

**The Rural and Microfinance
Sector in Tanzania: Capacity
Building Initiatives
Report RF-97/264**

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Scope:

The report highlights capacity building initiatives aiming to strengthen the microfinance sector in Tanzania. It is emphasized that a co-ordinated approach from GoT and donors is necessary if the microfinance sector in Tanzania should flourish. It is recommended to introduce a more demand-driven strategy for support to capacity providers and microfinance institutions.

Key-words:

Microfinance, Tanzania, Capacity building, Multidonor mission

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The Rural and Microfinance Sector in Tanzania: Capacity Building Initiatives

**Report of Sub-task 8 of the Rural and Microfinance Mission to
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List of Abbreviations

BAFIA	- Banks and Financial Institutions Act
BOT	- Bank of Tanzania
CC	- Co-operative College Moshi
CGAP	- Consultative Group on Aid to the Poorest
CRDB (1996) Ltd.	- CRDB (1996) Ltd – recently privatised bank.
DFID (UK)	- Department for International Development
ESAMI	- Eastern and Southern Africa Management Institute
EU	European Union
GOT	- Government of Tanzania
IFAD	- International Fund for Agricultural Development
KCB	- Kilimanjaro Cooperative Bank
KNCU	- Kilimanjaro Cooperative Union
K-REP	- Kenya Regional Enterprise Programme
MFI	- Microfinance Institution
MIS	- Management Information System
NBC	- National Bank of Commerce
NGO	- Non Government Organisation
NIGP	- National Income Generating Programme
NORAD	- Norwegian Agency for Development
OICT	- Opportunities Industrialization Centre of Tanzania
REDI	- Regional Enterprise Development Institute
SACCOS	- Savings and Credit Co-operative Society(ies)
SNV	- Netherlands Development Agency
TEAS	- Tanzania Enterprise Award Scheme
UCP	- Umbrella Credit Project
UK	- United Kingdom
VUASU	- Vuasuu Cooperative Union

Summary and Recommendations

Capacity building is the institutionalisation of the skills, tools and attitudes necessary to build a viable rural and microfinance sub-sector. There are four levels of demand for enhanced capacity:

Superstructure:	GoT, donors, supervisory system
Intermediate 1:	Capacity building service providers
Intermediate 2	All MFIs - differentiated by scale and viability into 2 or 3 tiers
Final:	Low income Tanzanians and their enterprises.

The report focuses on the creation of a generic and responsive (if not strictly demand-driven) system for handling capacity building initiatives within the microfinance sub-sector. This explicitly excludes initiatives in micro-enterprise development, i.e. for the purposes of this mission, final demand is identified as MFIs, rather than their customers.

K-REP's proposals are projects rather than a strategy and concentrates on training. We need to move away from a one-dimensional reliance on formal training of individuals outside their working environment, to an organisational learning focus. The sub-sector is already growing and a few institutions are capable of providing capacity building services to MFIs, though the number is small, outreach limited and serious capacity shortfalls are present at every level.

Skills and tools required include: a knowledge of international best practice; well-documented and consistent operations procedures; management information systems (including accounting, loan tracking and generation of financial and outreach indicators); marketing of services; pricing policy to ensure profitable sustainability; planning for growth and product diversification; ability by decision makers to interpret financial statements; personnel management, communication and networking skills.

Capacity shortfalls vary in MFIs, correlated more with the size of institutions than with their legal status. Basic knowledge in accountancy for financial institutions and financial management is a particularly severe constraint to entry and the development of viable operations. To invest in capacity building in many small institutions, however, is a long term undertaking with uncertain outcome. There is an important policy choice between picking a few winners and offering support to a wide array of potential players, much of which would probably be wasted.

For the bigger, established, MFIs the most immediate capacity issues are their legal status as deposit takers (the supervision question) and the question of ownership. These need careful and informed debate. At the national level, the challenge is whether and how NMB will acquire the capacity to design and execute viable lending products.

Capacity building services should deploy a variety of methods, including exchange of experience, twinning, networking, technical assistance, hardware, study tours, exhibitions, pilot programs, facilitation of in-house workshops, R&D of new systems and products, as well as more conventional techniques such as short courses, materials and curricula development, part time classroom and on-the-job training. Initiatives must aim to achieve an optimal mix of these inputs, designed according to context, needs assessment and absorptive capacity in the client institution.

Linkages among different institutions in the sub-sector are weak. We need to strengthen linkages among MFIs; between MFIs and service providers; between MFIs and other financial and business institutions; and between service providers. The output would be a more extensive exchange of information and experience, and a rapid dissemination of "best practice".

Although the need for intervention is obvious, *effective* demand (market-driven) for capacity building services is difficult to gauge and, under present circumstances, probably very limited. Most MFIs, accustomed to the traditions of public-sector support (supply-led), simply lack the ability to pay. Or think they do. But if we are to adopt the principle of full cost recovery for MFIs' clients, we should also seek, in the cause of sustainability, to apply this to the institutions themselves

Transformation will be gradual. Methods to promote competition between suppliers include tenders, award schemes and vouchers. Of these, vouchers are the most obvious technique available for giving consumers (ie. MFIs) the purchasing power necessary to drive an emerging market. However, Tanzania's experience of vouchers in re-training retrenched civil servants has been disappointing and, in the absence of a regulatory framework, there will be some difficulty in deciding which MFIs should be eligible and for how much. Vouchers should be introduced cautiously (first, through pilots) but with the firm intent of moving away from free, targeted assistance.

In principle, the availability of support should be advertised and responses evaluated. Criteria for support might include: track record; financial statements; quality of proposal - including the degree to which applicants have identified their own needs and solutions; existing and proposed strategies to integrate gender and equity considerations and proposed degree of cost sharing. No support should be offered without the beneficiary sharing some proportion of the cost, to be determined on a case by case basis.

