**KWAME NKRUMAH UNIVERSITY OF SCIENCE AND TECHNOLOGY,**

**KUMASI**



# CHALLENGES OF MAKING MICROFINANCE MORE ACCESSIBLE IN THE INFORMAL SECTOR

**(PG3094509)**

**INSTITUTE OF DISTANCE LEARNING**

A Thesis Submitted in the Institute of Distance Learning of the Kwame Nkrumah University of Science and Technology in partial fulfillment of the requirements for the award of a degree of Commonwealth Executive Masters of Public Administration (CEMPA**)**

**JUNE 2011**

## DECLARATION

I Hannah Tenkorang, author of this thesis, do hereby declare that the work presented here was done by me as a student of the Institute of Distance Learning, Kwame Nkrumah University of Science and Technology, 2010/2011 acadamic year under the supervision of Mr. Samuel Kwesi Enninful. All references to other literature have been duly acknowledged. This work has never been submitted in whole or part for any degree of this University or elsewhere.



Hannah Tenkorang (PG3094509)

| | | |
|---|---|---|
| ……………………… | ……………………… | …………………… |
| Student Name & ID | Signature | Date |

Certified by:

S.K. Enninful

| | | |
|---|---|---|
| ……………………. | ……………………… | ………………….. |
| Supervisor (s) Name | Signature | Date |

Certified by:

| | | |
|---|---|---|
| ……………………. | ……………………… | ………………….. |
| Head of Dept. Name | Signature | Date |

## DEDICATION

I dedicate this work to first and foremost, our Almighty God, secondly to my lovely father Mr. Alex Kwabena Tenkorang, I pray that the good Lord will shower his blessings on you to make you first among equals.

It is also dedicated to my siblings Prince Tenkorang, Agnes Tenkorang and David Bartels for their love, support and concern, I say God bless you all.

## ABSTRACT

The overall goal of this research is to study the challenges confronting the informal sector accessing microcredit facilities from the microfinance institution. The study used a survey research strategy to survey informal sectors operators in the Greater Accra region. An extensive literature review was conducted to provide a thorough understanding of the recent developments and the underlying philosophy of Microfinance vis-à-vis the evolution and practice of Microcredit in Ghana. The data was analyzed using simple random, and the SPSS. As demonstrated by the findings, the key barriers in accessing microfinance was centered on lack of specific policy guidelines and goals from the microfinance institutions towards the informal sector(1st), lack of credits funds and growing demands from microfinance institutions (2nd), unfavorable collateral security demands from the microfinance institutions (3rd), lack of eligibility criteria (4th), low loan size and unfavorable repayment terms (5th) cost of access to credit source due to time and money. The study found that majority of the respondents are satisfied with the nature of the microcredit scheme provided by their respective microfinance institutions. It is recommended that a deliberate attempt should be made to incorporate the informal sector into the main stream economy by appropriately studying the sector at the national and regional levels to develop a reasonable database on which sector specific policies could be design and implemented. Further, public and private financial institutions should be encourage to grant the sector access to loanable funds on flexible terms to reflect their distinct characteristics. Future research to explore the dynamics of possible Microfinance regulations that would formalize Microcredit operations in Ghana would be important.

## ACKNOWLEDGEMENTS

I am grateful to God Almighty for giving me good health and strength to embark on this academic exercise successfully. I am also thankful to my supervisor Mr. Samuel Kwasi Enninful whose directions, critique and mentorship has helped me tremendously to enable me produce this thesis. Your quick responses to my submissions are worthy of notice and appreciation.

I would also like to thank the academic staff of the Institute of Distance Learning (IDL) at the Kwame Nkrumah University of Science and Technology for their outstanding contribution to my academic up-bringing by providing conducive teaching and learning environment. It is important to mention Mr. Alex Kwabena Tenkorang and Mrs Florence Baah-Yeboah. I am so grateful for your advice and commitment. I am also grateful to Agnes Tenkorang and Prince Tenkorang for their support and prayers.

To Mr. Daniel Mensah-Bonsu and Ms. Rebecca Aggrey who graciously assisted me in the data collection and typing, I say God bless you. I would not have made it without you. I also thank Mr.  To Daniel Adu-Gyamfi who timelessly assisted me in the use of SPSS package for the analysis. I also wish to thank Pastor Michael and Pastor Ben for their prayer support and encouragement during this period of academic exercise. To Mrs Kate Larbi, I say thank you for your continual commitment in my academic progression. To the wonderful people I came into contact with in and outside campus, I wish to express my sincere thanks and gratitude.

Finally, and most importantly, I am most grateful for the continuous love and support that my family has always given me, during my studies. To my cousin Kwadwo Larbi and my lovely uncle Mike Anim Danquah, I say thank you. I am delighted to be a student of IDL-KNUST, where student experience was very interesting and refreshing.

TABLE OF CONTENTS

More Accessible in the informal sector

## LIST OF TABLES

## LIST OF FIGURES

# CHAPTER ONE

## INTRODUCTION

### 1.1 BACKGROUND TO THE STUDY

Morduch (2000) reported that about one billion people globally live in households with per capita income of less than one dollar per day. Increasing poverty has been known to worsen the poverty problem in the world today particularly in Sub Saharan Africa. In both developed and less developed countries human livelihood is characterized by a sharp contrast of increasing disparity between the rich and the poor as well as the formal and informal sector. Poverty alleviation is thus becoming one of the most important challenges faced by policy makers of many less developed countries. The provision of financial services to low income households according to Morduch (2000) is believed to eradicate, (or at least reduce), poverty through the transformation of social and economic infrastructures.

Developing countries, including Ghana, seem to be characterized by a dual financial system with an informal and a formal financial sector where the lower-income clientele tends to be left out of the latter. The lack of access to the formal financial sector is a result of the lack of the collateral required due to risks involved in lending but also due to high costs involved in small-scale financial services and weak legal enforcement (Ray, 1998). The proliferation of microfinance programs, particularly microcredit, targeted to women and the marginalized in society is increasing from time to time. There has also been a drastic shift in the focus of credit allocation by microcredit institutions to those in the informal sector rather than those in the formal sector due to the fact that the informal sector employs a large number of people who also contribute significantly to the development of the country.

Microcredit has been changing the lives of people and revitalizing communities worldwide since the beginning of time. Microcredit can be offered, often without collateral, to an individual or through group lending. Micro entrepreneurs are people who own small-scale businesses that are known as microenterprises. These are the enterprises to which microcredit schemes are implemented. Microfinance has been used by NGOs, the UN and other agencies intensively in the development debate the last few decades. It is the framework within which microcredit scheme operates. According to BancoSol (2006 p. 7) microfinance builds on those financial services that are needed to make investments in both physical and human capital, in order to smooth consumption and overcome unexpected shocks. Microfinance can be seen as a solution to include on a large-scale, previously excluded poorer groups without access to capital into the financial system so that they may "rise out of poverty" by themselves.

The World Bank is engaged in reducing poverty through promoting best practice in the microfinance industry and funding selected institutions to bring financial services to the poor. The provision of microcredit has been recognized as instrumental tool for eradicating and/or reducing poverty by many developing countries, including Ghana. According to the former_United Nations Secretary General Kofi Annan at the Global Microcredit Summit 2006, "Microcredit is a critical anti-poverty tool and a wise investment in human capital. Now that the nations of the world have committed themselves to reduce the number of people living on less than $1 a day by half of the year 2015, we must look even more seriously at the pivotal role that sustainable microfinance can play and is playing in reaching this Millennium Development Goal."

From various studies, Park and Ren (2001) summarize that microcredit programs have increased incomes and had other positive effects such as gender empowerment, improved nutrition, higher educational attainment, and reduced consumption variability. However, there is partial evidence and is contested that microfinance would make a larger contribution to reduce poverty or promote small and micro enterprise development in most developing countries as compared to investments in social and economic infrastructures (Hulme, 2000). Micro-enterprises may be small, but their cumulative impact is huge: depending on the country, micro-enterprises employ an estimated 30-80 percent of the working population (Charmes, 1992).

Studies by several scholars including Mulat (1999) indicate the following reasons, among others, as causes for the reluctance of banks to serve the rural poor and other micro entrepreneurs.

- Physical remoteness of borrowers.
- Lack of collateral.
- Repayment for working capital can be required only once at the harvest season.
- High cost of intermediation in geographically dispersed beneficiaries.
- Small size of the transaction.
- Mobility of many informal sector enterprises.
- General lack of information about the borrowers.
- Poor transportation.
- Lack of confidence on the repayment of the loan by borrowers.
- Lack of information.

As a result of these reasons, bank's financial services are inaccessible to the poor. Thus delivering financial services to the poor requires an innovative targeting design and a credit delivery mechanism that helps identify and attract only the poor who can initiate and sustain productive use of loans (Wolday, 2002). He further noted that the delivery of financial services has thus been viewed as an anti-poverty tool because it helps the unemployed become employed, thereby increasing their income and consumption and reducing poverty.

## 1.2 STATEMENT OF PROBLEM

In recent times, microfinance and micro credits are concepts that are frequently used in discussion on poverty reducing actions and micro enterprises. Micro credits are believed to help people lift themselves out of poverty. There have been several studies discussing whether the microfinance institutions have an impact on poverty or not. Some studies have indicated that microfinance help families and micro enterprises to higher consumption and smoothing, but a microfinance programme that lack sustainability and cost-effectiveness hinders long-term effects on income expansion and poverty.

Several microfinance companies exist within the country with the focus of providing micro credits to the informal sectors which happens to be the largest employers in the Ghanaian economy. Despite their numbers, majority of entrepreneurs in the informal sector have difficulties assessing credit from such institutions as a result of reasons such as mobility of some informal sectors, lack of collateral and the general lack of information on the borrower, among others. Why is this so? Can there be a way out? This study therefore seeks to investigate the challenges confronting the informal sector in assessing credits facilities and how these challenges could be addressed.

## 1.3 RESEARCH OBJECTIVES

The main research objective of the study is to investigate the challenges of the informal sectors of the economy in assessing credit facilities. But specifically, the following objectives were be used.

1. To find out microcredit institutions requirement before granting credit facilities to informal sector operators.
2. To ascertain the challenges that confronts the operators of the informal sector in accessing micro credits for their micro enterprises.

## 1.4 RESEARCH QUESTIONS

1. What requirement do microcredit institutions prefer before granting credit facilities to informal sector operators?
2. What are the main challenges confronting the informal sector operators in accessing micro-credit?

## 1.5 JUSTIFICATION OF THE STUDY

Micro finance continues to assume increasing importance as a result of several factors. The emphasis on micro credit in this century is such that the global conscience believes that if unemployment is reduced, the world would be a better place as there will be a reduction in poverty, an improved living condition, increased productivity, and an overall resultant effect of an enhanced economic performance. Khandker (1998) observes that the lack of savings and capital makes it difficult for many poor people to become self-employed and to undertake productive employment generating activities. Also, lack of capital makes it difficult for the disadvantaged to become self-employed.

The study will relate to such ideas on making credit facilities accessible to the informal sector and the challenges that they face. Thus, this study will help in facilitation and loan repayments as well as the challenges confronting the microfinance institutions. From a practical perspective, the findings of this study will be useful to financial institutions to design their credit strategies within a strategic condition at the informal sector in order to improve access to credit facilities by this sector whiles contribution to the institutions performance. Also, this research is expected to become, in an important part, a meaningful guideline for micro finance institutions in formulating policies and practices that will go a long way to enhance the performance of their target groups as well as achieve their overall business goals.



## 1.6 LIMITATIONS, SCOPE OF RESEARCH

The study focused on the problem statements discussed in the earlier part of the study. In this regard, the possibility of bias or any other possibility of veering away from the topic was averted. In the same regard, the study also has an inherent limitation such that it only covered a limited number of qualitative data on the informal sector operators in the Greater Accra Region of Ghana. Thus, generalization of the findings has a limited effect. Nevertheless, the findings will be surely effective with the respondent operators of the informal sector in the Greater Accra Region.



