

THE NATIONAL MICROFINANCE POLICY OF TANZANIA

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1.0 Introduction

This paper tries to provide information on the content and context of the National Microfinance Policy in Tanzania. Because I was not given any more terms of reference other than the title, I will take the liberty to develop my own. But doing so, will involve a bit of speculation on what the audience would like to hear from the presenter. I will try to do three things in this presentation. First, I will look at the Tanzanian economic context. Second, I will look at the contents of the Microfinance Policy 2000 and third; I will provide some analysis, observations and conclusion.

2.0 The Economic Context of Tanzania

Tanzania is a poor agricultural country with a population of over 34 million people. Of these, almost over 75%, live in the rural areas depending on subsistence agriculture, producing their own food but vulnerable to famine in any incidence of drought. The country however, has a number of foods producing regions which are logistically disconnected from food-deficit regions. In the high crop producing areas, the colonial system introduced the traditional cash crop economy where coffee, cotton, tobacco, cashewnuts, sisal, pyrethrum and tea are grown to meet conditions and

standards of foreign demand. As a result, countries such as Tanzania, are facing the challenges of restructuring the dual economy where the largest proportion of domestic demand exist side by side with an externally determined cash crop sector. The result of this dycotomy, is stagnation of the domestic demand as the cash crop economy moves fast in fulfilling its international obligations. The subsistence sector is a marginal player in the totality of the domestic cash economy. Research has indicated that 16 million people in Tanzania and mostly in the rural areas, are living below the poverty line. They are low income and are not connected to any formal financial or commodity markets.

All food-producing areas are erratically connected to organised markets. They are therefore prone to underpricing while the middlemen in the cities, make more money out of their products. Those in the traditional cash crop areas produce values which are exported as raw materials and multinational companies make more money out of such crops, than the local producers. The whole cry about falling coffee, and prices is a phenomenon for primary producers of coffee not the processors and coffee distributing chains under multinational companies. The finality of the dual economy is three important features: First, the domestic market remains small relative to the value of exports when they are in the hands of multinational companies. Second, the economy is gradually being turned into an importer of industrial consumer goods, capital goods, agricultural commodities and skilled labour.

The closure of national industries due to liberalisation, resulted into active labour being turned into redundancy. As new industrial technology becomes more automated and standardised, it will demand less skilled labour and the more skilled labour becomes gradually redundant. With the rise of international supermarkets, there is a gradual expansion of agricultural imports, making agricultural labour redundant.

Third, as Tanzania continuously becomes a comprehensive importing country, it will continue to slow down the growth and expansion of its domestic market. This means, any intervention into financial intermediation and financial services development, must look at the restructuring of the dual economy and linking domestic production with domestic demand. This is the challenge of all forms of economic policy including the microfinance policy.

3.0 The National Microfinance Policy

3.1 Background to the Policy

The national microfinance policy is an instrument of economic reforms in the financial sector which started in 1991. With a strong background of 30 years of state-controlled banking, the reforms in the financial sector were addressing two important aspects of financial services delivery: First, they were meant to allow banking institutions to operate commercially but secondly, the banks were now required to carry out market-driven business decisions outside government control.

In the operationalisation of a liberalised financial sector, government commitment in the microfinance policy was directed to remove all features of a state-owned banking sector including:

- Liberalisation of interest rates.
- Elimination of administrative credit allocation.
- Strengthening of the BOT role in regulation and supervision.
- Restructuring of state-owned financial institutions.
- Free entry of private banks.

The Banking and Financial Institutions Act of 1991, took on board all these reforms. But, while the reforms took a partial analysis of the total financial system (the commercial banking sector), the only microfinance institution that was in operation, was the Savings and Credit Co-operative Movement which was covered by the 1991 Cooperative Act.

It must be pointed out here that although the 1991 Co-operative Act recognised SACCOs as equity based financial institutions with the freedom of association by members, they were not reformed.

Therefore, since 1991, there was more restructuring processes of the old commercial banks and entry of private banks such as community banks, cooperative banks and foreign owned commercial banks some buying out the restructured state banks while others coming to invest such as STANBIC, Standard Chattered and Kenya Commercial Bank. All these meant that the banking sector had entered the era competition.

4.0 The Emergence of Microfinance Policy

While the banking sector was being restructured with the evolution of a competitive framework, policy makers noted that a very important sub-sector in the financial system, had been left and yet it was critical. The microfinance sub-sector, including the unreformed SACCOs, had not been touched but had the following features.