Above all, we need some rules of the game for this infant industry. The main players, in this sense, are government and the donors. There is no doubt that, in the past, public sector interventions have tended to undermine healthy credit discipline among both lenders and borrowers, as well as ignoring savings. Such market distortions (sometimes called 'contamination' or 'pollution'), may arise from capacity building initiatives as well as from lines of credit and revolving funds. If we are to avoid this, government and donors need to reach a common understanding of what constitutes 'best practice'. Indeed, this is the purpose of the mission.

Proposed Guidelines

- Support initiatives to disseminate information about successful approaches to commercially sustainable microfinance ('best practice') at **all** levels.
- Support development of a range of institutions capable of building capacity in MFIs, and enable them to compete with each other in providing services. Providers should aim to offer capacity building inputs for fees which cover costs (at a minimum). Initial support to providers should be based on grants for development of appropriate products and phased progress to full cost recovery in the delivery of services.
- An MFI seeking to enhance its capacity (or capability) should have choice between suppliers of services. Selection of providers should be transparent and market based. Indicators of success in reaching this goal, which measure the extent of public subsidy, should be defined in advance of implementation.
- Wherever possible, funds for capacity building should be placed in the hands of the client MFI, rather than the provider. A voucher scheme is the most obvious way of doing this but operational problems should be approached cautiously. A responsive awards scheme which puts much of the onus of identifying and evaluating capacity building inputs on the consumer would have the same effect.
- There should be significant input from practitioners from institutions which embody best practices in the development of capacity building methods and materials.
- Support for capacity building should be based on a commitment by the client to improve performance. Costs of capacity building for a MFI should be related to projected improvements in performance within a determined length of time.
- Hiring criteria in MFIs receiving support should be transparent and merit based, including recruiting personnel with experience in commercial and consumer finance, as well as with a commitment to community and micro-enterprise development.
- Support the identification and regular reassessment of potential service suppliers. Establish a transparent system for monitoring and evaluation of quality of provision, including easy access to main findings for Government, donors and other providers.
- Invite service providers to make proposals for enhancing their in-house capacity to design and implement services to MFIs, focusing on their customers' most immediate capacity needs. Agree on criteria for evaluation of proposals and performance.
- Support initiatives to exchange experience and know-how among MFIs. This could lead to a common interest in the establishment of a microfinance association.

1 Introduction

1.1 Background

Since 1986, the World Bank has supported the Bank of Tanzania (BoT) in its financial sector reforms. This co-operation has now been extended to improvement of rural and microfinance services in Tanzania. Other donors in Tanzania have also been actively involved in the sector in a variety of ways. Interest in development of this sub-sector has increased significantly, because of the success of the 'new world of micro enterprise finance' in other developing countries. A new approach has emerged, focusing on business-like and sustainable microfinance institutions (MFIs), only providing financial services to lower income households and enterprises ¹.

The Bank of Tanzania, the World Bank & other donors have initiated a mission to:

- develop a consensus among all interested stakeholders on the goals and objectives for any intervention aimed at supporting the development of rural/microfinance facilities,
- identify key areas requiring support, and
- identify further preparatory work required to justify investment in the sector.

1.2 Objectives and terms of reference

The mission has been organised in 11 sub-teams, each responsible for assessing different topics. This report reflects the work of the sub-team dealing with *capacity building initiatives* within the sector. The objective has been to "*review and assess the strategies proposed for enhancing the capacity of institutions working in the area of the rural and microfinance including financial intermediaries, supervisors and others.*" The team should pay a special attention to:

- The range and appropriateness of different capacity building inputs available within Tanzania.
- The optimal mix of capacity building inputs needed.
- The linkages between different institutions involved.

¹ Microfinance institutions (MFIs) are specialised organisations providing financial services to poor people who have not been able to access existing commercial banks. They can provide savings facilities, loans and other financial services. Loans are small (less than TSh 1 million), and normally do not require collateral. In Tanzania, the relevant institutions are SACCOs, village banks (as, and if, these emerge), national and international NGOs, and the new National Microfinance Bank Ltd.

- The development of mechanisms to create a competitive and dynamic market for capacity building inputs and the creation of healthy incentive framework whereby good performance is rewarded with additional inputs.

The report is based on

- the research and preliminary proposals made by K-REP and other sources,
- presentations and discussions in the dissemination workshop in Dar-es-Salaam: "Rural and Microfinance in Tanzania" (September 9-11, 1997),
- interviews with relevant institutions (listed in appendix 1), and extensive discussions both within the team and with other sub-teams in the mission.

1.3 Capacity building and best practice:

Capacity building is understood as *the institutionalisation of the skills, tools and attitudes necessary to build a viable rural and microfinance sub-sector*. This draws attention to capacity building needs across the whole sub-sector. We can distinguish four main levels of demand for enhanced capacity:

- Super-structure: GoT and funding agencies, supervisory system
- Intermediate 1: Service providers
- Intermediate 2: MFIs and their staff
- Final: Low-income Tanzanians.

Although micro enterprises are the end users of financial services provided by the sub-sector, this report focuses on the creation of capacity building processes within MFIs and service providers. In the context of a financial sub-sector program framework, we take final demand for capacity enhancement to be the MFI level. The mission leaders have made it explicitly clear that this is not an MSE development program (though the mission has adopted the 'enabling environment' set of arguments).

In order to ensure that capacity building efforts lead to efficient and effective performance, the benchmark of "best practice" is often referred to. This is an elusive and inexact term. To avoid reducing "best practice" to an empty and slippery phrase, it is understood as *any practical set-up and methodology which has proven to provide microfinance services with a high degree of self sustainability*. This implies that any MFI aiming to match best practice should have the clear objective of becoming self sustaining with respect to financial, skills and equipment resources within a limited period of time.