## 1.7 METHODOLOGY

Primary data was collected from respondents through the questionnaires which was the main research instrument. The primary data was gathered from a section of the operators of the informal sector in the Greater Accra Region. The study selected 60 operators of the informal sector from various disciplines who were access microcredit facilities from microfinance institutions. Stratified sampling procedure helped in selecting the various segments in the informal sector.

The questionnaires were distributed by the researcher and was be made at a time all the respondents were less busy. The interview was conducted using the questionnaires that the interviewer administered. The data was generated from the study and analyzed quantitatively.

## 1.8 ORGANISATION OF THE STUDY

The whole study is divided into five chapters. Chapter one is on the introduction to the topic where the background, statement of the problem, the research questions and objectives of the study, as well as the limitations and significance of the study. Chapter two provided an overview of the theoretical foundation that provides the premise for the study in the form of literature review. The concepts and definitions of micro credit and finance, its role and impact on development as well as its access are discussed. Chapter three presented insight into the methodology used in the whole research. Chapter four discussed the findings and the analyses data collected during the study. Chapters five provided a summary, draw conclusions as well as make relevant recommendations to overcome the potential challenges in the sector.

# CHAPTER TWO

## LITERATURE REVIEW

### 2.1 INTRODUCTION

This chapter endeavour to review relevant literatures in line with the objectives of the study. In this regard, the concepts and definitions of key terms relevant to this study are presented. Also, the concept of micro credit, the role of micro credit to development as well as the significance of micro credit is reviewed.

### 2.2 THE INFORMAL SECTOR

The concept of "informal sector" since its invention in the 1970s has attracted much interest, discussion and disagreement. Since the International Labour Office (ILO) employment mission to Kenya introduced the concept into the international spectrum in 1972, a number of definitions have been introduced into the literature. One generally accepted definition of the informal sector has been that which is characterized by small-scale units engaged in the production and distribution of goods and services, whose primary objective is to generate employment for the participants rather than to maximize profits (Lubell, 1991). The ILO defines informal sector as: "A way of doing things characterized by:

a) Ease of entry;

b) Reliance on indigenous resources;

c) Family ownership of resources;

d) Small-scale of operation;

e) labour-intensive and adapted technology;

f) Skills acquired outside the formal school system; and

g) Unregulated and competitive markets" (Lubell, 1991, p.21).

There are currently two approaches to defining informal sector activities: the definitional and behavioural (Farrel, Roman and Fleming, 2000). Farrel et al. defines the informal sector as one which consists of economic activities which are not recorded in the gross domestic product (GDP) and or the national income accounts. This definition is rather doubtful because though their activities may not be record in the national income accounts, their contribution to various tax regimes in any country contributes significantly to the national income level of any country. The behavioural definition which is at times referred to as the legalistic definition is based on whether or not an activity complies with the established judicial, regulatory, and institutional framework (Feige, 1990). However, Sethuraman (1981) defines the informal sector as consisting of small scale units engaged in production and distribution of goods and services with the primary objective of generating employment and income, notwithstanding the constraints on capital, both physical and human, and the technical-knowhow.

Arimah (2001) opines that the informal sector does not appear to have a meaning independent of the formal sector, as it only derives its meaning when contrasted with the formal sector. Ademu (2006) also defines the informal sector as comprising those employment generating activities of some urban residents, undertaken for survival in the absence of formal employment. But informal sector operators are not only found in the urban areas. In fact, almost all businesses in the rural areas are characterised by well known characteristics of informal sectors and hence constitute informal sectors. The activities of the informal sector are characterized by the lack of regulations by institutions of society in a social and legal environment in which similar activities are regulated. Common characteristics of operators in the informal sector thus include:

- Easier access to production factors which are derivable from social organisation of family and friends.
- Involves entrepreneurs in virtually all branches of the economy ranging from productive activities general services and specialized services.
- Technology is determined more by the constraints of the social relations.
- Motivation for production by the operators in the informal sector is becoming more profit oriented (Ademu, 2006).

It must be said also that informal sector operators mostly operates using indigenous knowledge with little or no formal training or professional development in the specific areas of their operations. In Ghana, informal sector operators are said to constitute about 80% of the population. Whiles it is well understood that people in the informal sector mostly fall into the low income earners, their contribution to the economic group of the country cannot be overemphasised. This is because of the amount of money they pay through various tax regimes in the country. Thus, with adequate support to this sector, their businesses can boom to the benefit of the country.

## 2.3 MICROFINANCE

According to the journal of Microfinance the term defines what'' is arguably the most innovative strategy to addresse the problem of global poverty '' this view is shared by United Nation (UN) which declared that the 2005 will be the international year, while their General Secretary Kofi Annan stated in 2002, that microcredit is a critical anti-poverty tool and a wise investment in human capital.

Various definitions have been provided to microfinance. Some of the definitions are:

Microfinance is the provision of small scale financial services to low income clients who have no access to financial services provided by the formal sector (Ledgerwoo, 1999; Robinson, 2001). Although microfinance services primarily include saving and credit, it may involve insurance, payment or money transfer. Therefore microfinance is a wider term that includes microcredit. Schreiner (2000) also define micro finance as formal scheme designed to improve the well being of the poor through better access to saving and services loans.



Houssain also describe microfinance as ‘’the practice of offering small, collateral free loans to members of cooperative who otherwise would not have access to capital necessary to begin a small business or other income generating activities. This view is to narrow, since it not only exclude such services as saving account and insurance but also ignores the possibility of collateral demanding MFIs. Although it is true that many MFIs do not take collateral, especially if they are focusing on the poorest that normally do not possess any collateral, several MFIs in fact do not require some form of collateral.

Armendáriz and Morduch (2005 p. 1) define microfinance as “a collection of banking practices built around providing small loans (typically without collateral) and accepting tiny savings deposits”. This collection may include pure banking services, or may include a broader social mandate, such as catering only for the very poor or women (empowerment). Other services can be part of what the microfinance offer, such as education, health, and training, marketing and planning. Microfinance institutions vary in size, geographical location, and institutional shape and may use different lending mechanisms (p. 20). Their target clients are those mostly in the micro enterprises or informal sector operators. The microfinance movement started with microcredit, focusing on loans only but the shift to microfinance has emphasised a broader concept that includes savings, provision of insurance and sometimes even distribution and marketing of clients' output (p. 14). Other financial services such as remittance transfers are also starting to make their way to microfinance (Meyer and Nagarajan, 2006, p.167).

According to Robinson and Marguerite (2001), "microfinance refers to small-scale financial services primarily credit and savings provided to people who farm or fish or herd; who operate small enterprises or micro enterprises where goods are produced, recycled, repaired, or sold; who 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". Many such households have multiple sources of income". Thus micro credit should be differentiated from micro finance; micro finance includes all financial services including micro credit.

## 2.4 MICROCREDIT

### 2.4.1 The Defining Criteria

Much of the current interest in microcredit stems from the Microcredit Summit (2-4 February 1997), and the activities that went into organizing the event. Definitions differ, of course, from country to country, but some of the defining criteria used include:

- *Size* - loans are micro, or very small in size.
- *Target users* - micro entrepreneurs and low-income households.
- *Utilization* - the use of funds - for income generation, and enterprise development, but also for community use (health/education) etc.

- *Terms and conditions* - most terms and conditions for microcredit loans are flexible and easy to understand, and suited to the local conditions of the community.

Microcredit, a central theme of microfinance (Greene and Gangemi, 2006), is broadly recognised as 'the practice of offering small, collateral-free loans to members of cooperatives who otherwise would not have access to the capital necessary to begin small businesses (Hossain, 2002, 79). A similar definition which defined microcredit as the extension of small amount of collateral–free institutional loan to jointly liable poor group members for their self-employment and income generation has been provided by Rahman (1998). According to the Wikipedia (2010), "microcredit is the extension of very small loans (microloans) to those in poverty designed to spur entrepreneurship. These individuals lack collateral, steady employment and a verifiable credit history and therefore cannot meet even the most minimal qualifications to gain access to traditional credit. Microcredit is a part of microfinance, which is the provision of a wider range of financial services to the very poor". All these definitions have elements identified above as characteristics of micro credits i.e. size of loans/credit, terms of loans/condition, target users and the use of the loan.

### 2.4.2 Principles of Microcredit

The principles of microcredit have also been applied in attempting to address several non-poverty-related issues. According to www.ssrn.com microcredit is based on a separate set of principles, which are distinguished from general financing or credit. It emphasizes building capacity of a micro-entrepreneur, employment generation, trust building, and help to the micro-entrepreneur on initiation and during difficult times. Sapovadia (2006) noted that microcredit is a tool for socioeconomic development.

### 2.4.3 The Three C's of Credit

Three variables are considered in order to give access to credit: the first is the character which explains how a person has handled past debt obligations. This is done by analyzing the borrowers' credit history, personal background, honesty and the reliability of the borrower to pay credit debts. The second is the capacity of the borrower. This indicates how much debt the borrower can comfortably handle. Income streams are analyzed and any legal obligations looked into, which could interfere in repayment. The last variable is the capital. The capital refers to the current available assets of the borrower, such as property, savings or investments which could be used to repay debt if income should be unavailable. ‘’ patant consultant international ‘’ Harness the power of Article marketing.www.financialvictory.com.

## 2.5 THE BACKGROUND AND CONCEPT OF MICRO CREDIT

Microcredit as a financial innovation is a concept that evolved as early as the 18th century but gained momentum only after the establishment of the Grameen Bank in Bangladesh by Prof. Muhammad Yunus in 1976 and for which he was awarded the Nobel Peace Prize in 2006. By lending amounts as small as $5 to women involved in making bamboo stools in Jobra village out of his own resources, Prof Yunus proved that micro loans can effectively tackle and reduce poverty. Over the years Grameen bank has disbursed several such small loans and assisted poor entrepreneurs to afford low cost credit to improve their small scale business units. Now microcredit programs have spread across the globe and are regarded as the best way to alleviate poverty.

According to www.nobleprice.org the origins of microcredit in its current practical incarnation, with attention paid by economists and politicians worldwide, can be linked to several organizations founded in Bangladesh, especially the Grameen Bank in the 1970s and onward. Cons and Paprocki (2008) observed that, in that country, it has successfully enabled extremely impoverished people to engage in self-employment projects that allow them to generate an income and, in many cases, begin to build wealth and exit poverty.

Due to the success of microcredit, many traditional banking industries have begun to realize that these microcredit borrowers should more correctly be categorized as *pre-bankable*; thus, microcredit is increasingly gaining credibility in the mainstream finance industry, and many traditional large finance organizations are contemplating microcredit projects as a source of future growth, even though almost everyone in larger development organizations discounted the likelihood of success of microcredit when it was begun. The United Nations declared 2005 the International Year of Microcredit (Wikipedia, 2010).

According to Buss, Terry. 1999 Microenterprise in International Perspective: An overview of the Journal of Economic Development. www.spaef.com/sample.html a review of current issues in the microcredit field as to why we need microcredit; the market structure- institutional size, organizational complexity, market share and branch bank location can negatively affect a formal bank's ability to lend to the poor

Market concentration- banks may not be lending to the poor because the financial market in developing countries are still underutilized so they are not forced into small business lending.

Monetary and taxation policy- National Government monetary policy can channel large amounts of capital away from credit into other investment instrument. This is especially a problem in developing countries where exchange rate and interest rate are highly politicized. Taxes levied by government make some lending profitable, forcing bank into other investment. Importantly, poor monetary policies especially inflation and instability reduce savings among the poor and affects group based microcredit programs adversely.



