Impact of Microfinance Regulations on Microfinance Institutions' Performance in Tanzania

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Abstract

In this paper, we examined the impact of newly established regulations on sustainability and outreach performance of Microfinance Institutions' (MFIs). We argue that any newly established regulations for MFIs are expected to enhance their sustainability and outreach performance, otherwise, the reverse may be true. The study focused on problems, practices, problem solution and contribution to future practices of new regulations based on the theory of development. Thus, the study employed inductive approach to collect qualitative data using in-depth interviews and focus group discussion. The study findings revealed that that new regulations in Tanzania have been inadequately designed with inadequate participatory environment during policy formulation. This led to limiting the number of licensed MFIs and new entrants in the financial sector, which, in turn, affected the sustainability and outreach performance of the MFIs. The provisions also seem to discourage MFIs members and investors through significant political interference from the government by imposing the impractical interest caps which have led to MFIs operating under stiff and frustrating conditions. The study concludes that, MFIs operations in Tanzania are mired with inadequate design of regulations causing inadequate outreach performance of most of MFIs. This situation has far reaching practical implications for stakeholders in the MFIs sector and the regulators who play essential roles in policy formulation where MFIs expect some necessary amendments. As such, there is a need to adequately involve stakeholders in policy formulation, to review interest cap rates, and a balanced political involvement in policy making which will again attract new entrants and encourage more funding for MFIs.

Keywords: Microfinance Regulations, Microfinance Institutions Sustainability, Outreach Performance, Participatory Environment, Corporate Governance.

1.0 Introduction

Globally, from the end of 20th century to present moment has marked many reforms in developed and developing countries. These reforms were associated with various structural adjustment programmes reflected in public administration trends related to New Public Management/Governance (NPM), re-inventing the government and related trends. They (reforms) categorically entailed how best governments should conduct their business. The introduction of Performance Management Systems (PMS), Public Private Partnerships (PPP), corporate governance, decentralization of business, and citizen involvement were the main tenets of the reforms. Consequently, reforms in finance, human resource, procurement and enterprise development were given due attention.

Like many other developing countries, Tanzania undertook various financial sector reforms as advised by Bretton woods institutions such as International Monetary Fund (IMF) and The World Bank (WB). The objectives were, among many others, to reform the commercial banks for operations performance, diversify ownership of banks, make financial restructuring, and reform financial institutions. These initiatives were meant to expand a pool of resources available for investment, to reform other financial institutions so as to improve customer services and ensure financial viability, integrity and sustainability. Succinctly, these reforms aimed at liberalizing the banking sector. Given the reforms and the attendant liberalization of the banking sector, Tanzania witnessed a mushrooming of Microfinance Intuitions (MFIs). However, the establishment of MFIs was marred with inadequate regulatory framework to guide their operations (URT, 2000). This omission was inconsistent with Satta (2004) who commend for the creation of regulatory framework for effective functioning of MFIs. The argument is that the regulatory framework would provide a conducive environment for sustainability and outreach performance of MFIs. In this paper, we offer an insight on financial reforms centred on newly established regulations and their impacts on sustainability and outreach performance of MFIs.

With the structural adjustment programme (SAPs) of 1990s to 2000s, and the NPM approach, the financial reforms entailed a review of the structure, organization procedures, operational arrangements, and policy issues related to the finance sector. Consequently, there was a need to introduce prudential regulations such as capital and liquidity requirements and the need to streamline the banking industry to include the enactment of Banking and Financial Institution Act of 1991. The aim of this Act was to provide for capital, liquidity and licensing requirements of new banks and financial institutions, and liberalization and rationalization of interest rates. Thus in 1992, Tanzania enacted the Foreign Exchange Act, which led to the Liberalization of foreign exchange and interest rates. In addition, the Government enacted the Bank of Tanzania Act of 1995 whose aim was to enhance supervision and regulations of the banks and Microfinance Institutions. Of recent, the Central Bank of Tanzania issued the Microfinance Business regulations in trio. They contain Microfinance (Non-Deposit to cater for Microfinance Service Providers) Regulations, Microfinance (Savings and Credit Cooperative Societies) Regulations, and Microfinance (Community Microfinance Groups) Regulations of 2019. Therefore, the most important tenets of the financial sector reforms was related to the liberalization of interest rates, elimination of administrative credit allocation, strengthening of the Bank of Tanzania's role in regulating and supervising financial institutions. In this study, we assessed the extent to which new regulations (resulting from financial reforms) have influenced the sustainability and outreach performance of MFIs in Tanzania.

Some studies on MFIs regulations in Zambia and Nigeria emphasized the appropriateness of designing special MFIs regulation to meet social goals (Siwale & Okoye, 2017). A study by Lucky Yona and Eno Inanga (2014) examined the impact of change in banking regulations and supervision on competitiveness among Tanzanian commercial banks in respect of service quality. The study findings revealed that there is little positive significance correlation between reforms on the banking regulations and banking competitiveness in respect to service quality despite that private banks were leading ahead of semi-quasi banks. Another study by Temu (1998) investigated the impact of the financial sector reforms on the financing of small and micro enterprises (SMEs) in Tanzania. The study concluded

that further innovations in the financial sector are needed so as to increase access of SMEs to credit and savings services. The innovations may either be in the form of institutional linkages between formal financial institutions and other financing agencies, the adoption of collateral substitutes or the establishment of financial transactions between large and small businesses.