- i) Interest rates went below market rates and could not cover their operational costs.
- ii) A group of financial NGOs continued to depend on foreign funding instead of building from internal resources.
- iii) There were no procedures for tracking down and analysing microfinance operations.
- iv) Financial NGOs operated under different laws making it difficult to develop common standards for monitoring, supervision and regulation.
- v) SACCOs were facing poor administration and lack of supervision.

But at the same time, the Tanzanian financial system was facing two challenges: first, the poorly organised microfinance subsector, while on the other hand, the restructuring of commercial banks ended into closure of bank branches in the rural areas without substitute financial services. The essence of microfinance policy, is underscored by the very need for such institutions in a poor country like Tanzania.

It is now recognised that in order for development to be more comprehensive, the largest proportion of the poor, must be integrated into an organised financial services system. Microfinance institutions have the following development services:

4.1 Financial Services

The poor needed financial services to give them protection, resource allocation efficiency and investment. They also need financial services so that they can synchronise deficit and surplus periods and therefore making rational use of their resources. Availability of financial services, creates opportunities for enterprise development and economic development in general.

The poor also need savings services. Savings as mother of credit are a source of self-reliance, freedom and sustainable development. They are important during emergence periods; they absorb shocks during food shortages and useful for school fees. They provide time for capital accumulation and savings in financial forms provide funds for investment by others.

4.2 Credit Services

When savings are available, credit for investment is practical. Enterprises grow and expand when they can access credit for working capital and long-term capital investment.

4.3 Payment Services

Payment services are part and parcel and central functions of banks and microfinance systems. Profitability as well as efficiency of the financial system, very much depends on the nature of the payment system.

5.0 The Policy

5.1 Objectives and Scope of Microfinance Policy

The National Microfinance Policy defines microfinance as a process of addressing the financial needs of the largest proportion of the population, found in the low-income households.

The objectives of the policy are as follows:

i) Overall objective

To establish a basis for the evolution of an efficient and effective microfinancial system in the country that serves the low-income segment of the Tanzanian society and thereby contribute to economic growth and poverty reduction.

ii) Specific objectives

The specific objectives of the microfinance policy are:

i) To establish a framework within which, microfinance operations will develop.

ii) Laying out the principles that will guide the operations of the microfinance system.

iii) To serve as a guide for co-ordinated intervention by respective participants in the system.

iv) Describing the roles of the implementing agencies and the tools applied to facilitate microfinance development.

The microfinance subsector covers the provision of financial services to households, small and micro-enterprises in both rural and urban areas. The services themselves include savings, credit, payments and any other financial innovations that may be developed by the microfinance institutions. The target of microfinance is on all types of legal economic activity such as commerce, trade, manufacturing and agriculture. The groups to be served by microfinance institutions are those households usually excluded from mainstream financial institutions.

5.2 Policy Principles for Microfinance

Vision

The microfinance policy aims at attaining a more comprehensive and inclusivistic vision of microfinance. It wants to achieve widespread microfinance throughout the country by institutions operating on commercial principles.

The vision also touches all possible providers of microfinance services such as banks, community banks, non-bank financial institutions, cooperative banks, financial NGOs and SACCOs.

It is flexible in the sense that it allows all levels of specialisation from credit only to savings only as well as those which can perform both savings and credit operations together.

The vision of the policy puts the microfinance organisation on a possible integration with main commercial banks with the flexibility that their features are not compromised.

It spells out Competition. Microfinance institutions are allowed to compete in the market so that customers get quality products and services and more efficiently and effectively.

Finally, the vision of microfinance policy emphasises the creation and support of a self-reliant financial system that is self-driven and sustainable, without external support from government or donors.

5.3 Best Practices

Modern microfinance institutions are required to provide services effectively, efficiently and sustainably.

There are two basic principles for the promotion of microfinance best practices: First, is the question of innovative design where there is the combination of commercial and financial principles with ways and methods of delivery under circumstances of low-income households.

Secondly, is the application of world recognised best practices which include self-determined pricing, information based and appropriate provisioning in the control of delinquency, financial reporting on operations, outreach and profitability. Emphasis is also on, internal rate of financial substitution and internal control systems. Other best practices include the development of appropriate products and services for the poor and the use of unconventional collaterals and incentives. Gender equality is emphasised so that financial services are available and accessible to both men and women and finally good governance in terms of putting up the appropriate structures of governance, client or member participation and minimal government interference.