Regulation- Government bank regulation greatly reduces capital available for lending to small business, because banking stability is valued over more widespread access. Even if banks wanted to lend to microenterprises, regulations in many countries would not allow much of it.

Political intervention- Political interference in credit markets is rampant, especially in developing countries. Politicians direct funds into moribund state-owned firms, political cronies, or into the pockets of wealthy people, but rarely into the hands of poor people seeking credit. Poor people may need their own credit system.

## 2.6 THE ROLE OF MICRO CREDIT IN DEVELOPMENT

The roles of micro credit as a poverty alleviation strategy and a vehicle for providing financial services to the informal sector have continued to gain prominence in most developing countries and in Ghana in particular. The impact is not far fetched; this is because developing a broad based of micro-entrepreneurs in any economy is consequential to the substance of its growth and development process (Olujide, 1999). More recently, commentators such as Littlefield, Murduch and Hashemi (2003) have commented on the critical role of micro-credit in achieving the Millennium Development Goals. According to Simanowitz and Brody (2004, p.1), micro-credit is a key strategy in reaching the MDGs and in building global financial systems that meet the needs of the most poor people. Microcredit is a form of financial development that has primarily focused on alleviating poverty through providing financial services to the poor.

Littlefield, Murduch and Hashemi (2003) stated that "micro-credit is a critical contextual factor with strong impact on the achievements of the Millennium Development Goals (MDGs). Micro-credit is unique among development interventions: it can deliver social benefits on an ongoing, permanent basis and on a large scale". However, some schools of thought remain skeptical about the role of micro-credit in development. One such skeptic is Hulme and Mosley (1996). In their study on micro credit, while acknowledging the role micro-credit can play in helping to reduce poverty, they concluded from that "most contemporary schemes are less effective than they might be" (p.134). The authors argued that micro-credit is not a panacea for poverty-alleviation and that in some cases the poorest people have been made worse-off.

This notwithstanding, microfinance and thus micro credit has emerged globally as a leading and effective strategy for poverty reduction with the potential for far-reaching impact in transforming the lives of poor people. It is argued that micro credit and microfinance can facilitate the achievement of the MDGs as well as national policies that target poverty reduction, empowering women, assisting vulnerable groups, and improving standards of living. As pointed out by the former UN Secretary General Kofi Annan during the launch of the year 2005 as the International Year of Micro Credit:

*"The stark reality is that most poor people in the world still lack access to sustainable financial services, whether it is savings, credit or insurance. The great challenge before us is to address the constraints that exclude people from full participation in the financial sector.… Together, we can and must build inclusive financial sectors that help people improve their lives." --UN Secretary General Kofi Annan, 29 December 2003, announcing 2005 as the International Year of Microcredit (*Arch, 2005*).*

## 2.7 THE IMPACT OF MICRO CREDIT ON THE INFORMAL SECTOR



Micro-enterprise credit has become an increasingly popular development tool for addressing issues of poverty and unemployment. Since its birth in Asia in the early 1980's, it has spread to every corner of the globe (Ghate, 1992). In Bangladesh the "programmatic" success of the micro-credit scheme of Grameen Bank among poor women in Bangladesh became a demonstration of a successful development strategy (Rahman, 1998). It has proven very effective in providing support to street vendors, market vendors, and small-scale home-based businesses.

Micro-enterprise credit is based on the premise that small loans made to individuals with little or no collateral can help sustain and develop self-employed initiatives (Berger et al., 1989). A micro-enterprise is a business activity run by individuals or families with less than five workers (Lubell, 1991). Micro-enterprise credit increases productivity by allowing individuals to purchase equipment that is more efficient as well as achieve economies of scale through wholesale rather than retail purchases (Ghate, 1992). In terms of its social impacts, micro-enterprise credit has been a very useful strategy for empowering low-income informal sector participants, particularly females (Berger et al., 1989). Microenterprise credit has allowed females to gain access to economic resources, and achieve a higher degree of decision-making power in the home (Karim and Osada, 1998).

Microcredit has proven to be an effective powerful tool for poverty reduction. Like many other development tools however it has insufficiently penetrated the poorer strata of the society.

The poorest form the vast majority of those without primary healthcare and basic education; similarly they are the majority of those without access to microfinance.

While there is no question that the poorest can benefit from primary healthcare and basic education it is not as intuitive that they can benefit from microfinance, or microfinance is an appropriate tool by which to reach the millennium goals.

Microfinance has been extensively examined over the 10 and past 15 years, and the resulting literature is now very large. A focused review was conducted to evaluate the recent publication regarding the impact of microfinance on poverty reduction.

Interest in the social impact of microfinance has led to a number of impact studies published in scholarly journals. Ten of these studies assess microfinance programs in Bangladesh. Mckernan (1996) find that program participation can exert a large positive impact on self-employment profits, while Pitt and Khandker (1998) find that program credit has a significant impact on the well-being of poor households and that this impact is greater when credit is targeted to women. Seven other studies in Bangladesh (Hashemi et al. (1996); Goetz and Gupta (1996); Schuler and Hashemi (1994); Hashemi and Reiley (1996); Schuler et al. (1997); Schule et al. (1998); Steele et al. (2001) focus on the question of female empowerment. All but one find evidence that microfinance program participation exerts a statistically significant impact on one or more aspect of female empowerment, such as contraceptive usage or intra-household decision-making. The sole Bangladishi impact study failing to find significant impacts is Goetz and Gupta who find that significant portions of the women's loans were controlled by male relatives, thereby limiting the women's ability to develop meaningful control over their investment activities.

Outside of Bangladesh, published studies have assessed the impact of microfinance programs in Bolivia (Mosley (2001), China (Park and Ren (2001), Ecuador (Woller and Parson (2002), Ghana and South Africa (Afrane (2002), Guatemala (Kevane and Wydick (2001); Wydick (1999a), (1999b), (2002), Honduras and Ecuador (Smith (2002), Indonesia (Bolnick and Nelsos (1990), Peru (Dunn (2001), Thailand (Coleman (1999), Uganda (Barnes et al. (1999), Zambia (Copestake et al. (2001), and in multiple countries (Mosel and Hulme (1998) and Anserson et al. (2002). The findings vary considerably from study to study, suggesting that impacts are highly contextually specific.

Analyzing four programs in Bolivia, Mosley (2001) show that assets and income increased commensurate with initial poverty levels, but also that MFI services may increase vulnerability if borrowers over-leverage. Bolnick and Nelson (1990) find that MFI participation had a positive impact on enterprises that were typically small, labour intensive and growing, although the impact was far from uniform across sectors and target variables. Copestake et al. (2001) find that borrowers who were able to obtain two loans experienced high growth in profits and household income compared to a control sample, but borrowers who never qualified for the second loan were actually worse off due to MFI collection mechanisms.

Wydick (1999a) find that upward class structure mobility increases significantly with access to credit. Using the same Guatemala data set in a subsequent study (2002a0, Wydick also finds that rapid gains in job creation after initial credit access were followed by prolonged periods of stagnant job creation. Dunn (2001) finds that program clients' enterprises performed better than non-client enterprises in terms of profits, fixed assets, and employment. Finally, Anderson et al. (2002) analyze 147 MFIs and finds that microfinance participation increased environmental awareness and common pool resource stewardship.



Two published impact studies explicitly assed community, or village-level, impacts. In Bangladesh, Khandker et al. (1998) find that program participation has positive impacts on household income, production, and employment, particularly in the rural non-farm sector, and that the growth in self-employment was achieved at the expense of wage employment, which implies an increase in rural wages. Woller and Parson (2002) estimate that a microfinance program in Portoviejo, Ecuador contributes $480,000 per year in direct and induced economic benefits to the local economy.

Other impact studies address trade-offs that need to be considered when performing microfinance impact assessments. Mosely and Hulme (1998) study 13 MFIs in seven countries (Bolivia, Indonesia, Bangladesh, Sri Lanka, Kenya, India, and Malawi) and construct an "impact frontier" describing the inverse relationship they find between outreach (depth of poverty reached) and impact. Wydick (1999b) constructs a theoretical model to analyze the economic trade-off between future returns to schooling and the current return to child labour in Guatemalan household enterprises. He finds that in some states, microcredit increases the probability that children will attend school; however, during certain states of moral hazard, the cost of schooling may outweigh the benefits of child labour. Kevane and Wydick (201) find that targeting microenterprise credit to poor women appears to imply a trade-off between economic growth in favour of poverty reduction and child welfare. In particular, female entrepreneurs of child bearing age create significantly fewer jobs than male entrepreneurs.

Each of the impact assessment studies cited above, with one noted exception, provide evidence of positive impacts of microfinance. Other impact assessment studies, however, fail to find significant impact. In his assessment of Thai MFIs Coleman (1999) finds that “naive” estimates of impact failing to control for self-selection and endogenous (non-random) program placement significantly overestimate program impacts. He generalizes this finding to other impact assessments, arguing that most impact studies neglect the issues of self-selection and endogenous program placement thus leading to systematic overstatement of impact.

Making comparison across impact studies is greatly complicated by the contextual heterogeneity of programs assessed and the diversity of empirical methodologies used. The diversity of empirical methodologies in turn reflects the diversity in methodological options available. Hulme (2000) reviews the methodological option for doing impact assessments identifying three broad approaches: the scientific method (principally control-group surveys), the humanities tradition (ethnography and other qualitative methods), and participatory learning and action (participatory qualitative tools that include, for example, participatory rural appraisal, rapid rural appraisal, and farming systems research). He concludes that an optimal impact assessment mechanism should be a mix of the different methods for a fit between assessment objectives, program a context, human resources, and timing.

Hyman (1998) also consider the issue of optimal impact assessment methods by reviewing and comparing four MFI evaluation systems. Through his analysis, he suggests improved methods for existing assessment approaches. Woller et al. (1999b) survey 73 MFIs in the US and developing countries on their impact evaluation practices. They find that the sampled institutions regularly evaluated their programs, albeit using inexpensive and unscientific methods, regularly monitored project performance, saw evaluations as vital, used findings to implement project changes, and sought formal feedback from clients. The surveys find significant impacts.



## 2.8 ACCESS TO AND DEMAND FOR MICRO CREDIT

The delivery of microfinance (MF) services, dominated by the delivery of micro credit but also including savings, remittance services and insurance, has become a global enterprise. The micro credit industry, and the later expansion to micro finance, grew out of a response to the failure of subsidised, government-sponsored rural credit programmes in many developing countries. These began in the 1950s in many regions, but came under significant criticism in the 1970s due to low repayment rates and politically motivated debt write-offs using public funds (Johnson and Rogally (1997). However, the micro finance industry boomed from 1997 with the first global Microcredit Summit. The industry drew support from the prevailing development approach of the time, which emphasised market-based solutions to the problem of poverty (Johnson and Rogally, 1997; Rogaly, 1997).

The aim of major micro finance actors globally and in Ghana to extend access to credit to the poor (www.micocreditsummit.org ) implicitly assumes that the poor lack access to credit. During the boom time for micro credit in the mid-1990s, claims about the large unmet demand for credit and about micro credit's role in poverty reduction were called a “new evangelism.” By this was meant that beliefs that micro credit would support viable self-employment activities and bring reductions in poverty were strongly held if not always empirically established (Rogaly, 1996). This period also marked a shift from viewing micro credit as a development intervention to viewing it as a commercial activity, which could achieve its aims through large scale delivery and operationally sustainable micro finance institutions (Sharif, 1997).

