directors		
h) Separation of responsibilities of the Board Chair and Chief Executive of the organization		
i) Existence of mechanisms for internal controls including organization structure, systems, policies and procedures		
j) Existence of strategic plan indicating clearly the mission and objectives		
k) Existence and implementation of a framework for: setting objectives, ensuring the objectives are met, assessing performance and for rewarding/sanctioning performance		
l) External factors that include the existence of a sound and regulatory framework for equity holders		

Source: (Volschenk et al., 2005)

12. (a) Describe the Board of Directors composition (How many are in each category)

Total Number by category

Nationality (Local or Foreign)	L	F
Gender	M	F

(b) Other specific attributes (Give a count on each category by tallying //// where applicable.)

Accounting	
Legal	
Business	
Commerce	
Other	

13. How would you rate the following risks associated with MFI operations?

Ranking Codes

1-Small risk

2-Minor risk

3-Moderate risk

4-Severe risk

5. No a problem

Client selection	
Product risk	
Portfolio composition	

Loan processing and information management

14. What is the number of staff employed? (Put a tick√ where appropriate)

Less than 10

10 to 20

20 to 30

30 to 40

Above 40 & more

15. In the past 12 months how high was your staff turnover? (Put a tick√ where appropriate)

Greater than 50%	High	
Greater than 20% & less than 50%	Moderate	
20% and less	Low	
Does not apply	Not applicable	

16. Please indicate the education level of your microfinance management staff?

Most have MSCE

Most have Diploma

Most have a University Degree

Most have a postgraduate Degree

17. Please indicate whether (<u>Yes or No</u>) if you currently experience the following factors/problems as challenge in your organization.

If your answer is "<u>Yes</u>", please rank that factor/problem by putting a tick against a relevant code concerning to which extent does that factor/problem affect operations of your organization.

4 - The factor is a severe problem.

3 - The factor is a moderate problem.

2 - The factor is a minor problem.

1 - The factor is a small problem.

Problem/Challenge	**"Yes" or "No"**	**1-Small Problem**	**2-Minor Problem**	**3-Modertate Problem**	**4-Severe Problem**
a) Quality of loan book (risk delinquency & repayment default risk)					
b) Fraud					
c) Increased competition among MFIs					
d) Theft by staff					
e) Double-dipping by customers (multiple borrowing from other MFIs)					
f) Service quality to customers (attracting new customers)					

g) Lack of information about customers (adverse selection enroute to moral hazard)					
h) Profit performance					
i) High operational costs					
j) Small and irregular cash flows from customers					
k) Delivering what customers want (Customer focus)					
l) Customer identification (IDs & KYC)					
m) Retaining existing customers (building customer loyalty)					
n) Educational level of your customers (effect on understanding the financial products)					
o) Education level of staff					
p) Skills development of staff (in microfinance)					
q) Lack of adequate capital to lend to customers					
r) Poor selection & recruitment practices					
s) Appropriate staff incentives/remuneration schemes					
t) Legislation & regulatory framework					
u) Unreliable infrastructure (Poor transport, communication, IT, etc.)					
v) ICT usage in MFI					
w) Inadequate funding /or capital financing (funding hitch)					
x) Unreliable loan repayment systems (i.e., bank debit orders, mobile money operations, government procedures etc.)					
y) Higher lending rates					
z) Collections gimmick and late payments					

Source: (Volschenk et al., 2005)

18. Suggest measures that can be put in place to mitigate the problems or challenges faced by MFIs?

Thank you!