While there are various studies on the impact of financial regulations, there is inadequate evidence regarding the post-regulation experiences of MFIs given new regulations especially at their infancy stage. Therefore, this research paper examined the preliminary effects of the new financial regulations on sustainability and outreach performance of MFIs in Tanzania. The study variables included the impact of observing corporate governance principles, stakeholder engagement in policy making, political interference in MFIs operations, and sources of capital for MFIs, the attraction of new investors, and the effects of regulations to new entrants. After this brief introduction, section two reviews literature, section three provides the methodology, section four presents the study findings followed by discussion of the findings in section five. Section six concludes the study and provides policy implication.

2.0 Literature Review

This section reviews the literature on what microfinance and MIFs entails, MFIs regulatory framework in Tanzania, the empirical literature, and the conceptual framework for the study.

2.1 Microfinance Institutions

The United Nations define micro finance as the provision of small-scale financial services such as savings, credit and other essential financial services to poor and low-income people. Hence, MFIs refers to institutions (including non-governmental organisations) such as credit unions, cooperatives, private commercial banks, non-bank financial institutions and parts of the state-owned banks which provide essential financial services to poor and low-income people." While micro finance and micro-credit may be considered synonymous, micro-credits deal with the provision of credit to small businesses whereas microfinance refers to a broader synergic set of financial products, including credit, savings, insurance, and sometimes money transfer (Bogan, 2008). Microfinance can be classified depending on their organisation structure (cooperatives, solidarity groups, rural or village banks, individual contracts, and linkage models) or on their legal status (NGOs, cooperatives, registered banking institutions, government organisations, and projects) or according to their capital adequacy standards (from Tier 1 mostly regulated MFIs to Tier 4 start-up MFIs) (Deutsche Bank, 2007).

MFIs' main objective is to reach the underserved and poorest customers through mixing unorthodox techniques such as group lending (Yunus & Jolis, 1999) and monitoring, progressive lending (if repayment records are positive), short repayment instalments, and deposits. They go for frequent repayments (short-term instalments, starting immediately after disbursement), which is another smart pragmatic device of avoiding failure of repayment due to financial illiteracy of the lenders. Microfinance go for meeting customers at home. In this context, branchless business-like mobile banking came into operations.

These services are also characterized by lacking guarantee/collaterals. Therefore, they are concerned with progressive loans, which are accordingly divided into regular instalments which can be cashed by the borrower only if previous repayments have been made. Henceforth, to do this business there is a need to be regulated by the government.

2.2 Microfinance Regulatory Framework in Tanzania

To understand MFIs in Tanzania one needs to look at the National Microfinance Policy of 2000 and the review of 2017 that describe microfinance as necessary entities for the provision of microfinance products and services. Microfinances are specifically micro-savings, microcredits, micro insurance, micro-housing, micro leasing, and other financial related services to individuals and community groups or SMEs. For over 20 years, MFIs have been considered as optional tools for the alleviation of poverty through access to finance by financially excluded groups and the poor (Armenda´riz de Aghion & Morduch, 2005 cited in Barry & Tacneng, 2014). It is during this time that Tanzania had relatively new financial institutions with twenty licensed banks and eleven non-bank institutions (Gallardo et al., 2005). As such, while the financial services to micro-lenders, SMEs, and households were offered mainly by the three categories of registered financial institutions, the regulatory requirements were still emerging due to the infancy of the sector (Gallardo et al., 2005). Therefore, the situation was characterized with numerous MFIs (regulated and non-regulated) and inadequate regulatory system. Mackie, Smith and Msoka (2015) view this as inadvertent lack of a coordinating body in charge of microfinance. In realising this deficiency, the Ministry of Finance formulated the National Microfinance Policy (NMP) 2000, which established reasonable standards for microfinance operations. In a sense, the policy adopted the non-interference approach where prices or interest rates are to be identified and set by the MFIs, which had to prepare their own policies, free from political interference. MFIs capital and other entry requirements were categorized depending on the scope of operations (National Microfinance Policy 2000).

While the NMP of 2000 was not accompanied by legal framework, it intended to strengthen the financial market structure, which consequently led to the enormous change in the landscape of the financial sector and eventually enhanced the contributions of MFIs including international MFIs (National Microfinance Policy 2017) to the economic wellbeing of the people. The flourishing of MFI led to review of NMP of 2000 in 2017, whose objective was to promote financial inclusion by creating a conducive environment to allow the growth of appropriate and innovative MFI products and services that meet the requirements and needs of the poor and expedite poverty reduction. The policy addressed some issues that emanated during the implementation of National Microfinance Policy 2000. These included high-interest rates, inadequate consumer protection, and inadequacy of capital, poor outreach, and lack of regulatory framework. Hence, in 2018 the Central Bank issued the regulations to regulate the microfinance business in Tanzania. Therefore, the establishment of NMP of 2000 and the attendant amendments of 2017 base on Adams and Tewari (2020) observation that the regulations ought to ensure fairness and promotion of development in the microfinance sector. For them, the regulations always create access to capital, deeper outreach, improve control and reporting standards, stimulate innovation on financial products, and enhance legitimacy in the financial sector, thus contributing to financial sustainability to MFIs.