Lack of data gathering about informal credit systems is a gap according to recommendations found in some of the micro credit literature. Some well-known micro credit practitioners recognise that good product design depends on knowledge of the context and customers (Sharif, 1997, Rogaly, 1996). This includes knowledge of the financial services already available, why they are used and what borrowers like and dislike about them. Being able to invest more in building knowledge of informal credit systems can assist micro finance institutions in understanding how their products may complement or displace existing credit products, and what the costs and benefits of such changes may be for poor clients (Johnson and Rogally, 1997, Rogaly, 1997). Investing the time to understand local credit systems can also lead to more responsive and innovative micro finance products, which are more widely accepted (Allen, 2007)

## 2.9 MICROFINANCE INSTITUTIONS (MFI)

According to the definition on ‘Microfinance Gateway’ an MFI is the organization that offers financial services to the low-income people (Microfinance Gateway, 2008). There is a wide range of micro financial institutions. Off all these, financial NGO`s seems to be dominant. Many NGO’s provide other financial services along with the micro finance and similarly some commercial bank are also providing micro finance along with their routine financial activities so because of these micro finance services which are quite bit part of the whole of the activities of these commercial banks we can call these as a micro finance institutions (Rehman, 2007).

There are some other MFI´s that can be considered in the business of micro finance. These institutions are the community based financial intermediaries such as credit union; cooperative housing societies and some other are owned and managed by the local entrepreneur and municipalities. This type of institution is varying from country to country (Rehman, 2007).

### *2.9.1 Structure and Key Stakeholders of Microfinance in Ghana*

In Ghana, there are many institutions working in the area of microfinance and micro credit in particular. The structure and key microfinance stakeholders in Ghana consist of the micro finance institutions, micro finance apex bodies, end-users, technical service providers, supporting institutions and the government institutions.

The Microfinance Institutions includes The Rural and Community Banks, Savings and Loans Companies, Financial NGOs, Primary Societies of CUA, Susu Collectors Association of GCSCA, Development and commercial banks with microfinance programs and linkages, as well as Micro-insurance and micro-leasing services. The Microfinance Apex Bodies are the Association of Rural Banks (ARB), ARB Apex Bank, Association of Financial NGOs (ASSFIN), Ghana Cooperative Credit Unions Association (CUA) and Ghana Cooperative Susu Collectors Association (GCSCA).

End Users of micro finance product are the economically active poor who are clients of microfinance products and services. Technical Service Providers of the micro fiancé product are the Business Development Service Providers to MFIs and their clients.

Supporting Institutions of micro finance in the country includes Microfinance and Small Loans Center (MASLOC), the Ghana Microfinance Institutions Network (GHAMFIN), Development partners and international non-governmental organisations and Universities, training and research institutions. Finally, Government Institutions regulating the microfinance sector are the Ministry of Finance and Economic Planning, Ministries, Departments, Agencies (MDAs) and Metropolitan, Municipal and District Assemblies (MMDAs) and the Bank of Ghana.



### 2.9.2 SUMMARY

In this chapter I have reviewed the evolution of microfinance over the past years and examined briefly three of the MFIs models that exist today. The role of MFIs in development, specifically in relation to alleviation of poverty was also examined.

Key challenges facing MFIs today that are affecting their impact on poverty alleviation were seen to be an over-emphasis on financial sustainability over social objectives, and a failure of many MFIs to work with the poorest in society.

## CHAPTER THREE

## METHODOLOGY

### 3.1 INTRODUCTION

In view of the topic, this chapter indicates the research methods used in collecting data for the study. It therefore consists of research design, sources of data, population of the study, the sampling size and technique, the type of data collection instrument that were used and how the data was analyze.

### 3.2 TYPES AND SOURCES OF DATA

For the purpose of this study, data was collected from two sources. They are data from primary and secondary sources.

#### 3.2.1 Primary Source of Data

Primary data was collected from respondents through the questionnaires which were the main research instrument. The primary data was gathered from a section of the operators of the informal sector in the Grater Accra Region.

#### 3.2.2 Secondary Source of Data

Secondary data was collected from the publication works of other people. This included literature from text books, journals and the internet. This was necessary since it helped to add to the findings of the research.

### 3.3 POPULATION OF THE STUDY

The population for this study is made up of all operators of micro enterprises in the informal sector. Obviously, it was impossible to cover the whole population so a sample was used.

### 3.4 SAMPLE SIZE AND SAMPLING METHOD

The study selected 60 operators of the informal sector from various disciplines who have and still access micro credit facilities from micro finance institutions. Stratified sampling procedure was employed in selecting the various segments in the informal sector. Then simple random sampling was used to select the individual operators from the segment. Simple random sampling procedure employed in selecting individual respondents. This approach ensures that every member of the target population has an equal chance of being included in the study. Its main advantage is that it eliminates bias.

### 3.5 RESEARCH INSTRUMENT: QUESTIONNAIRE

The questionnaire was used as the main research instrument. The research instrument will comprise both close and open ended questions. This was to enable the respondents to choose from alternative answers given as well as expressing their views on the subject. Only one set of questionnaire was designed for the informal sector operators. This helped the researcher obtain a varied and reliable data from the different operators of the sector who experiences the same set of issues that confront them in their operations.

The questionnaire has four sections based on the biographic information of the respondents and the objectives of the study. Section A comprised questions on the demographical information of the respondents using close and open ended questions. Section B and C consist of questions on the socio-economic impact of micro credit and the level of satisfaction of the respondents. The last section, D contains questions on the challenges of the informal sector with assessing micro credit. This section will employ the use of ordinal scale to rank the intensity of the challenges that the respondents face. Ordinal scale is a measurement in which numbers are assigned on the basis of some order of the objects. The most pressing challenge is to be ranked as **7** and the least as 1.

## 3.6 ADMINISTRATION OF THE RESEARCH INSTRUMENT

Before the questionnaires were distributed the operators of the informal sector were informed by explaining the purpose of the research, and how the information was used. Communicating to the respondents before distributing the questionnaire helps to increase the response rate, and address ethical concerns. The questionnaires were distributed by the researcher and it was made at a time all the respondents are less busy. The interview that was conducted was done using questionnaires that was interviewer-administered.

The validity of a research is concerned about whether the findings are really about what they appear to be about. For purposes of validation, a sample of the survey questionnaires was pre-tested by conducting an initial survey on fellow students to test the information gained from the questions and the time taking to complete it. They asked as part of the pilot study, suggestions and corrections that was help in re-examination of the content of the survey/interview questions to find out the reliability of the instrument so as to determine irrelevant questions that have to be discarded.

## 3.7 DATA PRESENTATION AND ANALYSIS

The data that was generated from the study was analyzed qualitatively. Processing the data from the questionnaires was evaluated using the latest Statistical Package for Social Sciences (SPSS)/PC software which is a computer program used for statistical analysis, data management and data documentation. Descriptive statistics was used to analyze the data. Frequency tables and figures were used mostly for the respondent's biography data.

# CHAPTER FOUR

# RESULTS ANALYSIS AND DISCUSSION

## 4.1 INTRODUCTION

This chapter provides the empirical findings and discussions from the collected data. The analyses of the findings are based on the research questions or objectives of the study. In all, 60 respondents in the informal sector were purposively selected and involved in the study. It provides demographic information of the respondents and the statistical analysis of the information collected from them. This is followed by the interpretation and discussion about the findings.

## 4.2 DEMOGRAPHICAL INFORMATION

### 4.2.1 Gender

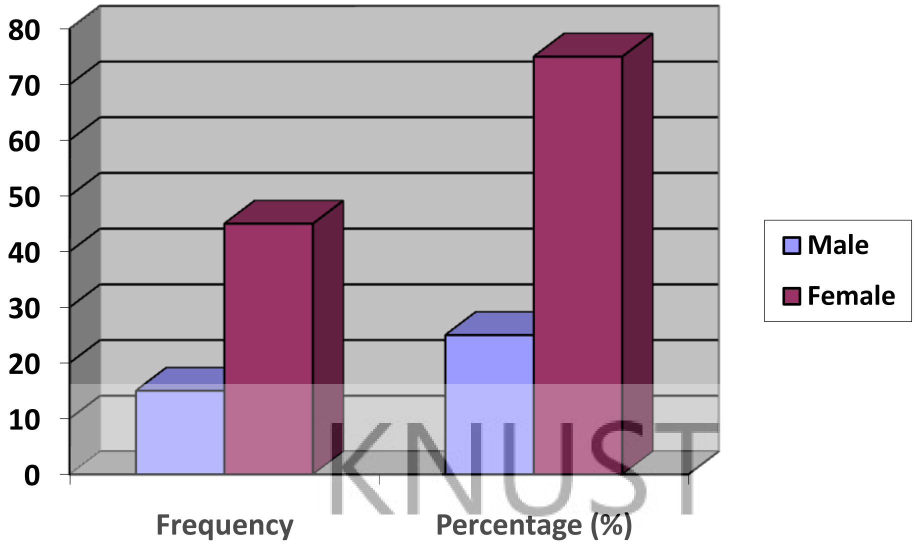
The study in Table 4.1 shows that, a majority of the respondents were women that testify to the fact that most of the beneficiaries of microcredit in the informal sector could be women because we have selected people randomly without any bias towards any segment of gender.

**Table 4.1: Gender Distribution of Respondents**

| **Gender** | **Frequency** | **Percentage (%)** |
|---|---|---|
| Male | 15 | 25 |
| Female | 45 | 75 |
| **Total** | **60** | **100** |

**Source: Field Survey (2011)**

**Figure 4.1: Gender Distribution of Respondents**




**Source:** Field Survey (2011)

### 4.2.2 Marital Status

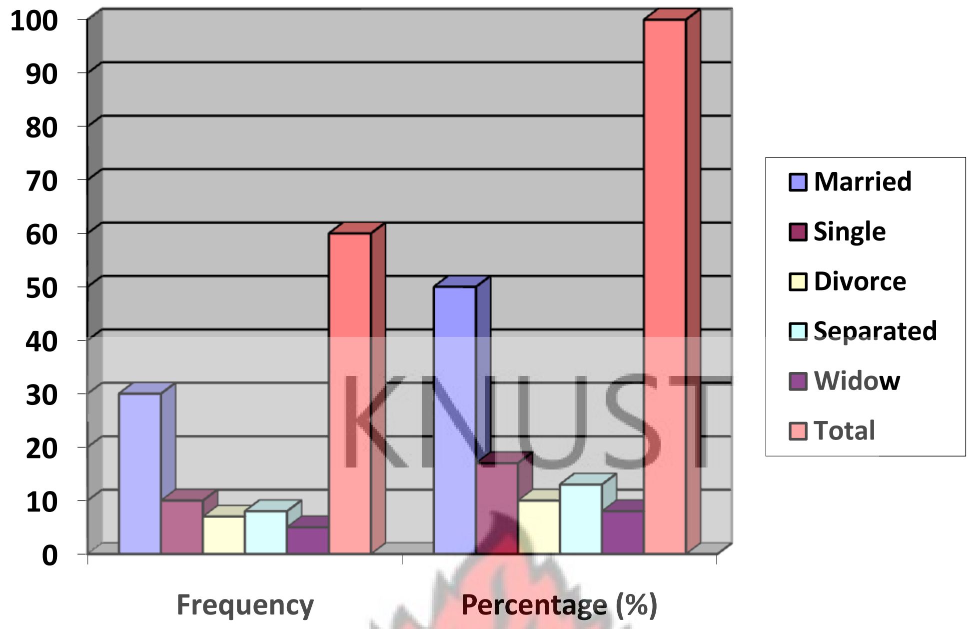
The study as indicated in Figure 4.2 shows half of respondents were married. And 17% were not married while an insignificant number were widow, 10% were divorce and 13% were separated. Traditionally, the thought is that it is married persons that do business to get funds to take care of the families. However, it can be seen from the data gathered that this does not hold true.