2 Some Comments upon the K-REP Work

The leading Kenyan MFI, K-REP, was contracted by BoT to undertake a series of studies on the rural financial sector in Tanzania. These studies, and the discussions they generated in the preparatory workshop, served as the point of departure for this mission.² They document virtually unlimited demand for microfinance services in Tanzania, although the exact figures are difficult to verify.

K-REP's survey and analysis of institutions capable of providing training, technical assistance and business services to the microfinance sector, offers an analysis of 6 (out of 7) educational institutions and 5 training institutions (among them 3 NGOs). Data was also collected in some 31 MFIs analysing the current capacities in the Tanzanian microfinance sub-sector. The most important conclusions are:

- The lack of institutional capacity among bank units and SACCOs is the most serious constraint. Only six in the K-REP sample of 31 institutions have a senior/middle level manager with any specific orientation/training on rural/microfinance services. Most of those with such skills are found among the NGOs in the sample.
- The most immediate training needs for the various categories of MFIs' staff were identified to be a community development approach for promotional activities, credit management, business plan preparation, loan appraisal, financial management, monitoring, evaluation and reporting, fiscal policies etc. Most topics are characterised as "very weak areas" in the majority of the MFIs.
- Although no formal educational institution is currently providing training in microfinance, they offer training in basic and/or related subjects. At present, only two or three international NGOs are set up to meet microfinance training needs (the quality of their training was not assessed). Educational institutions need to enhance and re-orient their activities in order to be suitable suppliers.
- Priority should be given to ex-bank staff and SACCOs staff rather than "project" based financial institutions.

² K-REP produced 3 reports and 7 proposals for further work in the sector. The most relevant reports concerning capacity building initiatives are as follows: (1): Wangwe, S.M. and Lwoga, C.M.F: "*Survey and Analysis of the Educational Institutions, NGOs and Private Companies Which can provide Training, Technical Assistance and Business Services to the Microfinance Sector*". (2): Oketch, H.O and Ndulu, J.K and Nyagetera, B.M: "*Survey and Analysis of Rural/microfinance Financial Institutions in Tanzania*". (3): Lwoga, C.M.F: "*Proposal for a Capacity Building Program for Management Teams of Rural/Microfinance Institutions*" and (4): K-REP: "*Proposal for Development and Promotion of Savings and Credit Co-operative (SACCO)*". All three reports issued by K-REP Dar-es-Salaam/Nairobi 20. August 1997.

The information gathered in the surveys has then been used to develop proposals for capacity building for management teams in MFIs, and in the development of SACCOs³. The proposals offer some detailed principles and strategies for implementing training programs, content of proposed training activities and cost estimates. They include detailed information about institutions, including considerations about main contents of training courses and the corresponding inputs required. The proposals also provide models and projects for further intervention which could be considered

The main strategy identified by K-REP is training, the conventional focus for capacity building in development projects. Historical results are mixed and training (especially formalised training courses) should only be regarded as one of several methodologies and options in future capacity building initiatives. Training is usually provided to individuals and, though the need for basic skills will remain the starting point, there is no straightforward correlation between individual training and organisational development.

In order to encourage an organisational learning process whereby MFIs can continuously improve performance, incentive structures are needed, both on the individual and organisational level, to encourage MFIs to develop and institutionalise skills, tools and attitudes. Similarly, incentive structures are needed to encourage Tanzanian and international service suppliers to develop products appropriate to the needs of the sub-sector. Mechanisms to implement such incentive structures should be a main focus for government and donor interventions.

A common approach has been to contract a single institution and to provide all necessary funds and technical assistance. In some cases this remains a reasonable strategy but it tends to create problems. The institution may acquire a monopoly where its main objective is transformed from customer satisfaction to donor satisfaction, creating a dependency which is unsustainable. We need a set of institutions able to enhance their customers' capabilities without a constant inflow of new external resources.

The team is not in a position to contest K-REP's empirical findings. Their capacity building proposals offer, however, appear to be projects rather than comprehensive strategies for creating *a dynamic system of capacity building initiatives*. A co-ordinated government and donor intervention policy to enhance capacity building in MFIs should be focused on initiatives which can strengthen organisational learning processes in MFIs and within the suppliers of capacity building inputs. It should also have the ambition to create a dynamic system of competitors where different means and institutions should be engaged to implement capacity building initiatives.

The team does not agree with K-REP's proposal to create, top-down, an apex organisation to coordinate and allocate equity capital. Until a consensus for the need for

³ In fact, all proposals touch, and often rely heavily, upon the problems of capacity building, although some proposals only regard capacity building as a precondition for implementation.

such an institution emerges amongst practitioners, followed by an initiative to create it, it is likely that any such intervention would be seen as just another donor project, essentially impermanent and sometimes in conflict with its constituents. UCP seems to have some of these problems.

3 Some ongoing Microfinance and Related Initiatives in Tanzania

Microfinance interventions and institutions have been around in Tanzania for a long time now. Their degree of effectiveness in meeting the needs of the rural poor communities has, however, mostly fallen below the desired level. During the course of the Mission, the team had the opportunity to acquaint itself with some of the ongoing initiatives relating to the development of the microfinance sector. A brief overview of some of these initiatives is given here, to put the analysis in context. More detailed descriptions and discussions are given in other relevant mission reports.

The following issues are summarised: present capacity, capacity building needs and the potential role in sector intervention.