2.3 Related Studies

Some studies have focused on the effect of new MFIs regulations; for example, Satta (2004) reveals that regulating microfinance institutions' operations and activities provide part of the solution to borrowers with difficulties in sourcing finance. They restrict formal financial institutions from providing full-scale microfinance services such as limits on unsecured lending. According to Satta (2004), the regulations should be enacted to deposit-taking MFIs and allow the creation of a particular regulatory framework to introduce large-scale savings mobilization schemes, which are likely to strengthen MFIs' sources of funding. On the other hand, a study by Blavy, Basu and Yülek (2004) on the experience of microfinance in Africa reveals that the performance of MFIs depends critically upon having autonomy in decision-making of the management such as setting interest rates to achieve reasonable profit-making business and avoiding nonperforming loans.

In another study, Gallardo et al. (2005) observe that regulatory framework for MFIs should be accompanied by complementary modifications of other business laws and regulations, especially in taxation, contract enforcement, collateral registration, securities regulations, and consumer protection. They insist on clear differentiation by regulators and supervisors on deposit-taking. According to Gallardo et al. (Ibid), MFIs with financial soundness need to verify through prudential supervision. Again, MFI need be registered and subjected to "perceived" non-prudential regulations and standards such as submissions of audited statements, consumer information, and the like.

A recent study by Adams and Datt Tewari (2020) reveals that deposit mobilization is crucial in MFI operations, and the understanding of how regulation impacts their social and financial performance is critical in enhancing their survival. The study reveals further that regulation has significant negative impacts on MFIs' broader outreach performance (breadth) and suggests the provision of grants to MFI or subsidized loans to help them reach out many poor borrowers for them to achieve the outreach goal.

A study by Siwale and Okoye (2017) examined the impact of new microfinance regulations in Zambia and Nigeria and found that the regulations have not supported the emergence of sustainable MFIs (especially in Zambia) and even not accelerated the sectors' outreach to the poor. This study notes that the significant political interference and poor regulation have led to unintended consequences to the sector, and increased the barrier to the primary goal of extending financial services to the poor. Another study by Erasmus (2013) who evaluated the performance of Microfinance institutions in Tanzania by integrating financial and nonfinancial performance metrics. The overall findings indicate that the financial performance indexes show that commercial banks outperform traditional Microfinance institutions.

From these studies, we note that while they (studies) have observed the need to establish regulatory framework and their importance on MFIs, they did not address the post-regulation experiences from both the MFIs and regulators in countries where microfinance regulation is still in its infancy stage. This research sought to provide an empirical contribution to the understanding of the appropriateness of newly established regulations and their impact on sustainability and outreach performance of MFI.

2.4 Conceptual Framework

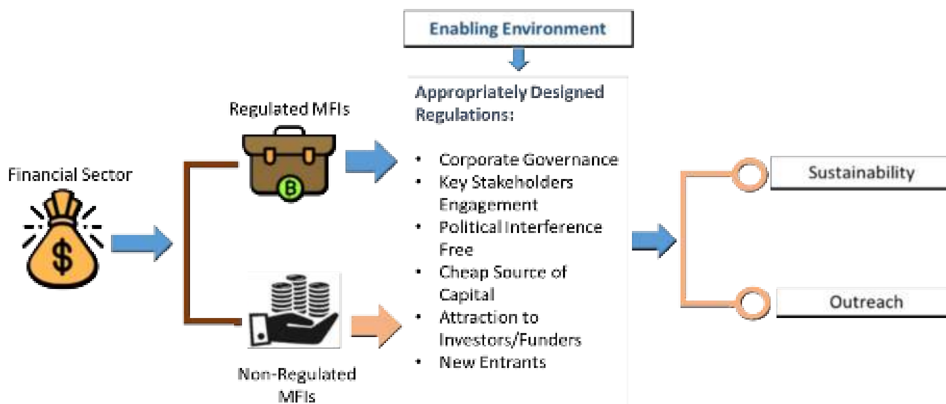
Various scholarships such as El-Chaarani et al. (2022) and Supriyatna et al. (2022) opine that corporate governance is among the key factors for effective performance of any MFIs. For Siele (2009), governance is all about institutions which comprise rules and regulations that systematically guide the way businesses should be conducted. Governance provides institutional framework that guides for responsibility and accountability of leadership and the management of MFIs More often, Corporate Governance is reflected on how the power of MFIs is exercised through a combination of total portfolio with the aim of maximising shareholder's value (Chenuos et al., 2014). Corporate Governance essentially is all about aligning different interests such as individual, corporation and society in order to achieve the organization's objective. This goes in tandem with the regulations regarding MFIs in Tanzania through which they (MFIs) are required to ensure financial sustainability. John and Senbet (1998) opine that MFIs that follow the principles of good governance will also be those that contribute significantly to poverty reduction.

Attendant to good corporate governance is the quest for stakeholder involvement in policy and decision making. We argue that involving stakeholder representatives formally acknowledges the importance of their relationship with the organization (Mitchell et al., 1997). Within the MFIs perspective, stakeholders may include clients (customers), employees, government, donors or technical assistance providers, creditors (debt holders), and investors (owners). The roles of stakeholder involvement hinges on the fact that they contribute important and necessary information if the information is well captured it leads to better MFIs policy. Various literature suggest that involving stakeholders in strategic decision-making results in a process characterized by rationality, political behaviour and intuition. Rationality, according to Chaserant (2003), occurs when decision makers (in this case stakeholders) gather information and act upon the information they have in making strategic decisions. Involving various stakeholders is likely to yield enough information with the assumption that they (stakeholders) are well informed and thus can generate optimal alternatives (Elbanna & Younies, 2008). On the other hand, political behaviour occurs because there are varying powers and conflict of interests. Stakeholders have and represent differing interests and people. This observation reflects Eisenhardt and Zbaracki's (1992) observation that political behaviour will arise so long as there are many individuals with different interests. Again, intuition assumes that most decisions are made based on different perspectives of decision makers at that particular time (Elbanna & Younies, 2008). We argue that while we acknowledge different expertise and experience of stakeholders, their intuition becomes a necessary contributor of decisions made. Therefore, with different interests among stakeholders, one may observe different episodes of political meddling in the operations of microfinance institutions.