**Table 4.2: Distribution of the Marital Status of Respondents**

| **Marital Status** | **Frequency** | **Percentage (%)** |
|---|---|---|
| Married | 30 | 50 |
| Single | 10 | 17 |
| Divorce | 7 | 10 |
| Separated | 8 | 13 |
| Widow | 5 | 8 |
| **Total** | **60** | **100** |

**Source: Field Survey (2011)**

**Figure 4.2: Distribution of the Marital Status of Respondents**




**Source:** **Field Survey (2011)**

### 4.2.3 Age

From the data in Figure 4.2.3, it shows that most of the respondents are between 18-25 representing 45%. 25% are also in the ages between 26-35, whilst 20% are in the ages between 36-43 and the remaining 10% are above 44 years Thus, micro entrepreneurs in this age group are more interested in accessing micro credit services from the MFIs. Therefore, with emphasis on making credit facilities available to these entrepreneurs, micro credit provision will be enhanced.

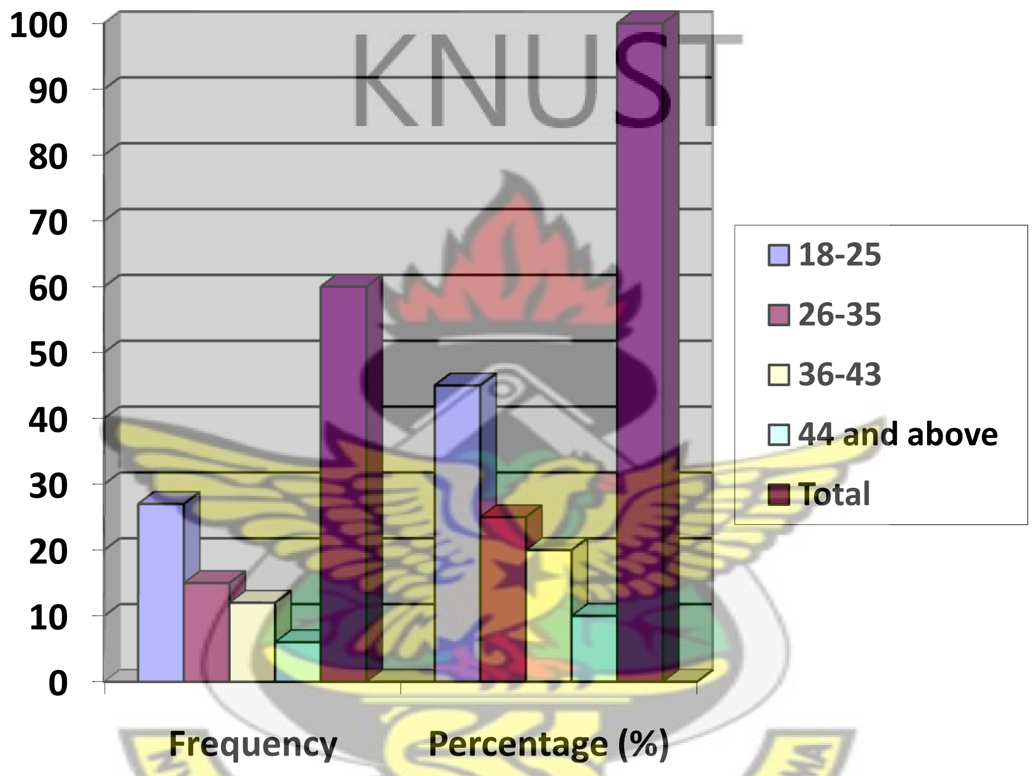
**Table 4.3: Age Distribution of Respondents**

| Age | Frequency | Percentage (%) |
|---|---|---|
| 18-25 | 27 | 45 |
| 26-35 | 15 | 25 |
| 36-43 | 12 | 20 |
| 44 and above | 6 | 10 |

| | | |
|---|---|---|
| **Total** | **60** | **100** |

**Source: Field Survey (2011)**

**Figure 4.3: Age Distribution of Respondents**




### 4.2.4 Educational Attainment

This variable classified the respondents in terms of their educational experience. It could affect the way in which they manage and live their daily lives and manage the household and business because of access to microcredit facilities. The study indicated that about 70% of respondents did not have tertiary education. As operators in the informal sector, this low level of education can affect management of business adversely since most of such business organisatons are self-managed.

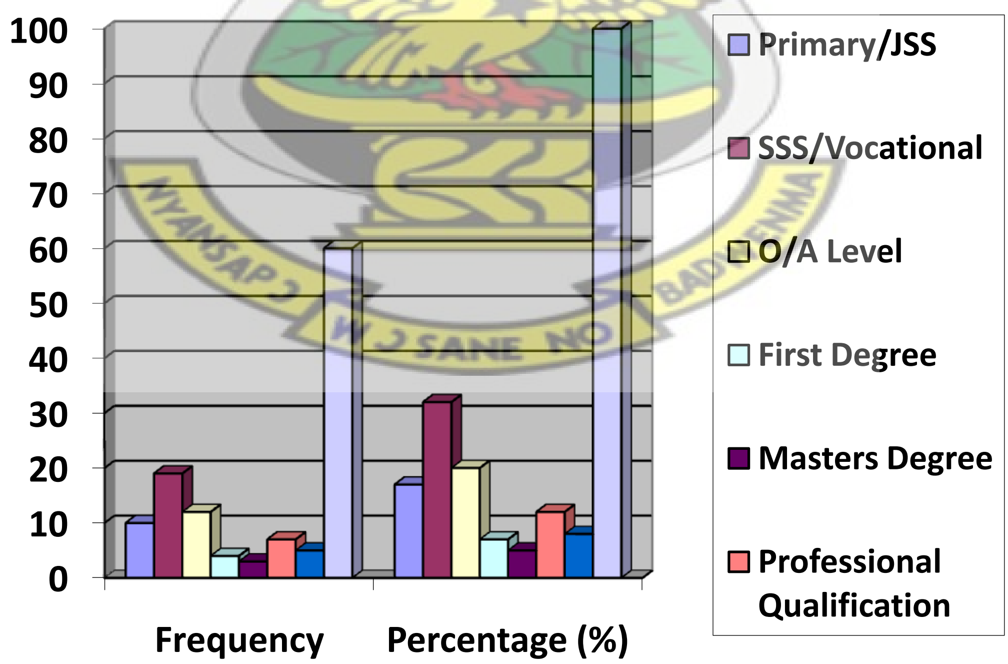
**Table 4.4: Distribution of Educational Level of Respondents**

| Educational level | Frequency | Percentage (%) |
|---|---|---|
| Primary/JSS | 10 | 17 |
| SSS/Vocational | 19 | 32 |
| O/A Level | 12 | 20 |
| First Degree | 4 | 7 |
| Masters Degree | 3 | 5 |
| Professional Qualification | 7 | 12 |
| Others | 5 | 8 |
| **Total** | **60** | **100** |

**Source:** Field Survey (2011)



**Figure 4.4 Distribution of Educational Level of Respondent**



### 4.2.5 Number of Children

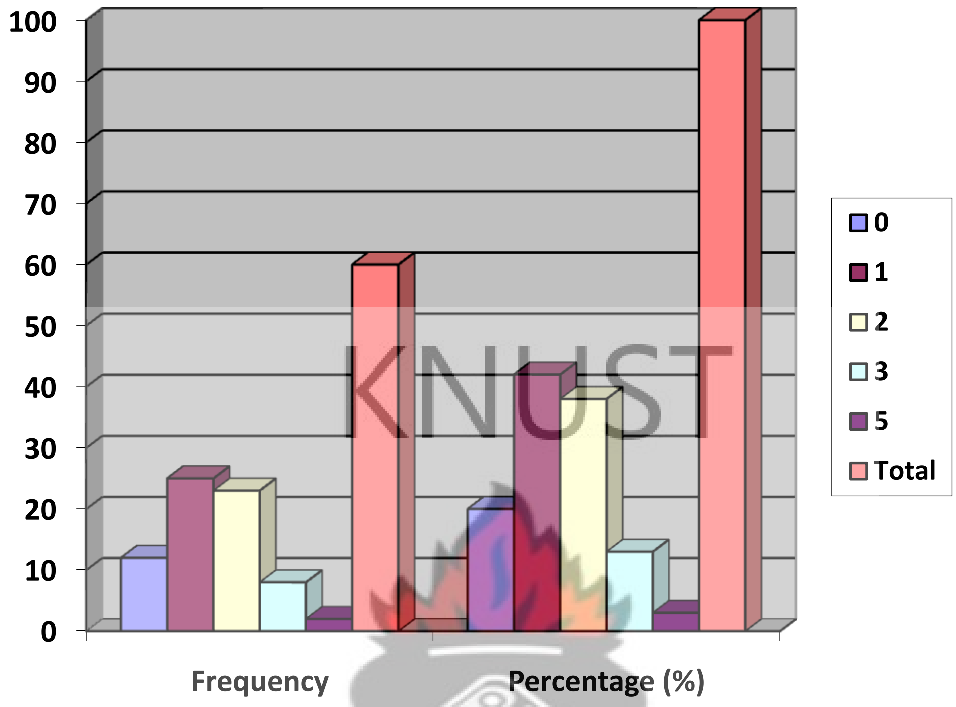
The researcher found out how many family members each respondent have because a large family size usually have higher expenses than a smaller family. In microcredit field and in most cases in the informal sector, most of the businesses have sole proprietors. Family members contribute to this small-scale business as additional workers. The data as indicated in Table 4B shows that majority of the respondents have no children. This means that majority of the respondents will not spend more on their family. Conversely, this will deprive the operators the needed family labour to support their business and will thus have to rely on hired labour as an added cost.

**Table 4.5 Distribution of Number of Children of the Respondents**

| **Number of Children** | **Frequency** | **Percentage (%)** |
|---|---|---|
| 0 | 12 | 20 |
| 1 | 25 | 42 |
| 2 | 23 | 38 |
| 3 | 8 | 13 |
| 5 | 2 | 3 |
| **Total** | **60** | **100** |

**Source: Field Survey (2011)**

**Figure 4.5 Distribution of Number of Children of the Respondents**




## 4.3 LOAN TERMS AND CONDITIONS

### 4.3.1 Sources of Initial and Subsequent Capital for Business

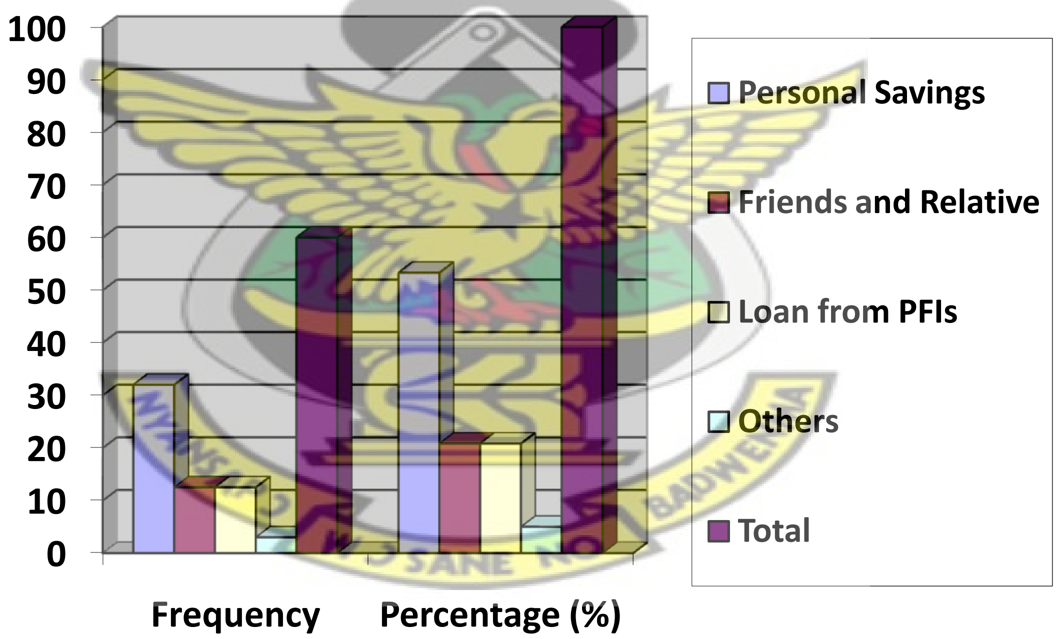
Figure 4.4 shows the source of start up capital of the respondents. The study found that majority of the respondents began with own savings and if it is anything to go by, the informal sector often depends on their personal savings to start their businesses. It also means that microfinance institutions may not necessarily be the major source of initial capital for the informal sector operatives and thus, may not play a significant role in helping poor people to start their own business.