3.1 The Superstructure Level: GoT and funding agencies, supervisory system

3.1.1 Donor funded projects

Different donors are currently supporting (at least) between 20 and 30 microfinance initiatives in Tanzania.⁴ They vary in terms of size, quality and implementing institution. Most initiatives are channelled through NGOs. Results are mixed, and efforts are not co-ordinated.⁵ Their capacity to learn from former experience and ongoing projects supported by other donors, is apparently limited.

3.1.2 GoT: The National Microfinance Bank

The National Bank of Commerce, hitherto the largest commercial bank, has been reconstituted into a commercial bank NBC (1997) with 35 branches covering every region of Tanzania; and a microfinance bank, NMB, with approximately 100 branches across Tanzania. To begin with the NMB will offer savings and deposits and limited payments services. Microfinance lending will be built up progressively thereafter. All planned branches should be opened by mid November this year.

Present capability: For the immediate future, limited to savings and money transfer. Ex-NBC staff should have considerable financial skills but doubts as to moral hazard are widespread.

4 See Kobb,D and Sizya,M,J: "A survey into credit and savings in Tanzania", for HIVOS, DSM 1995

5 Kobb and Sizya estimate an overall average repayment rate in donor supported microfinance programs of about 60 percent (1994/95). They also note that rates decrease over time. This is usual (and unsustainable).

Capacity building needs: Commitment to community/MSE development and micro-finance skills. Re-orientation of organisational culture and range of products.

Potential role in sector intervention: As the only remaining formal sector presence in many rural areas, NMB obviously has an enormous potential role.

Other national initiatives

As far as the team is aware, there are no ongoing capacity building initiatives within the supervision system directed towards microfinance systems. The need for this is discussed by sub-task 4.

3.2 Intermediate level 1: Service providers

3.2.1 Service providers in Tanzania

K-REP's report indicates the potential capacity of some of the existing training institutions to contribute to the human resource development needs of the MSE sector in general and microfinance institutions in particular. Existing capacity is limited in quantity and in quality.

Present capability: Many institutions are able to offer accountancy and management skills. Specific microfinance capability confined to in-house training wings of international NGOs (REDI & OICT). Cooperative College offers financial management skills to SACCOs, but lacks capability in contemporary microfinance best practice.

Capacity building needs: Wider access to knowledge and experience of best practice in microfinance. Resources to take training out of the classroom and into the field.

Potential role in sector intervention: Vital: these are key service providers which, together with technical assistance, exchange etc. (see section 4), will actually deliver capacity building.

The capability status of the main relevant training institutions visited during the mission is described below.

3.2.2 Opportunities Industrialization Centers of Tanzania (OICT)

OICT is the Tanzanian affiliate of Opportunities Industrialization Centers International Inc., an American international NGO initially formed to train young African Americans for self employment in the USA. OICI/OICT are mandated to implement the Income Generating Skills Development Programme in the NIGP.

OICT offers training to start-up entrepreneurs in the skills of starting an enterprise and operating it profitably. OICT has trained some credit officers for PRIDE Tanzania, as well as staff of various NGOs on the basics of Savings and Credit activities.

The Executive Director has extensive experience with microfinance having been trained at the Grameen Bank in Bangladesh. He has helped set up the model for microfinance being used in the Presidential Trust Fund operating in Morogoro.

While the core staff is very small, a pool of associate consultants has been identified who can be called upon to as needed. OICI provides backup whenever need arises.

3.2.3 Regional Enterprise Development Institute (REDI)

This is a PRIDE Africa subsidiary set up to meet the training and human development needs of PRIDE Tanzania and its equivalents elsewhere in the region (eg. Uganda) as well as other Tanzanian and regional MFIs. Services are offered on a fee basis. REDI programmes in the main address the institutional development needs of financial service organisations in planning, managing and financing. Its main training package is based on the standard PRIDE model, but its prospectus offers:

- Micro enterprise finance development: 6 modules/courses
- Enterprise development: 9 modules/courses
- Human resource management: 17 modules/courses
- Financial management: 3 modules/courses
- Secretarial & front-line staff development: 8 modules/courses

These can apparently be adapted/tailored to the requirements of other institutions. Recently REDI has organised courses designed by CGAP focused on Board members of microfinance institutions and others in leadership positions in the MFIs.

The staff strength of REDI is small, but a network of resource persons and facilitators is available where need arises. Physical resources are limited.

3.2.4 East and Southern Africa Management Institute (ESAMI)

ESAMI's 1998 program includes three courses on different aspects of microfinance. These are said to have been requested by Government ministries and some of the banks.

ESAMI's mandate is to support institutions in member countries to build the capacity to design and organise courses. While ESAMI's human resources and facilities enable it to offer training in microfinance to practitioners, a better use of the resource might be to design courses at a higher level for directors and policy makers.

3.2.5 The Co-operative College

The CC is the only institution of higher learning which has conducted training for SACCOs from as early as 1966. CC has ample physical capacity at its Moshi campus as well as its Regional Wings. Dodoma Wing manages a credit revolving fund, supported by the Canada Fund. CC has experienced professional staff in accounting, management, marketing, law, economics, sociology and cooperative enterprise management.

As noted by K-REP, CC has not yet conducted training on microfinance, *per se.*, but has expressed the need to enhance its own capacity in this new discipline.

3.2.6 Private companies and consultants

The team has not looked at the private companies and individual consultants claiming to offer capacity building in microfinance. K-REP offers no analysis of these companies either. However, it is probably safe to say that the private sector includes a number of organisations capable of providing TA and other inputs, both to indigenous service providers and MFIs themselves. The quality of their products and organisational capacity must vary, and should be evaluated before they are contracted.

3.3 Intermediate level 1 and 2: NGOs in micro enterprise development

3.3.1 NGOs as service providers and MFIs

The very term NGO is a constraint to understanding the sub-sector. The range, in scale and competence, that it covers is so wide that, at the extremes of PRIDE and tiny, poorly equipped charitable organisations, the only factor in common is the use of the word 'credit', which is made to cover substantially different activities.