Governments have tended to intervene in public policy making especially those related to MFIs with reasoning behind the interferences. However, we note that the causes of political interferences vary from country to country. Government intervention has been observed especially during policy formulation and its implementation to ensure that the establishment of MFIs is consistent to the interest of stakeholders and the government itself. While there is a need for good corporate governance, stakeholder involvement and government intervention through policy making, it suffice to note that, operations of MFIs need to consider the availability of capital. Sources of capital for MFIs has had profound

effects on their sustainability. Literature has provided different sources of capital and their implication on their sustainability. Some scholars such as Agier and Szafarz (2013) and Stiglitz and Weiss (1981) opine that there is a statistical significance between access to credit and microfinance's sustainability. As such, MFIs are subjected to conditions that usually inform the decision-making process in accessing credits. This could be determined by financial strength (Parvin et al., 2020). Traditionally, most MFIs get their capital from the government, NGO-donor agencies, and microfinance owner's equity. However, we could argue that, dependence on third party for capital investment is likely to affect the business operations. For example, experience indicates that credit lenders would want to collate an asset's ownership to measure the client's wealth and repayment ability (Henning et al., 2019) which may appear problematic to newly established MFIs. These collaterals may include assets such as land and houses to ensure credit repayment which are inadvertently expected to have a positive or correlation with access to credit in Tanzania MFIs. Other determinants for credit access for MFIs is the household characteristics (gender, marital status, literacy, family size, and food constraint); these are vital determinants of credit by microfinance credit (Sekyi, 2017), and which are used to measure creditworthiness, household responsibility, loan diversion, and education level (Santandreu et al., 2020; Hemtanon & Gan, 2020). Other factors for access to credit relate to asset ownership, regional characteristics, and geographical location (Li et al., 2011). The proximity of an individual household to a microfinance institute can also be a determinant factor. Other scholars (i.e., Agier & Szafarz, 2013) believe that proximity to lending organisation, attracting investors/ funders, institution affiliation, credit management experience savings habits, and credit history have an impact on accessing credit. Also, the type of microfinance institution and its operations significantly influence new entrant's access to credit. All of these factors influence the ability of the MFIs to access capital from lending institutions. Figure one b is indicative of the same.

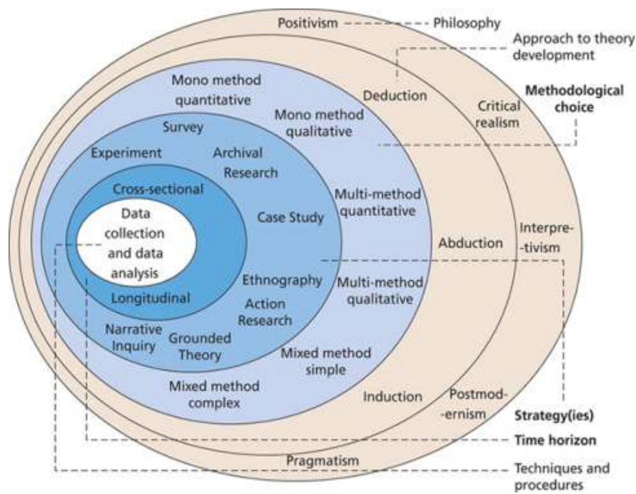
Figure 1: Conceptual framework



3.0 Methodology

Methodologically, the study was informed by the research onion by Saunders et al. (2020), which shows each step in the process of making the choices. Figure two is indicative of the same.

Figure 2: The Research Onion (Saunders et al., 2020)



Data for this study were collected based on fact that the environment for MFIs' sustainability and outreach performance was important. The study focused on problems, practices, solutions, and contributions to future practices (Saunders et al., 2020) given new regulations. Hence, we philosophically converged to pragmatism and theory development. Therefore, inductive approach was adopted whereby data were qualitatively collected via interviews. The in-depth interviews were designed to understand the impact of the real-life settings and implications for action. The sample comprised licensed and not yet fully licensed MFIs. Non-probability sampling approach was employed to get Chief Executive Officers, Directors, and Managers of licensed MFIs and those MFIs that had already applied for the license via Tanzania Central Bank (BoT). The response rate was 27 (87%) out of anticipated 30 respondents. Furthermore, 19 departmental officials from Tanzania Central Bank and Tanzania Association of Microfinance Institutions (TAMFI), and 25 MFIs top officials were interviewed. To analyse the data, themes were developed, and labels were derived from the data source by using the qualitative analysis software - QDA Miner 6.