5.4 Tools for Policy Implementation

The policy specifies three major tools of implementation

a) Regulation and supervision

The system of regulation and supervision will be managed by the Bank of Tanzania and will be standard for all actors in the financial system. It is aimed at protecting depositors as well as the financial system as a whole.

The features of the regulation and supervision framework Will be as follows:

- Only microfinance institutions accepting deposits Will be subjected to regulation and supervision.
- Supervision will be applied to microfinance organisations above a certain size of deposits.
- Supervision will also cover unconventional security on loans and hence a design of unconventional instruments of regulation.
- Minimum capital requirements will differ from those of traditional financial institutions.

b) Development and application of standards

Standards are important for monitoring and evaluation because they allow inter-institutional comparison and provide profiles which give status of performance, efficiency and effectiveness. Also, practitioners using same standards, can develop self regulatory mechanisms in order to improve their operations. With the above advantages, the policy specifies three broad categories of standards outreach to clients, institutional development and financial performance.

c) Capacity building

The policy recognises the fact that microfinance institutions in Tanzania are new and smalls They therefore need capacity building in crosscutting skills of management such as accounting, auditing and computer information systems. They will also be connected to professional service providers where efforts will also be centred on standards.

5.5 Roles and Responsibilities

The microfinance policy has assigned specific responsibilities by different players in the implementation process for the creation of a supportive and effective and efficient supervision and regulatory environment for microfinance institutions. The main players

in the microfinance industry include the central government, the Ministry of Finance, Bank of Tanzania, other government entities, MFI providers and SACCOs.

5.5.1 The government

The central government has responsibilities of keeping inflation low, overseeing free interest rates, developing rural infrastructure and building a healthy credit culture. Other government responsibilities include the provision of high-quality bank supervision and developing a supportive legal framework.

The Ministry of Finance has overall responsibility for the financial systems development. It will also oversee official donor assistance going to microfinance institutions including the coordination of programmes planned jointly with other Ministries for the development of microfinance institutions.

5.5.2 The Bank of Tanzania

This is the government entity overseeing the financial sector with an overall responsibility to implement this policy. In carrying out its responsibility, it ensures that a regulatory and supervisory framework that support microfinance operations is developed.

It will also co-ordinate the implementation of the microfinance policy by collecting and disseminating relevant information, monitor progress, examine key technical issues, relevant to microfinance providers and advise the government on appropriate structures. The BOT will also advise the microfinance institutions on technical aspects of government programmes in microfinance.

5.5.3 Other government entities

Entities supporting the promotion and development of microfinance institutions are expected to follow best practices. In doing so, they will have to consult the BOT.

5.5.4 MFI providers

Microfinance institutions have been given the freedom to develop microfinance services based on their objectives.

- The objectives could be profitability, self-help promotion or poverty reduction.

- They are supposed to learn and make the best choices of services which link with their objectives.
- They are expected to learn about best practices and apply sound financial principles.

5.5.5 Banks and Non-Bank Financial Institutions

Banks as deposit institutions, will be encouraged to enter into microfinance markets through government incentives.

5.5.6 Saving and Credit Cooperatives

These operate under the Co-operative Societies Act but as savings and credit institutions they offer financial services to the members. As financial intermediaries, they are going to be supervised by the Bank of Tanzania.

The policy however, puts in place the following guidelines for the promotion of efficient and sustainable SACCOs:

- After membership reaches more than a small group, they will be subject to regulation and supervision.
- As savings-based institutions, loan portfolio should not undermine incentives to promote savings.
- Pricing policies in SACCOs should promote saving and allow sufficient interest rate spread for the profitable operation of the SACCOs.
- Promotion of the SACCOs should be separated from supervision to allow for the application of standards. Currently promotion and supervision are still under the Ministry of Cooperatives and Marketing.

6.0 Observations

The microfinance policy of Tanzania has both strengths and challenges.

We can highlight seven areas of strength for the microfinance policy: First, it is entering into an area where most of the population is found. Most developing countries' population are poor and yet there are no deliberate policies to link the poor and the realities of financial

services. Tanzania is largely a smallholder-small-enterprise country. As such, it is automatically a microfinance country. But microfinance must be organised in order to meet the requirements and challenges of poverty alleviation. This policy is introducing the basic conditions for organised microfinance against poverty.