**Table 4.6: Distribution of Initial Source of Capital**

| Source of Capital | Frequency | Percentage (%) |
|---|---|---|
| Personal Savings | 32 | 53.3 |
| Friends and Relative | 12.5 | 20.83 |
| Loan from PFIs | 12.5 | 20.83 |
| Others | 3 | 5 |
| **Total** | **60** | **100** |

**Source:** **Field Survey (2011)**

**Figure 4.6: Distribution of Initial Source of Capital**




Since the study used a purposive sampling to select those who have accessed microcredit facilities from micro finance institutions, all the respondents have accessed credit from those institutions before. The study found that most of the respondents obtained their loan facility from microfinance institutions. Some of these institutions as used by the respondents include Pro-Credit Savings and Loans, Express Savings and Loans, Begee Capitals, Sinapi Aba Trust, JB's Capital Limited, Easy Savings and Loans, Micro Wealth Savings and Loans, and E-jobs Limited. Only two respondents obtained their credit facility from commercial banks i.e. SSB Bank Limited and Women's World Banking Limited.

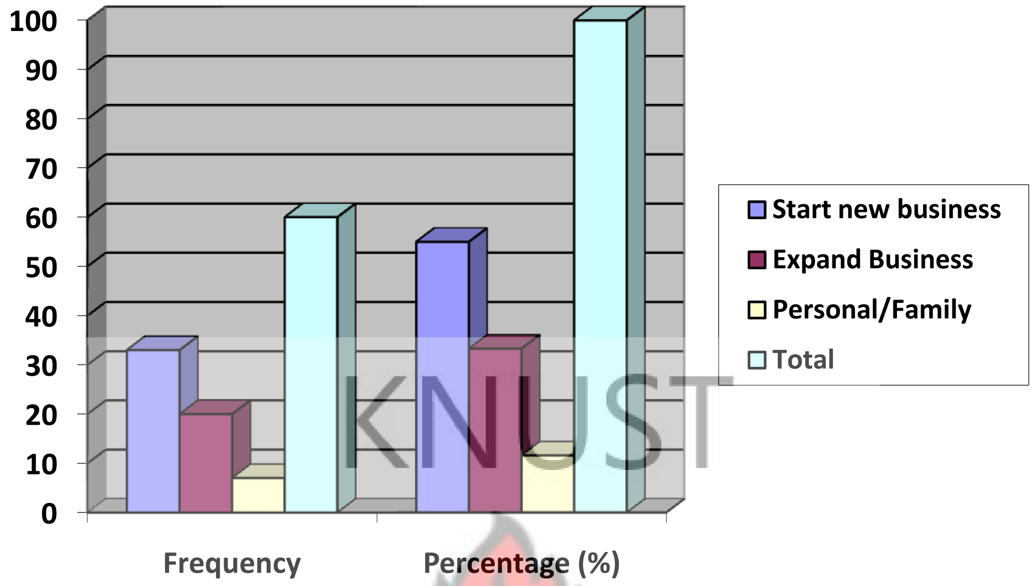
### 4.3.2 Purpose and Amount of Credit Obtained

The study found that majority of the respondents accessed the credit facility to enable them expand their business. These represent 53.3% of the sample. Those who accessed the facility from the microfinance institutions did to start their business. 20.83% of the respondents obtained their credit facility to specifically meet their personal or family obligations. These obligations include paying for their children school fees and feeding. These findings are consistent with the earlier findings on their source of initial capital. Majority of the respondents who used their personal savings to engage in business are those who went in for the credit facility to expand their business. Conversely, those who got their initial capital from the institutions are those who used the facility to start their business.

**Table 4.7: Purpose for Accessing Loan from MFIs**

| **Purpose** | **Frequency** | **Percentage (%)** |
|---|---|---|
| Start new business | 33 | 55 |
| Expand Business | 20 | 33.3 |
| Personal/Family | 7 | 11.6 |
| **Total** | **60** | **100** |

**Figure 4.7: Purpose of Accessing Loan from MFIs**




The study further indicated that the amount of credit facility obtained from the financial institutions depends solely on whether the source of the credit facility emanates from a microfinance institutions or a commercial bank. It appeared from the study that those respondents who borrowed their loan facility from the microfinance institutions got smaller amounts than those from the commercial banks. In all, the amount of loan approved for the respondents ranged from GH¢ 200.00 to GH¢ 20,000.00. The minimum amount that was approved for the respondents from the microfinance institutions was GH¢ 200.00 while the maximum amount was GH¢ 3500.00. Most of the respondents were approved an amount of GH¢ 500, GH¢ 700 and GH¢ 1000. The amount approved for those who accessed their facility from the commercial banks vary from GH¢ 5000 to GH¢ 20,000.00.

**Table 4.8: Amount of Loan Granted by Microfinance Institutions**

| Characteristic | Measuring group | Frequency | Percentage (%) |
|---|---|---|---|
| Amount of Loan Received from MFIs | Less than GH¢ 1,000 | 38 | 63.4 |
| | GH¢ 1,000 – GH¢ 3,500 | 13 | 21.6 |
| | More than GH¢ 3,500 | 9 | 15 |
| | Total | 60 | 100 |

**Source: Field Survey (2011)**

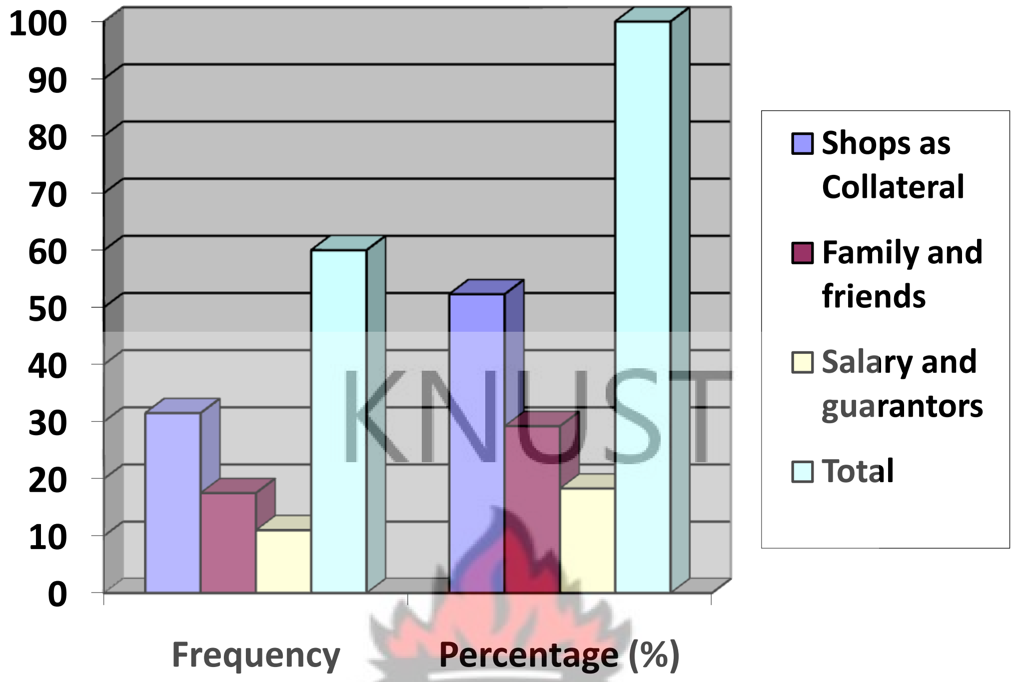
These findings revealed that microfinance institutions have a limited amount of credit facility that they offer their clients who are mostly those in the informal sector. As a result, an informal sector operator who wants to embark on a huge business venture will be limited by the amount of loan facility to be obtained from the microfinance if such a person could not access the facility from a commercial bank. Indirectly, the result shows the lack of sufficient capital to start up a business by the informal sector operators due to less amount loan offered by microfinance institutions.

### 4.3.3 Nature of Collateral and Durations of Credit Facility

**Table 4.9**

| Nature of Collateral | Frequency | Percentage (%) |
|---|---|---|
| Shops as Collateral | 31.5 | 52.3 |
| Family and friends | 17.5 | 29.2 |
| Salary and guarantors | 11 | 18.3 |
| **Total** | **60** | **100** |

**Figure: 4.9 Nature of Collateral and Duration of Credit Facility**




The study found that the nature of collateral facility used for acquiring the credit facility vary depending on the amount of loan facility approved by the institution. The study shows that most of the respondents (52.5%) used their shops as collateral in order to access the loan. This was followed by those (29.2%) who used their family or personal lands as collateral. Eleven respondents (18.3%) used their salary and a guarantor to obtain the credit facility. These are respondents who obtained their credit facility from the microfinance institutions with the amount of loan involved being from GH 200 to GH 3500.

Further, those who obtained their facility from the commercial banks used their house and some cases in addition to a car to secure their loan. The requirements for the use of these types of collaterals by the microfinance institutions tend deter the informal sector operatives (who lack these facilities) from accessing credit facilities from them. This could certainly explain why most of the respondents rely on their personal savings to start their businesses. After establishing their business, they then have a safety net which they could rely on for use as collateral to obtain sufficient loan to expand their business.

From the study, the duration of the processing of the loan facility tends to depend on the amount of the loan requested for and the institution offering the loan. The duration varies from three (3) days to six (6) months. Those who accessed their facility from the microfinance institutions got their loans within three days to three weeks while those who got theirs from the commercial banks got it in months. Most of the loan applications of the respondents were approved within three and five days for the microfinance institutions.

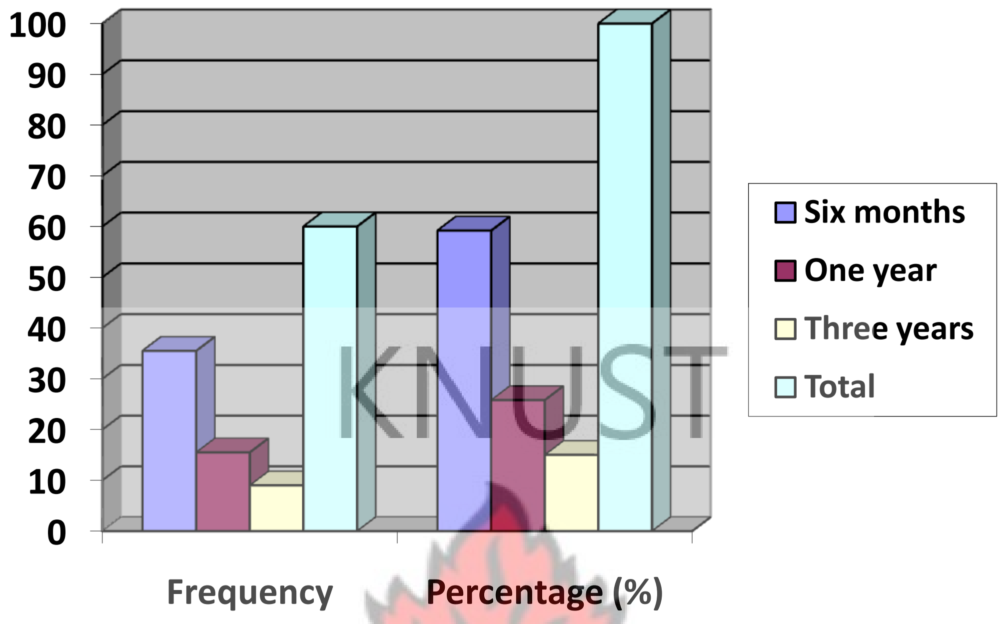
In accessing the effectiveness of a microcredit facility, the duration taken for the loan to be processed and approved greatly tend to affect the ability of the borrower to repay. This is because the borrower wants to use the facility within a given business period with the anticipated gain and when that is not done, he or she may not be able to gain the needed capital to pay back. This initiative by the microfinance institutions is thus a good step in ensuring the effectiveness of the facility, as it will reduce default rates.