International and local NGOs are very actively involved in the promotion of micro enterprises as a major component of their poverty alleviation programmes. To meet the demand for credit of their target beneficiaries, NGOs have focused on the provision of microfinance services. Most NGOs involved in community and micro enterprise development (e.g. training, linkage creation, etc.) tend sooner or later embark on microfinance deliveries if they - or a donor - can afford it.⁶ It is not clear if a definitive inventory of the number of primarily financial NGOs exists⁷. Nor that it is always a simple task to distinguish between 'financial' NGOs (ones that only offer financial services) and those which include 'credit' as a means to other ends.

Present capacity: Extremely variable. Two or three are among the best performers in the sub-sector. Many others are of such limited capability that measures are needed to exclude them. In between are perhaps (at most) a dozen with potential for growth, though they lack the necessary skills in financial management and organisation systems.

Capacity needs: Impossible to generalise, due to high variance. Can only be approached on a case by case basis.

Potential role in sector intervention: The best performers have a crucial role in disseminating best practice and undertaking product and systems development. Nevertheless they have yet to prove their own viability, being very substantially dependant on donor support. The worst performers continue to contaminate the market by offering unsustainable services.

⁶ The logic of the process which draws NGOs into microfinance is not discussed here.

⁷ Malima, R. "Experience in Microfinance Initiatives" (Tanzanian Bankers Journal, June 1997) estimates 18 'financial' NGOs. The draft report of subtask 7 of this mission mentions 34.

Three NGO operated microfinance programs were visited.

3.3.2 PRIDE Tanzania

PRIDE Tanzania Ltd is both an NGO and a company limited by guarantee (est. 1993); the latter status is necessary because NGOs lack legal personality. It carries on microfinance business under the general guidance of a Board of Directors appointed by its trustees (or guarantors). Administrative and management support is provided by PRIDE Africa, a pan territorial NGO based in Nairobi.

PRIDE Tanzania is funded principally by NORAD⁸, which has supplied most of its start-up capital. This grant is administered as part of bilateral collaboration of Norway with the Government of Tanzania, funds being disbursed through BOT's Financial Markets department.

PRIDE Tanzania follows a Grameen-model lending programme. Groups of prospective borrowers undergo intensive orientation to introduce the highly simplified and standardised procedure designed to inculcate the necessary discipline in credit management. In addition an elaborate loan tracker system using specialised computer software has been developed by PRIDE Africa to support operations. This has yet to interface with the institution's accounting software.

The first two years were used as a pilot period when only three branches were opened. Presently 13 branches are operational in 10 regional towns of Tanzania. A total of 20,000 loans have been disbursed amounting to USD 1.5 mill. No loan defaults have been experienced and 10 branches are scheduled to open by the end of the year.

PRIDE Tanzania and PRIDE Africa are aware of the constraints of the model particularly with regard to the status of the Loan Insurance Fund and plans are underway to refine the model to the added advantage of the borrowers. Consideration is already being given to the possibility of transforming PRIDE Tanzania into a Bank. This transition from a NGO to a bank, entails important issues of ownership which should be of general interest.

Based on its track record to date PRIDE Tanzania stands out as an example of best practice in Tanzania. Nevertheless, its highly structured group lending techniques should not be taken as the only model for successful microfinance. PRIDE's track record is limited in time, and experiences in the years to come will be of great value.

3.3.3 MEDA

The Mennonite Economic Development Associates(MEDA) is an international NGO which is the implementing agent of The Umbrella Credit Project (UCP) for Micro-enterprise Credit Development. UCP operates within the general framework of the National Income Generation Programme (NIGP).

⁸ NORAD also supports REDI, as well as PRIDE Uganda, which is similar in scale.

UCP is a two phased, five year project whose objective is to support the expansion of micro enterprise credit in Tanzania. It is a capacity building intervention to enable microfinance institutions to increase the volume of credit availability and the quality of the services given. It has been operational since 1995 and its services have been accessed by only few MFIs.

3.3.4 NGOs in cooperation with Banks: CRDB (1996) Ltd, Juhudi Credit Scheme

CRDB (1996) Ltd, with support and funding from FAIDA, has designed a new microfinance facility called the Juhudi Credit Scheme. FAIDA is an NGO whose activities are limited to Arusha Region and is engaged in small enterprise development activities; it is not a financial NGO, preferring to interface with the financial sector. It is funded by the Netherlands Government through SNV. Juhudi will focus on meeting the credit needs of small scale entrepreneurs operating at the level above, say, PRIDE clients (the “missing middle”). The actual financial instrument appears to be problematic, with the prospect of further pollution, due to perception of the loan as being backed by the NGO.

3.4 Intermediate level 2: MFIs and their staff

3.4.1 Savings and Credit Co-operative Societies (SACCOS)

These are by far the most widely established microfinance institutions in Tanzania, numbering approximately 1,000, and a country-wide spread covering all except one of mainland Tanzania’s regions. SACCOS have grown and spread through government promotion, supported by donor programmes and organisations.

Present capacity: Highly variable. Their main strength is their grass root basis. A very few offer both savings and loans. Most are primarily savings institutions. A well defined financial reporting system is in place, though implementation and supervision are incomplete. It is not clear if the present system is adequate to generate all the financial indicators required in best practice, especially with respect to portfolio quality.

Capacity building needs: A review of the present record keeping system to meet best practice and regulatory requirements. SACCOS need to resolve the conflict between the principles of co-operation and high risk/high return microfinance lending. Most of them lack a competence in financial management necessary to act as a viable financial institution. In short, they need to acquire competence and experience in lending.