3.0 Findings

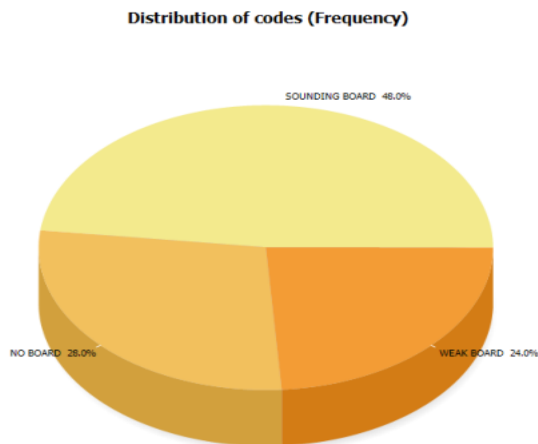
The findings of this study are organised into key themes, including corporate governance, participatory environment, and source of capital. Others include political influence, investors' response and new entrants. The subsections are used to explain in detail each theme in the analysis.

3.1 Corporate Governance

The first theme emanating from the establishment of new rules and regulations for MFIs is corporate governance. To ensure sustainability and outreach performance, MFIs were required to have in place company's management and board structure. While this was the major requirement for MFIs, the study found out that to have the right people as members of the Board was time consuming and was further frustrated by the central bank's delays

in approving members of the Board. It was also observed that there were no obstacles in adopting new corporate governance frameworks although most of the MFIs had weak board and management structure which required them to conditionally recruit board members with no tax liability. Therefore, they (MFIs) were required to submit tax clearance certificates from Tanzania Revenue Authority (TRA) for the proposed members of the board and management. This requirement by TRA inadvertently led to another problem of getting the right people to fill the positions as stipulated in the regulation. The question was much more on experience which again led to poor performance of some of MFIs jeopardizing their sustainability and raised uncertainty among shareholders. Furthermore, the study revealed that some MFIs had no board and proper management structures, which indicated inadequate good governance practices. While subscribing to new regulations on good governance, complaints related to reduced profits emerged because these new structures led to increased costs of operations. Generally, the regulations regarding corporate governance aspect came to reshape and transform most of the MFIs. Figure 3 shows the status of board and management structures of MFIs prior to the provisions of new regulatory framework.

Figure 3: MFIs' Corporate Governance Status



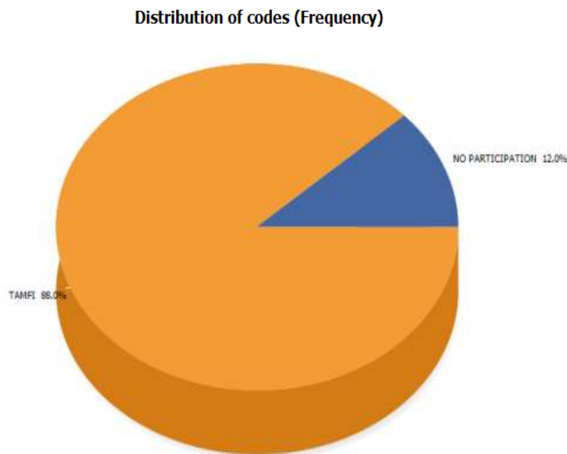
The results indicate that only 48per cent of MFIs had sound boards, and the rest (52%) had either weak or no boards at all. Generally, most of the respondents were of the opinion that they needed to adhere to new regulations while castigating the associated cost implications. More so, there was an insistence by TAMFI personnel on the necessity to comply with the corporate governance aspect due to its importance in achieving sustainability of MFIs while operating professionally.

3.2 Participatory Environment

The aim of this theme was to establish whether necessary stakeholders were involved in making new rules for MFI. Many participants reported to have been involved via their association known as Tanzania Association of Microfinance Institution (TAMFI). In the first part of the secondary code, we analysed only whether or not the participants were involved in the formulation of the regulatory provisions, in terms of percentage. The results indicated that 88per cent of the participants were involved via TAMFI, while 12per cent

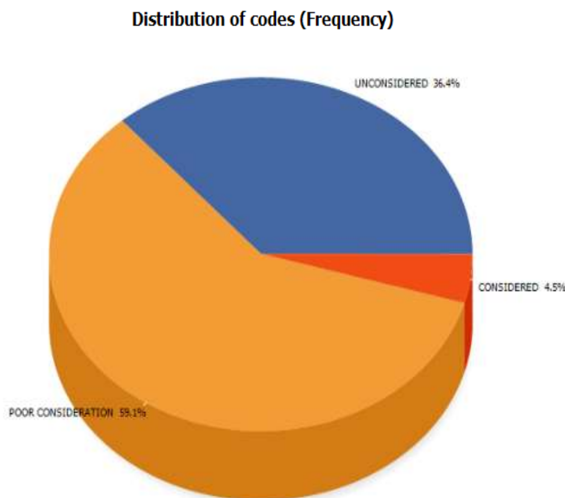
were not involved. Figure 4 presents the findings on participation of MFIs in regulations formulation.

Figure 4: Participation of MFIs in Regulations Formulation



Furthermore, as for the extent to which opinions and recommendations from MFI members were considered, the data indicate that 36.4per cent of participants through TAMFI, reported that their opinions and recommendations were not considered, 59.1per cent thought that their views were poorly considered, and 4.5per cent reported to have their views considered as depicted in the Figure 5.