**Table 4.10: Length of Loan**

| **Length of Loan** | **Frequency** | **Percentage (%)** |
|---|---|---|
| Six months | 35.5 | 59.2 |
| One year | 15.5 | 25.8 |
| Three years | 9 | 15 |
| **Total** | **60** | **100** |

**Source: Field Survey (2011)**

**Figure 4.10; Length of Loan**




The length of the loan facility was found to vary from six months to three years. This variable depends on the amount of loan borrowed. 59.2% of the respondents have their loan length to be six months while 25.8% and 15% of them have theirs to be one year and three years respectively. The study found that the repayment terms are mostly monthly and bi-yearly. While 84.60% of the respondents pay monthly, 15.40% of them pay bi-yearly. It appeared from the study that the length of the loan facility is in the best convenience of the respondents. 69.20% of the respondents said they are able to pay within the given period but 30.80% of them said they could not.

The 30.80% of the respondents said they had difficulty paying the loan within the stipulated time due to reasons such as decline in business performance, and insufficient funds to pay because of their customers' indebtedness to them. The study found that for these categories of clients who are unable to pay at the given time, the microfinance institutions often extend the repayment period for them but with an increase in the interest rates of the loan. In some cases, the institutions does nothing about extending the duration but only to ask them to do everything possible to pay on time.

## 4.4 SOCIO-ECONOMIC IMPACT OF MICROCREDIT

The study found that access to microcredit by the informal sector operatives has had an impact on their social and economic lives. Micro-enterprise credit had a significant effect on both business and personal assets. On the economic impact, the study found that the credit facility had help the operatives to expand their business by enlarging their product varieties, increasing the size of their shop, increasing their profit margin, employing more employees and thus their output and income increases. Thus, microcredit facilities were found to be important is the creation of employment opportunity. They also claimed that these improvements on their economic lives have helped them to meet their family obligations and responsibility by contributing significantly to the household income. The access to micro-enterprise credit also empowered females both at home and business. This has helped them to educate their children, meet their health needs as well as other unforeseen needs. To sum up, it can be noticed from the overall analysis that there is significant impact of microcredit activities on improvement of the living standard of the informal sector operators' family not only in economic term but also in social term.

The respondents further indicated that to this end, the microcredit has affected their business and households. 38.50% of the respondents said the microcredit has affected their socio-economic lives to a very large extent. While 15.40% of them said it has not much impact on them, 46.20% of them said it has only affected them to some extent. The study found that majority of the respondents (69.20%) said they made a profit after accessing the loan facility but 15.40% of them incurred a loss. Another 15.40%

of them said they have not seen any change on their output level. For those who made profit, they claimed they made about 50.00% of the loan they acquired.

The respondents indicated that in the short-term, they intend to use part of their profit to pay back the amount they owe the financial institutions, and reinvest in the business. In the long-term, they intend to invest in treasury bills, and build a house. Those who run a loss said they rely on the intervention of their friends and family members in order to repay the loan.

### 4.5 LEVEL OF SATISFACTION WITH MICROCREDIT FACILITY

Most of the respondents claimed that interest rate was quiet high. Some other respondents said it was comparatively okay compared to the commercial banks. On the procedure for accessing the loan, the study found that the respondents have mixed feelings. While some said it was cumbersome and hectic, others claimed it was simple.

The study also established the conception about operational assistance of microfinance institutions that affect positively to run the business successfully. This is also one of the reasons of micro-credit scheme being popular. It is an effective mechanism, which assists both lenders and borrowers. The borrowers get the guidelines from the microfinance institutions' workers to develop or to run the small business, which can hardly be expected from conventional banks. This is another reason of poor people to become microfinance institutions oriented. The respondents have also indicated that incentives for repayment are favourable and most often takes the form of a promise of more loan facilities.

The study found that 53.80% of the respondents said they are satisfied with the nature of the microcredit scheme provided them by the microfinance institutions. 30.80% of them were not satisfied and attributed their level of dissatisfaction to the high interest rates and collateral requirements. This is shown in Figure 4.6 below.

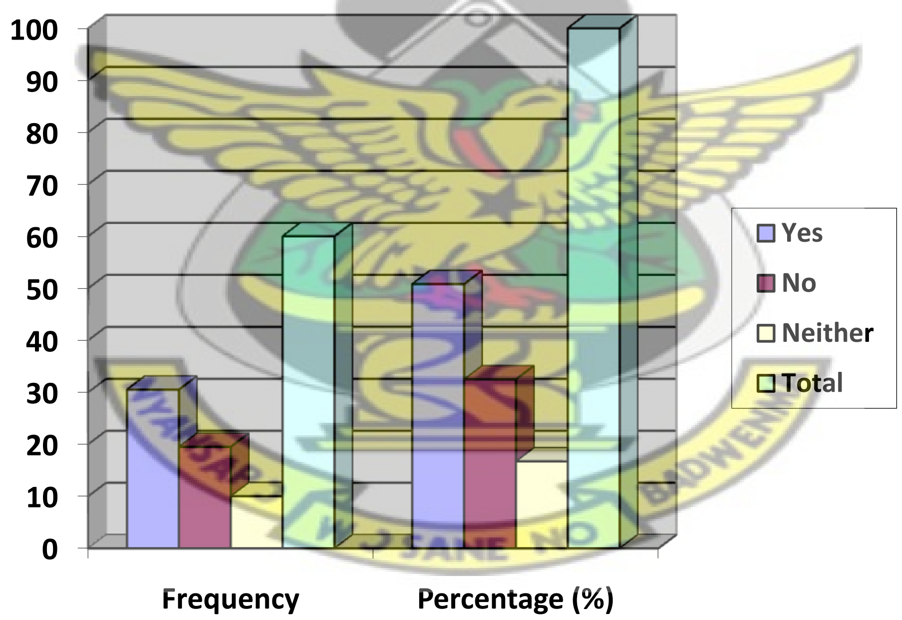
**Table 4.11: Respondents Satisfaction with Microcredit Facilities**

| Level of Satisfaction | Frequency | Percentage (%) |
|---|---|---|
| Yes | 30.5 | 50.8 |
| No | 19.5 | 32.5 |
| Neither | 10 | 16.7 |
| **Total** | **60** | **100** |

**Source:** Field Survey (2011)



**Figure 4.11: Respondent Satisfaction with Microcredit Facilities**



## CHALLENGES CONFRONTING INFORMAL SECTORS TO ACCESSING MICROCREDIT FACILITIES

The study purports to find out the challenges that informal sector operators face in acquiring loan facilities from microfinance institutions. The respondents were to rank the challenges as it affects them. The total ranks of the challenges were summed up and the results are presented below. The study found that the most pressing challenge facing the informal sector operators in accessing microcredit is unfavourable collateral security demands from the microfinance institutions.

As seen in the previous sections, the requirement for collateral by the institutions deters most of the informal sector operators from accessing their initial capital from them. This was followed by low loan size and unfavourable repayment terms (2$^{nd}$) and cost of access to credit source due to time and money (3$^{rd}$). Lack of specific policy guidelines and goals from the microfinance institutions toward the informal sector (5$^{th}$) and inadequate credit funds and growing demands of credit (6$^{th}$) have been identified as the least pressing challenges facing the informal sector operators.

**Table 5: Challenges of the Informal Sector in Accessing Microcredit Facilities**

| **Challenges** | **Sum of Ranks** | **%** | **Rank** |
|---|---|---|---|
| Lack of specific policy guidelines and goals from the microfinance institutions toward the informal sector | 84 | 13.68 | 5th |
| Inadequate credit funds and growing demands of credit | 74 | 12.05 | 6th |
| Unfavourable collateral security demands from the microfinance institutions | 156 | 25.41 | 1st |
| Unfavourable eligibility criteria | 88 | 14.33 | 4th |
| Low loan size and unfavourable repayment terms | 120 | 19.54 | 2nd |
| Cost of access to credit source due to time and money | 92 | 14.98 | 3rd |
| **Total** | **614** | **100** | |

**Source:** **Field Survey (2011)**

# CHAPTER FIVE

# SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

## 5.1 SUMMARY OF FINDINGS

The goal of this research was to study the challenges confronting the informal sector in accessing microcredit facilities from the microfinance institutions. The study used a survey research strategy to survey 60 informal sector operators in the Greater Accra Region. A self-developed questionnaire was developed by the researcher and used for the study. The analysis of the data was done based on the research questions or objectives and was divided into two parts; the biographic information of the respondents and the analysis of the specific objectives.

The following findings were made in relation to the specific research objectives:

There is significant impact of microcredit activities on improvement of the living standard of the informal sector operators' family not only in economic term but also in social term through the improvement in the business activities and employment creation avenues among others.

The study found that 50.8% of the respondents are satisfied with the nature of the microcredit schemes provided them by their respective microfinance institutions. 32.5% of them were not satisfied and attributed their level of dissatisfaction to the high interest rates and collateral requirements.

The study found that the most pressing challenge facing the informal sector operators in accessing microcredit is unfavourable collateral security demands from the microfinance institutions.

The study also found out that most of the respondent obtain their loan facility from the microfinance institutions some of these institutions as used by the respondent include Pro-credit savings and loan, express savings and loans, Easy savings and loans etc.

The study reveals that microfinance institutions have a limited amount of credit facility that they offer their clients who are mostly those in the informal sector. As a result an informal sector operator who wants to embark on a huge business will be limited by the amount of loan facility from the microfinance institutions.

Also the study further reveals that the nature of collateral facility used for acquiring the credit facility vary depending on the amount of loan facility approved by the institutions. The study further shows that most of respondent (52.5%) used their shop as collateral in order to access the loan. This was followed by those (29.2%) who used their family and friends or personal lands as collateral. While (18.3%) used their salary and a guarantor to obtain the facility

The study also revealed that access to microfinance by the informal sector operators has had an impact on their social and economic lives by a significant effect on both business and personal assets

On the economic impact, the study found that the credit facility had help the operators to expand their business by enlarging their products varieties, increasing the size of their shops, increasing profit margin, employing more employees and thus their output and income increase. Thus microcredit found to be important by creating employment opportunities.

Lack of specific policy and guidelines and goals from the microfinance institutions towards the informal sector was also found out as a challenge in the informal sector.

## 5.2 CONCLUSIONS

Provision of financial services to the poor and thus the informal sector operators is considered as one of most effective strategies to eradicate poverty in developing countries. The poor need finance services; they should be able to borrow money for consumption purposes, start a business, expand an enterprise and need to save in small amounts and send their child to school and all these opportunities open the door to increase quality of their lives.

Access to financial services at all level of the economy makes substantial growth and development, and this is more consequential for the informal sector in the country which happens to be the largest employer in the country. However, traditional financial systems i.e. commercial banks are reluctant to provide financial services to this section of people of the population. Consequently, informal sector operators are for the most part excluded from the formal credit markets.