Second, the microfinance policy is inclusivistic. All types of microfinance institutions with diverse objectives are all included and accepted by this policy. Banks and no-banking institutions, cooperative banks, SACCOs, community banks are all included and given opportunities to emerge and grow.

Third, is flexibility in the regulation and supervision principles. The vision of this policy is wide, showing government commitment in achieving widespread access to microfinance by all poor people in Tanzania. The policy also accommodates a high degree of generality and specialistic microfinance institutions ensuring the construction of a competitive framework and the institutionalisation of financial self-reliance through the development of a more encompassing microfinance industry in Tanzania.

Fourth, is the emphasis on the institutionalisation of business oriented best practices, away from the traditional social service microfinance culture. The policy puts emphasis clear on market-driven pricing of products and services, delinquency control, financial information and reporting as well as gender equality and good governance.

Fifth, the policy gives important guidelines on the tools to be applied on its implementation, monitoring and evaluation as well as specific roles of different players in the microfinance subsector. Important in the roles played by stakeholders, is the special commitment by the government to improve rural infrastructure in order to expand geographical accessibility to financial services by the remote poor and the development of a supportive legal framework for the development of microfinance institutions in Tanzania.

Sixth, is the special attention given to SACCOs as a special microfinance institution that has a structure which generates opportunities for the creation of a strong domestic-driven microfinance industry in Tanzania. The guidelines given for the development of sustainable SACCOs in Tanzania are introducing best practices and commercialisation processes in the traditionally managed social service oriented SACCOs.

Seventh, is the ambition by the policy to create opportunities for linking microfinance institutions with mainstream commercial banking institutions in Tanzania. Although this is a challenging area, experiments on the ground, show high degrees of success. The CRDB bank in Tanzania has tried to link with all types of SACCOs and new lessons have been articulated. One of those lessons, is the wholesale-retail credit and a high level of repayment both at the retail and wholesale levels.

7.0 Challenges

There are a number of challenges that are faced by the microfinance policy and its framework. They include the fact that the context is not wide enough on the macro-economic structures, but more fixed on the Bank of Tanzania supervisory and regulatory agenda. The Policy is a more formalistic document that tries to reflect on the 1991 Banking and Financial Institutions Act. It is more of a reformist instrument of a historically forgotten sub-sector. As a result, the policy is more of an instrument of monetary policy of the Bank of Tanzania rather than a government instrument to restructure a colonially distorted economy.

Secondly the policy does not provide the scenario for the problem being addressed. The economic structure and the slow growth of the domestic market, should have been analysed. Microfinance institutions are derived institutions. They do not exist for themselves and by themselves. They exist and grow where there are vibrant supply and demand systems for goods and services. The analysis of markets, enterprise development and constraints should have introduced the microfinance policy.

Third, the policy is silent on the status of informal financial markets in the country. The challenge of the organised financial market proposed by the microfinance policy, is how microfinance institutions can become instruments to reduce the size of the informal and exploitative rural and urban financial markets where the poor have more access.

Forth, is the question of reforms for SACCOs. The policy is taking for granted about the status of SACCOs in Tanzania. While the commercial banking sector has been reformed and restructured, the SACCOs movement has not of today.

But SACCOs are people owned institutions and operate under the Cooperative Societies Act.

One may argue that the right location for the reforms in co-operatives and SACCOs in particular, is the Ministry of Cooperatives and Marketing. Currently, the Ministry is working

on the cooperative reform programme, which will take on board, the SACCOs too. However, collaboration between the Ministry of Cooperatives and Marketing, the Ministry of Finance and the Bank of Tanzania, will be called for when it comes to SACCOs reforms.

8 0 Conclusion

The Tanzania National Microfinance Policy is an important instrument for the development of microfinance institutions, especially SACCOs. It provides the right guidelines for the development, professionalisation and the commercialisation of SACCOs in Tanzania. It introduces best practices and standards of a world class microfinance system. Although some of the regulatory and supervisory structures for microfinance institutions are not yet in place, the policy provides useful guidelines for any active player in the microfinance industry.

SACCOs take a special position in the policy because they have a genuine structure for developing a self-reliant economy that creates the conditions for an expanded domestic market. However, if we want the SACCOs movement to play its historical role, the cooperatives reforms initiated by the Ministry of Cooperatives and Marketing are historically necessary.