Figure 5: Consideration of MFIs Opinions and Recommendations



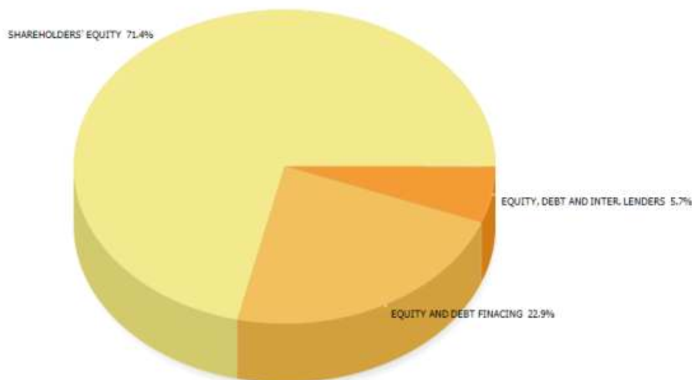
These results corroborate with the interview results from TAMFI personnel whereby only 20per cent thought that their opinions were considered. On the other hand, the results from personnel of the regulators reported to have invited closest stakeholders including TAMFI and a few big MFIs to review the draft and received their recommendations indicating that the level of stakeholders' involvement was quite enough (BoT Official), a large percentage (80%) of MFIs supported by TAMFI reported to have been poorly involved.

3.3 Source of Capital

An important theme emanating from the study was on sources of capital. More importantly was the extent to which the new regulations would facilitate acquisition of funding and funding investors. Managers and Directors were of the opinion that shareholders' equity was the only source of funds. As such, most of MFIs found it difficult to access loans from the banks due to lack of collateral. And interestingly, it was observed that commercial banks were reluctant to lend money to institutions which would be their competitors in the financial sector.

In as much as most MFIs relied on shareholders' equity financing, few MFIs were able to secure loans from other funders especially international lenders. Some MFIs sought funds from debt financing by borrowing from offshore banks at market rate interests. Therefore, commercial banks contribute about 45per cent of capital as debt financing, overdraft from local banks guaranteed by one of the shareholder and international lenders, and shareholders' equity (equity financing). More so, registering with Dar Es Salaam Stock Exchange, launching the Initial Public Offering (IPO) and selling of shares were other sources of finance. The study revealed that 71.4per cent of MFIs' sources of finances were from shareholders' equity, and 22.9per cent of them depended on equity and debt financing, and the rest, (5.7%) relied on all three funding options. Figure 6 depicts the source of capital structure of the MFIs.

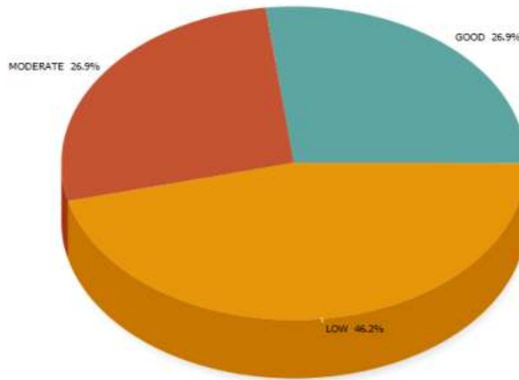
Figure 6: Capital Structures of the MFIs



In their quest for finances, MFIs sought help from two major players: The Central Bank and the Ministry of Finance. It was observed however that MFIs lacked awareness that the Central Bank was just a regulator. Hence, it was not responsible for searching and organizing the availability of funds for MFIs. On the other hand, while it is assumed that the Ministry of Finance needs to facilitate the availability of funds to Microfinance (Role of the Minister), Regulation (2019) does not state categorically or even make a provision that the Ministry of Finance is responsible for making funds available to MFIs.

Access to loans was also affected by the speed by which the regulator was able to release the license for operations. Regarding the regulator's speed of delivery, the majority of the respondents from MFIs indicated to have been dissatisfied with the regulator's speed. Figure 7 depicts the data on satisfaction on regulators' prompt service delivery.

Figure 7: Speed of Service Delivery from Regulator

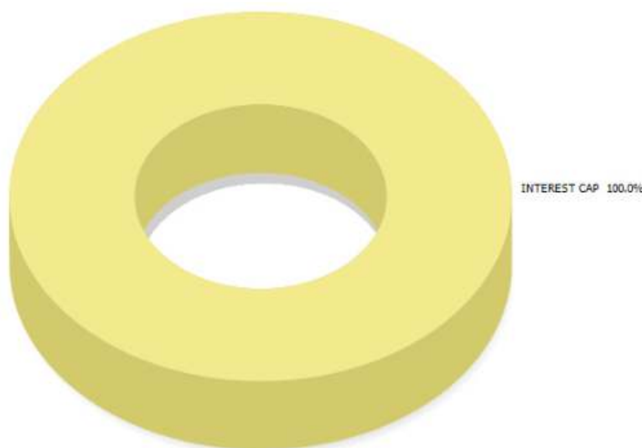


Inadequate in-service delivery by the regulator and their responses appeared to disappoint the MFIs as they had a lot of excuses. Respondents from the Department of Microfinance and Bureau de Change Supervision within the Bank of Tanzania reported to have limited resources (mostly human and finance) with a large number of MFIs amounting to 800 as per Business Registration and Licensing Agency (BRELA).

3.4 Political Influence

Another important theme emanating from this study was the issue of political influence. From the MFIs perspective, political interference by Parliament was so severe especially when enacting and implementing the regulations. Most importantly was the issue interest "cap" (BoT Official). It was noted that, before the new regulations, MFIs used to have free charge of interest. Therefore, with new regulations, MFIs were required to set the interest rate at 3.5per cent on the reduced balance per month in order to get the license for operations. For MFIs, this was thought to be impractical and difficult, which again resulted in some of them ceasing to operate. Figure 8 presents MFIs Major claim on political interference.