Appendix 3. Portfolio Report

Portfolio data	***2012***	***2013***	***2014***
1) Total value of loans disbursed during the period			
2) Total number of loans disbursed during the period			
3) Number of active borrowers (end of period)			
4) Portfolio outstanding (end of period)			
5) Average outstanding balance of loans			
6) Value of payments in arrears (end of period)			
7) Value of outstanding balance of loans in arrears			
8) Value of loans written off during the period			
9) Average initial loan size			
10) Average loan term (months)			
11) Average number of credit officers (loan officers) during the period			

Source: Rosenburg, Mwangi, Christen, & Nasr (2003)

Appendix 4. Portfolio Quality and Management Report

	Outstanding principal balance	
Normal loans	***Portfolio at risk (%)***	***Amount***
Current		
a) 1–30 days late		
b) 31–60 days late		
c) 61–90 days late		
d) 91–180 days late		
e) More than 180 days late		
Subtotal		
Rescheduled & refinanced loans		
Current		
a) 1–30 days late		
b) 31–90 days late		
c) More than 90 days late		
Subtotal		
Total		

Rosenburg, et al. (2003)

Appendix 5. Growth of MFIs in Malawi

	2012	***2013***	***2014***
Assets			
(K'bn)			
Growth rates (%)			
Number of MFIs			
Of which			
MCAs			
NDTMFIs			
Licenced DTIs			
Banks with microfinance window			
Not classified			
Number of SACCOs			
Provisionally licenced			
Fully licenced			
Not provisionally licenced			

Source: Reserve Bank of Malawi (2013)

Appendix 6. Academic Research Student Introduction Letter

UNIVERSITY OF MALAWI

PRINCIPAL
Professor Grant Kululanga, PhD. Eng., MSc. Eng., BSc. Eng., MASCE

Please address all correspondence to the Principal
The Malawi Polytechnic
Private Bag 303
Chichiri
Blantyre 3
MALAWI
Tel: (265) 01 870 411
Fax: (265) 01 870 578
E-Mail: principal@poly.ac.mw

Our Ref.: 34/F/2
Your Ref:
Date: 07th January, 2016

TO WHOM IT MAY CONCERN

ASSISTANCE TO CARRY OUT AN ACADEMIC RESEARCH FOR MBA DISSERTATION: *MR. KISA MWELEFU KALOLOKESYA*

I write to certify that ***Mr. Kisa Mwelefu Kalolokesya*** is a University of Malawi Postgraduate student who is pursuing a Master of Business Administration Degree course at the Polytechnic.

One of the important requirements of this degree programme is that students carry out research project known as dissertation in the final semester. This introduces the student to the methodology of research, the systematic analysis of ideas, the problems of data collection and the presentation of ideas in a clear and coherent way. ***Mr. Kisa Kalolokesya*** is currently working on his MBA dissertation titled **"An Analytical Case of Microfinance in Malawi Focusing on the Supply–side Issues and Challenges".**

I am therefore writing to ask for your kind assistance in allowing ***Mr. Kalolokesya*** access to carry out his research in your organization and help him with any information/literature that your organization may have on the topic of his dissertation.

Your assistance in this matter will be of greatest importance and highly appreciated and any information that may be provided will be treated with utmost confidentiality.

E.J. SANKHULANI, PhD
MBA COORDINATOR, MANAGEMENT STUDIES DEPARTMENT

Appendix 7. RBM Permission Letter

RESERVE BANK OF MALAWI

TEL: (265) 1 820 299/820 444
FAX: (265) 1 820 527
WEBSITE: http://www.rbm.mw
EMAIL: reserve-bank@rbm.mw

BLANTYRE BRANCH
10 HANNOVER AVENUE
P O BOX 565
BLANTYRE
MALAWI

10 March 2016

MBA Coordinator, Management Studies
The Malawi Polytechnic
Private Bag 303
Chichiri
BLANTYRE 3

Dear Sir

ASSISTANCE TO CARRY OUT ACADEMIC RESEARCH FOR MBA DISSERTATION: MR KISSA MWELEFU KALOLOKESYA

Reference is made to your letter dated 7th January 2015 on the above subject matter.

Please be advised that Mr Tosh Mwafulirwa has been assigned to assist Mr Kalolokesya in acquiring information from the Bank for his academic research. Mr Mwafulirwa can be contacted using the following email address: tmwafulirwa@rbm.mw.

Yours faithfully

Mtchaisi Chintengo
FOR DIRECTOR, MICROFINANCE AND CAPITAL MARKETS SUPERVISION DEPARTMENT