Potential role in sector intervention: In order to provide the majority of the Tanzanian people with financial services, SACCOS have to play a leading role. As a member owned and led organisation, the SACCOS are crucially involved in equity and participation issues. While there are reported cases of SACCOS which have begun transforming into microfinance institutions (Kindi and Kibosho Central), these appear to be the exception rather than the rule. They illustrate the possibilities and challenges for the dynamics involved in transforming the present SACCOS into viable microfinance

institutions meeting the needs of their members and the community at large. The proposed pilot project by KCB supported by EU, will be an opportunity to test methods for provision of capacity building inputs to SACCOs, and explore questions of replicability.

3.4.2 Kilimanjaro Cooperative Bank (KCB) & other co-op. banks

The Kilimanjaro Cooperative Bank (KCB) is registered as a secondary co-operative society under the Co-operative Societies Act No 15 of 1992 with a membership comprising of 100 Primary Coffee Marketing Co-operative Societies, 70 SACCOs, KNCU and VUASU the two unions all operating in Kilimanjaro Region. KCB is licensed to carry on banking business by BOT as a Regional Bank within the context of the Banking and Financial Institutions Act (BAFIA). Currently, it is the only institution designed according to these principles.

The KCB started operations in 1996 with a capital of Tsh 337 millions. By the time of the Mission's visit this had grown to TSh 405 millions. Each member society is estimated to reach about 1,000 individuals (adults), thus an potential outreach of 170,000 individuals has been attained.

Present capacity: KCB is reported to have reached break-even in the first 15 months of operation. This is admirable. KCB has in-house financial skills, its basic MIS in place. It has the will and commitment to contribute to the development of SACCOs, which could form the basis of a rural branch/agency network.

Capacity building needs: KCB has a limited experience, and a staff bottleneck in middle management. Operational manuals have yet to be prepared. RABOBANK has given technical support, providing the first General Manager, who will be replaced towards the end of this year. It was however emphasised that the Managing Committee of the KCB needs more in depth orientation on banking principles and particularly the management of credit and its contribution to the profitability of the banking business. It has to be underlined that KCB is a co-operative with a difference. It is a Bank above all else and must prove its worth at that front.

Potential role in sector intervention: KCB is actively involved in promoting the formation of other Cooperative Banks in Mwanza and Kagera Regions. In this regard KCB has given advice on feasibility studies and other requirements for banking business licensing. This gesture of good will and solidarity can only be afforded to a certain limit. The bank will soon reach its capacity for such a service. The EU, through its STABEX facility, has given KCB a grant for training members, committees and key staff of SACCOs on the fundamental aspects of credit management. Initially the programme would involve 20 selected SACCOs. This training aims at enabling SACCOs to carry out agricultural input supply credit business to meet the needs of their members.

4 The Need For Capacity Building

4.1 Capacity building and the problem of creating an organisational learning process

Capacity building is the process of institutionalising the skills, tools and attitudes necessary to build a viable rural and microfinance sub-sector.

This definition, which emerged from the workshop, has gone through a number of evolutions. Instead of 'institutionalisation', the word 'internalisation' was used. The concept is the same: A need for more than a one-dimensional reliance on the formal training of individuals, away from their working environment.

Shifting the focus to the internal processes of organisations and institutions is an appealing notion, but the practical solutions to actually doing it remain somewhat elusive, in spite of an array of available techniques. Success is difficult to measure, as much in the Western corporations from which many of these ideas originate, as in the Tanzanian microfinance sub-sector.

The techniques available include: the introduction of staff incentive structures; staff exchanges, secondments and study tours; the provision of management information systems hardware and software as well as the technical assistance necessary to design and install it. The workshop which opened the mission was itself part of the capacity building process and might well be replicated at lower levels. There is a role for capacity building in the civil society and a workshop for parliamentarians has been suggested. All these are in addition to more conventional training and curriculum development, which still have an important place. In the process, we must seek to set up and reinforce linkages between institutions, some features of which are considered in section 5.

Organisational learning is different from individual training.⁹ Organisational learning involves the acquisition and establishment of systems and operational procedures which will continue to work without relying on gifted individual staff members. More than this, it implies acquiring the capacity to uncover problems and failures and intervene in time to cope with the difficulty. To do so, organisations need to have staff with skills appropriate to daily operations, appropriate MIS (it is doubtful if SACCOs and small NGOs really need advanced computer systems), and well-understood and documented procedures. Performance-related incentives have a well established role in engaging staff buy-in and ownership of procedures.

⁹ According to ESAMI, for example, about 50% of Tanzanian attendants on their courses in management and finance over the years came from NBC.

Capacity building should be offered as an incremental process, with opportunities for regular re-assessment of both the form and the content of the support offered. Resources must be set aside to monitor and assess the impact on the organisational procedures and financial performance of client-institutions. These 'loops' are expensive, as they are next to impossible to install without using experienced consultants but, without them, there can be little understanding of effectiveness.

To return to our definition, the initial version adopted in the workshop ended with '..attitudes necessary to run a viable MFI'. This is, of course, incomplete. There are capacity shortfalls at every level in the sub-sector, from client to policy maker, from donor to household. Of all possible linkages, most cross in the work place of the people who actually manage MFIs, whether as employees or as voluntary leaders of SACCOs. While it follows that this should be the primary focus, management training on its own, however well-designed or executed, is not enough. Furthermore, attitudes towards tasks and customers could only to some extent be acquired through training courses.

4.2 Skills and tools

In the workshop 11 specific skills and tools were identified. These are laid out in the matrix on the following page. The skills needs of personnel at different levels in an organisation - board, management, operations staff - are indicated in the matrix. Needs vary according to scale of operations. In a typical Level 1 or 2 SACCO, for instance, decisions on loans are taken by a sub-committee of its 'board' (called committees), where in a larger, Level 3 NGO-type MFI they are the responsibility of operations staff.