Figure 8: MFIs Major Claim of Political Interference



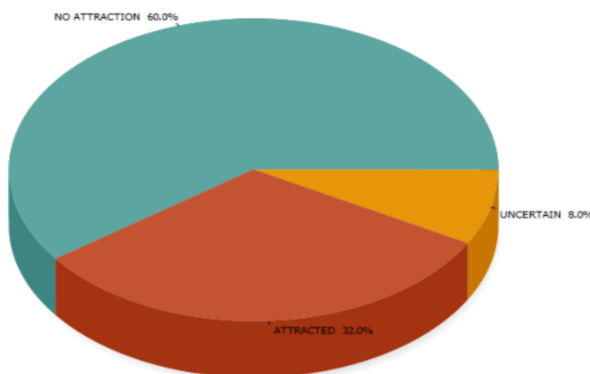
The results also indicate that, the fixed ceiling on interest rates led to some MFIs operating illegally. From the respondents, the 3.5per cent interest cap set by the regulations would not be taken favourably by all (100%) MFIs; thus, MFIs indicated negative reaction to this requirements. This 100% results corroborate well with qualitative responses above.

3.5 Investors' Response

Another important theme for the study was the reaction of investors on the process of investing in franchises being marred with perceived impediments. Investors were more sceptical on regulations of the Central Bank which they thought created uncertainties on what would happen in future. What they doubted was the capping of the interest rate at 3.5per cent which they thought was unsustainable business wise. Another concern for investors was inadequate public awareness regarding the financial sector in Tanzania. For them, most stakeholders were not aware of the ongoing exercise. Another confusion on the part of investors was the lack of harmonization within the financial industry. For example, they would argue that, it is impossible to have a requirement of TZS.20M/= as the minimum capital requirement to get a license and at the same time the banks need a regulator license to open a bank account. Their argument was clear, "how do the investor get the license before opening a bank account by the condition of having a license from the regulator."

Interestingly, while there are such impediments, some MFIs commended the introduction of these regulations in that they would bring more confidence to investors. They opined that, even customers would feel comfortable working with regulated MFI for security reasons. The respondents focused on investors' confidence in regulated MFIs and the credibility of the regulated MFIs and operating under the regulator's supervision. Figure 9 depicts the percentage responses regarding the extent to which investors are attracted to MFIs business given the new regulations.

Figure 9: Investors' Attraction to the Regulations



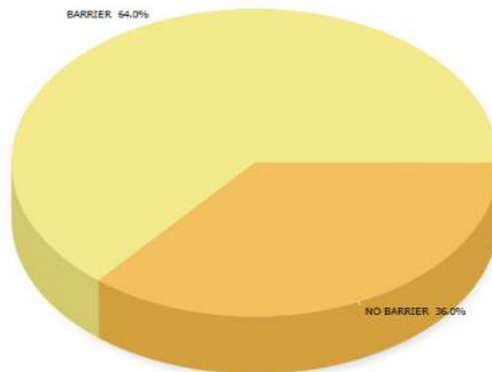
Generally, the data indicate that 60per cent felt that there was no attraction to the investors mainly due to the imposition of interest cap, lack of harmonization in the financial sector, and unstable policies, all coupled with lack of transparency.

3.6 New Entrants

The study findings revealed concerns regarding new entrants in the MFIs business in terms of their sustainability and outreach performance. According to the MFIs, the requirement of TZS. 20M/= as a minimum capital was considered as high. Similar observations were reported by other respondents that new entrants castigated the interest cap of 3.5per cent as very low for a business to operate profitably. New entrants argued that for those with high capital ranging from For TZS.500M/= to TZS.1B/= as investors who would make profits with such a small interest cap, otherwise those with small capital are likely to run into loses. As observed from earlier respondents, the new entrants in the business would want to operate the MFIs without adhering to what was described as stringent regulations. They had a feeling that the environment for investing in MFIs was not conducive.

Figure 10 indicates that 64per cent of the respondents thought there was a barrier to new entrants and the remaining 36per cent thought there were no barrier.

Figure 10: New Entrants Possibility



4.0 Discussion

Given the data in the previous section, we argue that it is imperative to have MFIs which are guided by prudent regulatory framework. We thus note that participation of different stakeholders in policy formulation is very important. Thus, a participatory environment among stakeholders during the formulation of regulations was meant to create conducive environment for the MFI's sustainability and outreach. It was meant to empower and serve the poor and those financially excluded citizens. However, it appear that participation of stakeholders in the MFIs policy formulation was inadequate. The regulator did not adequately engage the MFIs in policy formulation and did not consider valuable inputs from this crucial stakeholder during regulation formulation, which led to higher level of dissatisfaction among different players. Consequently, other players resorted to operating illegally and others leaving the sector altogether. In this regard, very few regulated MFIs were left to serve the mass, which again led to inadequate outreach performance. These discrepancies mirrors the observation by Quao (2019) who studied policy implementation deficiencies in Ghana's microfinance sector. One would argue that, participation in policy formulation is vital, the inclusion of the stakeholders' views is another aspect of consideration. Therefore, lack of user input during the formulation process hindered effective policy implementation.