Microcredit is recognized an effective endeavour started in this century as an alternative remedy to provide credit services to the destitute overcoming the typical problems that exists in the formal credit markets. In order to make microcredit facilities more accessible to the informal sectors, the challenges with regard to the collateral, and the loan amount that is approved among other factors needs to be properly looked at. The need to harness the potentials of the informal sector in development now in the history of the country cannot be overemphasized. This can be achieved through creating and making access to microcredit facilities by the microfinance institutions possible.

## 5.3 RECOMMENDATIONS

In order to make microcredit facilities accessible to the informal sector, the following recommendations become imperative:

Deliberate attempt should be made to incorporate the informal sector into the main stream economy by deliberately studying the sector at the national and regional levels in order to develop a reasonable data base on which sector specific policies could be designed and implemented.

Public and private financial institutions should be encouraged to grant the sector access to loanable funds on flexible terms to reflect their distinct characteristics.

Guarantee schemes are an important instrument for governments to support the informal sector. As such, the government should identify various loan and mutual guarantee schemes that are available to the benefit of the informal sector.

A combination of soft aid measures and financial support schemes may be an appropriate way to facilitate the informal sectors' access to finance. Soft aid measures (advice, training etc.), should aim at raising the operators awareness of the existence of support schemes and of the conditions under which support is provided. In addition, entrepreneurs' knowledge of financing issues should be encouraged and greater transparency of micro credit institution’s loan decisions and rating procedures should be ensured.

The micro credit lending institutions should be encouraged to emphasize on the relationship lending technologies, which is based on "soft" information. The soft information may include the character and reliability of the informal sector owner based on direct contact over time by the institution's loan officer; the payment and receipt history of the sector gathered from the past provision of loans, deposits, or other services to the informal sector by the institution.

Monitoring of the micro credit institution's sector in the aspects of loans and advances disbursement should be streamlined as nobody is following government directives. There is the need to develop various credit products and services, such as credit lines, risk sharing activities, leasing, credit scoring and expert decision-making, as well as efficient credit bureaus.

Banking norms and attitudes towards informal sector financing should be changed since this sector differ considerably from the traditional clientele and do not conform to the norms detailed in the manual of banking norms and procedures. Therefore, it needs a concerted effort of different micro credit financial institutions, commercial banks or even insurance companies to make informal sector financing a success.

Future research to explore the dynamics of possible Microfinance regulations that would formalize Microcredit operations in Ghana would be important

# BIBLIOGRAPHY

ADB, (2000). Finance for the Poor: Microfinance Development Strategy, Asian Development Bank, Retrieved from http://www.adb.org/Documents/Policies/ Micro finance/ financepolicy.pdf.

Allen, H. (2007). Finance Begins with Savings, Not Loans," in *what's wrong with microfinance?* Ed. by Thomas Dichter and Malcolm Harper, 49-59 (Rugby, UK: Intermediate Technology Publications, 2007).

Arch, G. (2005). Microfinance and Development: Risk and Return from a Policy Outcome Perspective, Journal of Banking Regulation, Volume 6 Number 3.

Armendáriz de A., and Beatriz, M. J. (2005). *The Economics of Microfinance*. MIT Press: Cambridge MA.

Asiama, J. P., & Osei, V. (2007). Microfinance in Ghana: An Overview. Bank of Ghana. Economics Web Institute.

Barr, M. S. (2005). *Microfinance and Financial Development.* The John M. Olin *Centre for Law & Economics Working Paper Series*, University of Michigan Law School.

Bastelaer, T. (2000). *Reform of Legal and Regulatory Framework for Microfinance*, IRIS Center.

Berger, M. and Buvinic, M. eds (1989). *Women's Ventures: assistance to the informal sector in Latin America*. West Hartford, Connecticut: Kumarian Press, Inc.

Charmes, J. (1992). *The informal Sector Revisited: A Critical Review of Concepts, Definitions and Research on Informal Sector,* Paris, OECD.

Cons, J., and Kasia, P. (2008). The Limits of Microcredit—A Bangladeshi Case, *Food First Backgrounder* (Institute for Food and Development Policy), Winter 2008, volume 14, number 4.

Geoffrey, W., and Sharif, I (1997). Introduction," in *Who Needs Credit? Poverty and Finance.* Dhaka: The University Press Limited.

Ghate, P. (1992). Informal Finance: *Some Findings from Asia. Hong Kong:* Oxford University Press (for the Asian Development Bank).

Greene, J. and Gangemi, J. (2006). Taking Tiny Loans to the Next Level. *Business Week*, New York. 27 November.

Hossain, F. (2002). Small Loans, Big Claims. *Foreign Policy* 12, 79-82.

Hulme, D., and Mosley, P. (1996). Finance against Poverty. Volumes 1 and 2, London: Routledge.

Johnson, K. (June 1999). Small Enterprise Development. Vol.10, No. 3 (PP 5-15)

Karim, R. and Mitsue, O. (1998). Dropping out: An Emerging Factor in the Success of Microcredit-Based Poverty Alleviation Programs. *The Developing Economies*, XXXVI-3, 257-88.

Khandker, S. R. (1998). *Fighting Poverty with Microcredit: Experience in Bangladesh, Daka, Bangladesh.*

Ledgerwood, J. (1999), Microfinance Handbook: *Sustainable Banking with the Poor, the World Bank, Washington, D.C*

.

Meyer, R. L., Nagarajan, G. (2006). Microfinance in Developing Countries: Accomplishments, Debates, and Future Directions. *Agricultural Finance Review* Vol. 66, No. 2, Special Issue, 167-193

Mosley, P. (2001). Microfinance and Poverty in Bolivia, *Journal of Development Studies*, 37 (4), 101-132.

Olujide, M. G. (1999). Activities of selected non-governmental organizations in rural development in South West Nigeria (PhD. Thesis), Department Of Agricultural Extension and Rural Development, University Of Ibadan, Ibadan, pp. 104-110.

Rahman, A. (1998). Micro-Credit Initiatives for Equitable and Sustainable Development: Who Pays? *World Development*, Vol. 27, No. 1, pp. 67-82.

Ray, D. (1998). *Development Economics.* Princeton University Press: Princeton

Robinson, M. S. (2001). *The Microfinance Revolution: Sustainable Finance for the Poor*. The World Bank, Washington, D.C.

Rogaly, B. (1996). Micro-finance Evangelism, 'Destitute Women', and the Hard Selling of a New Anti-Poverty Formula. *Development in Practice* 6, no. 2: 100-112.

Sharif, I. (1997). Poverty and Finance in Bangladesh: A New Policy Agenda," in *Who Needs Credit? Poverty and Finance in Bangladesh*, ed. by Geoffrey Wood and Iffath Sharif. 61-81 (Dhaka: The University Press Limited,).

Sapovadia, V. K. (2006). Micro Finance: The Pillars of a Tool to Socio-Economic Development. Development Gateway, 2006.

Sethuraman, S.V. (1997). *Urban Poverty and the Informal Sector: A Critical Assessment of Current Strategies.* Geneva: International Labour Organization.

URT, (2000). *National Micro Finance Policy*, Ministry of Finance, Dar es Salaam.

Webster, L., and Peter, F. (Ed.) (1996). The Informal sector and Microfinance Institutions in West Africa, World Bank Regional and Sectoral Studies, Washington.

Wikipedia (2010). Microcredit. en.wikipedia.org/wiki/Microcredit

## APPENDIX

## SAMPLE QUESTIONNAIRE ON CHALLENGES OF ACCESSING MICROFINANCE IN THE INFORMAL SECTOR

**Introduction:** The main purpose of this questionnaire is to gather relevant information to enhance our analysis and understanding of how micro credit can be made accessible to the informal sector operators and how the challenges can be overcome. Please be assured that the information you will provide will be treated with the strictest confidence and anonymity.



### A. BIOGRAPHIC DATA

1. Type of business entity..........................................................................................

2. What is your gender?
   - ☐ Male
   - ☐ Female

3. What is your age?
   - ☐ 18-25
   - ☐ 26-35
   - ☐ 36-43
   - ☐ 44 and above

4. Highest level of education *
   - ☐ Primary/JSS
   - ☐ SSS/Vocational
   - ☐ O/A-Level
   - ☐ First Degree

- ☐ Masters Degree
- ☐ Professional Qualification
- ☐ Others

5. What is your marital status?
   - ☐ Married
   - ☐ Single
   - ☐ Divorced
   - ☐ Separated
   - ☐ Widowed

6. Number of children? ............................

7. What is the source of your initial capital?
   - ☐ Personal Savings
   - ☐ Friends and relatives
   - ☐ Loan from MFIs
   - ☐ Others

8. Have you accessed credit facility from any financial institution before?
   - ☐ Yes
   - ☐ No

9. If yes, which institution? ...............................................................................

10. What were your reasons for borrowing?
    - ☐ Start new business
    - ☐ Business expansion
    - ☐ Personal/family
    - Others (indicate)....................

11. How much did you borrow? ...........................................................................

12. What did you use as means of collateral in order to get the loan? .....................

13. How long did it take to receive the loan? .....................................................

14. What is the length of the loan?

- ☐ Three months
- ☐ Six months
- ☐One year
- Others.............................................

15. What is the repayment term?

- ☐ Monthly
- ☐ Bi-monthly
- ☐ Weekly
- ☐ Bi-yearly

16. Are you on time with your loan payments or have you ever had difficulty making a payment?

- ☐ Yes
- ☐ No

17. If yes, what was the difficulty? ...................................................................

18. If so, what action did the lender take because of your late payment?

.......................................................................................................................

B. **SOCIO-ECONOMIC IMPACT OF MICROCREDIT ON INFORMAL SECTOR OPERATORS**

19 What have been the economic impacts of the micro credit on your life since accessing it?

- ☐ Economic impact
- ☐ Employment

- ☐ Ability to pay for other service like Rent, Telephone, electricity etc.
- ☐ Social impact

20. To what extent has the microcredit affected your business and household?

- ☐ To a very large extent
- ☐ Not much impact
- ☐ To some extent

21. What was your output after accessing the microcredit?

- ☐ Profit
- ☐ Loss

22. How much profit/loss did you make? ..........................................................

23. If you make a profit, what did you intend to use the profit for:

- In the short term? ...........................................................................

  ...............................................................................................

- In the long term? ............................................................................

  ...............................................................................................

24. If you make a loss, how were you able to recover the loss and payback the loan

- ☐ Remittances
- ☐ Request for recapitalisation from same institution
- ☐ Request for recapitalisation from another institution
- ☐ No idea

**C. LEVEL OF SATISFACTION OF ACCESS TO AND THE ACQUISITION OF MICRO CREDIT**

25. What is your assessment on the following?

Interest rate:

- ☐ Moderate

- ☐ High
- ☐ low

Procedure for accessing loan:

- ☐ cumbersome
- ☐ Simple
- ☐ Normal

Availability Incentives for repayment of microcredit:

- ☐ yes
- ☐ No

26. Overall, are you satisfied with the microcredit scheme?

- ☐ Yes
- ☐ No

27. How?..........................................................................................................................

## D. CHALLENGES OF ACCESS TO MICROCREDIT

28 Rank the following challenges according to how they affected you negatively in your pursuit of access to credit? Rank the **most pressing** challenge as **7** and the least as **1. Do not use any rank twice.**

| **Challenges** | **Rank** |
|---|---|
| Lack of specific policy guidelines and goals from the micro finance institutions toward the informal sector operators. | |
| Inadequate credit funds and growing demands of credit | |
| Unfavourable collateral security demands from the micro finance institutions | |
| Unfavourable eligibility criteria | |
| Low loan size and unfavourable repayment terms | |
| Cost of access to credit source due to time and money | |

29 What are your final comments?..................................................................................

..........................................................................................................................

*Thank you for your cooperation.*