The matrix distinguishes only larger (L) or smaller (S) institutions. Small MFIs face more and less the same problems and capacity shortages, whether they are small NGOs or SACCOs. Similarly, bigger institutions face more and less the same capacity shortfalls, independent of their legal status. The explanation is simply that scale determines the complexity in operations and logistics, the need for formalised systems and the division of labour/responsibilities within the organisation.

Everyone in the business needs to have a conception of best practice, though the depth and grasp of detail will vary with their position. From the matrix, it is clear that the primary focus for skills transfer in MFIs themselves is management. The needs of operations staff are evidently simpler, though without clear operations procedures, appropriately documented, no financial institution can work. These conclusions are hardly surprising.

It is clear that there are very serious shortfalls in the related areas of accounting and MIS development. The NGO group estimates that of the 30 + offering financial services of some sort (this number is uncertain), only three or four have meaningful accounts. Of the minority of others - perhaps another six - which are able to present accounts, none of these are either reliable or have grasped the basic (and, to outsiders, counter-intuitive) fact that, for financial institutions, loans are assets and deposits liabilities. This is presumably because the accountants concerned have a background in enterprise accounting. While the co-operative movement does have a simple financial balance sheet system in place, these are widely thought to be unreliable and will probably need to be revised if it is to generate financial indicators such as measures of portfolio quality.

Table 4.1: Capacity building; Skills and tools, institutions and techniques

SKILLS and TOOLS	CAPACITY NEEDS						TECHNIQUES				Exhibitions			
	Boards		Management		Ops. Staff		Training	Exchange	Incentive	Network-ing		TA	Hard-ware	Study Tours
	L	S	L	S	L	S								
<i>General</i>														
1. Best Practice	*	*	*	*	*	*	*	*	*	*			*	
<i>Technical</i>														
2. Operational procedures		*	*	*	*	*	*	*	*	*	*	*		
3. Accounting			*	*	*	*	*	*	*	*	*	*		
4. MIS development			*	*	*	*	*	*	*	*	*	*	*	*
5. Marketing			*	*	*	*	*	*	*	*	*	*		
<i>Strategic</i>														
6. Pricing Policy	*	*	*	*	*	*	*	*	*	*	*	*		
7. Planning	*	*	*	*	*	*	*	*	*	*	*	*		
8. Interpreting financial statements	*	*	*	*	*	*	*	*	*	*	*	*		
<i>Personal</i>														
9. Personnel management		*	*	*	*	*	*	*	*	*	*	*		
10. Communication	*	*	*	*	*	*	*	*	*	*	*	*	*	*
11. Networking	*	*	*	*	*	*	*	*	*	+	*	*		

The deficiency in accounting is important. The sub-sector comprises only a handful of actors able to match one of the most attractive theoretical features of microfinance: that it should be largely self-evaluating. Objectively verifiable indicators of both financial performance and outreach should be generated as a matter of course, without - for most purposes - the need for a special evaluation system.

This observation leads to a question of policy: do future initiatives seek to support the limited number of established MFIs, to reinforce success? Note that international experience suggests that only a few institutions will make the grade as sustainable, viable operations with significant outreach. The alternative is to offer support to as wide a community of potential successes as possible, knowing that most lack the even the basic ability to keep track of their own money, let alone anyone else's.

4.3 Creating a market for capacity building services

'Best practice' includes the principle of full-cost recovery applied to capacity building services. A broad program for the sub-sector should be demand-driven and these ideas are central to the framework principles presented in the work of sub-task 2. These concepts imply both pricing and marketing. Techniques for marketing support are fairly straightforward: programs may be either responsive or targeted at a pre-identified institution, in the old way. A responsive program would rely on informing the market that support is available, under what terms and conditions (including price), and then evaluating the response, before deciding whether to make the 'sale', and provide the service.

The four main sector levels in this 'market' may need different approaches in order to create a market for capacity building.

Superstructure: GoT and the funding agencies

If this mission results in increased flows of assistance to the sub-sector, much of it will pass through a GoT department. The most appropriate institution would seem to be the Financial Markets department of BoT. According to the director, this department lacks the capacity to handle increased flows and the technical skills to evaluate an increased number of proposals. A number of bi-lateral programs will presumably follow their organisations' usual practice of establishing independent funding channels, whether as stand-alone projects or by contracting existing institutions in Tanzania. Given donor commitment to the framework produced by the mission, even bi-laterals will wish to interact with some central point at which information is shared and policy issues aired.

It follows that one of the first actions following the mission will be to design a capacity-enhancing program for this department of BoT. One of the central aims of this should be for the department to acquire the means and authority (intellectual) to resist the tendency of donor funds to distort rural financial markets, by setting clear priorities for the sub-sector.

The principal determinant of demand has, until now, been the availability and accessibility of donor funds, which absolutely dominate the market in new initiatives (and have largely abandoned the older model of the SACCOs). It is donors who create the market, essentially supply-led. There is an obvious need for funding agencies to ensure that their role in the allocation process is properly informed, perhaps by organising a seminar in best practice for Dar es Salaam based staff (few of whom participated directly in the mission), run by a consortium of the Tanzanian service providers.

Superstructure: Supervision

The relevant section of the mission report recommends the creation of a new agency to supervise larger NGO MFIs and SACCOs. If this goes ahead¹⁰, it will create very significant demand for increased capacity in the relevant GoT departments, central and regional. This is not an area in which a pricing mechanism for capacity building services is appropriate, though it must be asked who will bear the cost of supervision.