The requirement of corporate governance, as necessary for establishing MFIs in the regulation was meant to improve good financial performance, sustainability, and outreach performance. This would mean having professional capacity, a sounding board with good management structure, and a sound accounting system, leading to financial discipline. Similar observations were made by Bakker, Schaveling and Nijhof (2014) in a study on the linkage between financial performance, sustainability and outreach performance of MFIs. Hence, as per the provisions of Tanzania regulatory framework for tier2 MFIs, corporate governance requirements were stipulated. These include a Board of Directors, management structure, and Internal and External Auditors (MFI tier2, 2019). However, adopting corporate governance standards seemed to be temporarily costly to most of the MFIs (only 48% had boards). MFIs incurred high costs during the implementation of the process in a bid to meet statutory requirement as most of them were operating clandestinely. The implication is that, formalization of the sector which earlier on operated without any legal framework led to increased overhead costs. This means that the requirement of adopting good corporate governance made it harder for most MFIs operating with weak corporate structures; although, this requirement is significantly essential for all MFIs.

On the issue of capital adequacy, it was noted that, most (71.4%) MFIs rely on shareholders' equity financing and international funders for the few remaining NGO-based MFIs. However, they (MFIs) face stiff challenges in accessing loans from commercial banks. The lack of collateral, demand for BoT, and the perception of the local banks treating the MFIs as their stiff competitor were cited as leading factors hindering access to loans through debt financing. The regulations did not provide any provisions for cheap loans nor did provide a better environment for the MFIs to access funds from other sources. Thus, many MFIs struggle to seek cheap funds and narrow their outreach capacity and uncertain sustainability. The implication therefore is, while the introduced regulations are meant to adhere to good corporate governance, issues of sources of funds and human resource for MFIs growth and sustainability were compromised.

Political interference was a major obstacle to many MFIs; and regarding new regulations through the interest cap 100 per cent of the respondents were dissatisfied with the interest rate ceiling of 3.5 per cent, which the regulator set because it made it harder for MFIs to operate profitably. Several MFIs decided to cease their operations in the anticipation of governments' review of the regulations and specifically on interest cap. Some MFIs contemplated on closure of businesses altogether, which led to unsustainable MFIs and thus inadequate outreach. These observations echoes findings by Dowla (2015) who studied political interference on microfinance noting issues such as quick commercialization that involved exploitative rather than profit maximization bringing about a political backfire leading to colossal harm to microfinance. Most of the MFIs in Africa are prone to interventions from the governments (CSFI, 2012 cited in Barry and Tacneng, 2015).

New investors' views on the new regulations seemed to be driven by the extent of political interference through the interest cap as a significant challenge. An interest rate (3.5%) is the backbone of any MFI, as a primary source of their income. Thus, unsatisfactory interest cap set by the regulator, which seemed lower than the real business environment, led to poor financial performance of MFIs. The implication is that, there is no investor or funder who would be interested in investing money where profits cannot be realised. More so, several MFIs would consider ceasing operations to avoid loses. However, there are some of

the MFIs operating under these rules although they claim to operate under loss impacting on their sustainability. We note that, from MFI's tier 2 perspective, their primary objectives is making profit-. Similar observations are made in a study by Labie (2001 citing Barry & Tacneng, 2014) who contend that any investor in any private MFIs is much more interested in profit-making for the growth of the organisation.

More importantly, given the regulations for MFIs, investors are likely to have confidence in running the business. However, there are still some reservations on issues of interest cap of 3.5 per cent, political interference, and unstable policies. Again, issues of inadequate harmonization of transactions as observed in the demand of license from MFIs during account opening on one hand and the requirement for the applicant to have a bank account with TZS. 20M/= as the minimum. This implies that, unpreparedness on the part of the regulator is a setback for new MFIs entry into business.

The new entrants in the MFI sector are very vital as they challenge traditional MFIs by enhancing services to consumers. It was observed that to a large extent there was a barrier for the new entrants mainly due to capital requirements and discouraging interest cap of 3.5 per cent. Limiting the new entrants will definitely impact the outreach performance although Rhyne and Otero (2006) argue that new entrants may wish to enter and identify a different niche market for all kinds of providers, even in competitive markets.

4.1 Conclusion and Policy Implication

The main conclusion drawn from this study is that the operations of the MFIs in Tanzania are still mired with bottlenecks emanating from inadequate design of the regulations which inadvertently have led to unsustainability and inadequate outreach performance. From the discussion we realise that inadequate stakeholder involvement, the adoption of good corporate governance, political interference, unreliable sources of funds especially to new entrants in business, seemed to be more challenging although the establishment of new regulations were meant to improve service delivery of MFIs. Based on the research findings, discussion and the conclusion, this paper recommends the following: first, further exploration of the MFI sector by the regulator is vital for understanding the natural environment in which the MFIs in Tanzania are operating. The approach will significantly deliver the necessary inputs during the formulation or amendment of the regulations. Secondly, intensive engagement of key stakeholders, explicitly MFIs' members, is critically important with careful consideration of their inputs. This will assist in formulating co-created regulations, including setting the interest cap that will be adopted by the majority MFIs and eventually achieving sustainability and leveraged outreach. Third, political influences or interferences should be avoided and focus on running the sector professionally. This has the propensity to attract new investors and even new entrants leading to the leverage value prepositions from players in the sector. Hence both MFIs and consumers are mutual beneficiaries of the business. Fourth, planning for the strategic provisions of cheap loans for the regulated MFIs will leverage the capital adequacy and be able to serve the poor and other financially excluded masses, hence becoming sustainable and enhancing outreach. Fifth, there should be better planning of process execution (regulating MFIs) by the regulator by strategically increasing the number of human resources, tools, and facilities. It is also important to adopt the emerging technologies which will fast-track license application and supervision of MFIs.

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