Intermediate 1: Service providers

This part of the market is small but crucial. Currently, there are few indigenous players with existing capacity. There is a need to strengthen these institutions before they are able to compete (see section 3). We are talking of first enhancing the capacity of the capacity builders. In the nature of a supply-led market, their role is more as 'buyers' of donor support rather than sellers of services. The question is how to reverse this (see section 6.1).

Intermediate 2: MFIs & their staff

This is the main focus of demand for the skills and tools identified in the workshop and shown in the matrix in figure 4.1. It is important to distinguish according to scale. The demands of the proposed regulatory system will differ significantly from level to level. The categories and definitions proposed in the work of sub-task 4 offer an opportunity for a framework on which to structure programs catering to these differing demands.

Final Demand

The extent of effective final demand for financial services is contested (see NGO group report) and important distributional issues are analysed in the work of both the economics and the gender, equity and participation groups. In principle these issues should be addressed indirectly, by internalising them in the strategic planning and product development processes of client institutions. Again, regular re-assessment of the impact of such interventions on the operations of the client is vital. 'The number of staff attending gender sensitisation workshops' is a poor proxy of quality or impact.

10 There are good arguments why we should hesitate before imposing a regulatory structure on an industry so small, barely developed and poorly understood.

4.4 An optimal mix of services

The examples of existing initiatives discussed in section 3 are all supply-led. To be sure there is a growing trend to responsiveness by funding agencies, as in TEAS (see section 6 - award schemes), but to shift immediately to a truly demand-led, full cost-recovery market for knowledge is an extreme challenge. The ability of MFIs - across the range - to pay for services has yet to be tested, as many continue to depend on soft (usually free) donor money. The exception to this is the SACCOs, which are savings-driven.

The prevailing view is that some period of transition from full subsidy to market prices is unavoidable. REDI, for example, is offering a set of one week best practice courses, funded by CGAP. The first round was 75 percent subsidised. The next will be 50 percent subsidised and so on. It remains to be seen what the extent of demand for these courses on a full-cost basis will be.

Across the region there is consensus that the principal risk facing the sub-sector is the probability of excess attention by donors flocking to the latest development fashion. It is all too easy to see how the sub-sector could be contaminated (or, as the French term has it, 'polluted') by MFIs growing too fast, without proper systems in place, leading to a collapse which could set off a domino-effect throughout the sub-sector. Resolute progress towards the principle of full-cost recovery would form an important brake on any tendency to overheat.

A truly competitive market would set an 'optimal mix' of capacity inputs on its own but in this market we lack almost all the conditions of classical equilibrium. Product information is highly imperfect, transparency low and goods are not, and cannot (yet) be priced. The fact is, that until it is tried on a wide enough scale, we cannot know what effective demand would be, though indications are that it would be small. The success of organisations like PRIDE offer no guide, as this has been achieved with grants. These observations also apply to many international examples of best practice.

The team have concluded that the rhetoric of the free market is premature (not to say, contradictory) in this context and that significant progress can only be achieved by continued donor support. What can be included as a guideline is the proposition that, in general, no support should be offered, without the beneficiary - institution or individual - sharing a significant proportion of the cost. The exact size of that proportion would have to be considered on a case by case basis and there are some obvious examples (e.g. third country training) where Tanzanian institutions' ability to contribute will be severely limited. In interventions at the superstructure level (ie. within the public sector), the concept of full cost recovery hardly makes sense. But, given the commitment in principle to a market-driven approach, we have to make a start in introducing a price mechanism and also to consider setting targets for withdrawing subsidy.

5 Linkages

Linkages are the *interaction of different institutions in the sub-sector to their mutual benefit*. At present these are weak and arbitrary.

5.1 Advantages

- Provide opportunities for training and employment
- Improve standards through dissemination of “best practice”
- Exchange experiences
- Support each other where there are shortfalls (e.g. product development)
- Provide opportunities to learn from others in the form of networking, exchange of information, secondments etc.
- Enhance access to supervisory techniques and information searches to avoid duplication of effort.

By their nature, creation and maintenance of linkages are to a large extent informal, and are based on trust, information and transparency. All these areas of interaction and co-operation offer the opportunity to capture economies of scale within the sub-sector. Linkage creation and strengthening should be regarded as one of the most important means of capacity building and yet the scope for intervention is limited by this informality; linkages ‘forced, not forged’ will be weak and impermanent. The role of the public sector, again, is to respond to and complement initiatives from practitioners, on a cost-sharing basis.

5.2 Problems

- Limited resources: most MFIs have limited ability to pay to enhance linkages, and may require external facilitation both for identification of relevant contacts and practical arrangements.
- A self-centred view: each MFI operates according to its own principles. Different MFIs have also to see that they can learn from other institutions.
- Lack of information: exposure to best practice is so low that the process of creating productive linkages has not yet taken off.
- Co-ordination: there is no apex institution. The solution to this is not to impose one, but to trust that as the sub-sector develops, a consensus for the need for one will emerge and that the public sector can stand by, ready to assist.

- Donor domination: donor finance dominates the market. Donor programs, especially those targeting NGOs, account for a large part of the sub-sector and have in the past followed a fragmented and contradictory approach.

5.3 Forging linkages for the future

- Continue the present process of enhancing linkages between different donors and between donors and GOT.
- Forge a regional supervision network in East Africa between local supervisors dealing with the sub-sector.
- Link international and local service providers to increase the level of exposure to best practice.
- Link local service providers. This could be in the form of exchange of methodologies, curricula, data on clients, products offered, etc. The most immediate need is to develop and adapt curricula and methodologies to the Tanzanian context.
- Link local service providers and practitioners. Twin training institutions with practitioners for materials, expertise and course delivery.
- Co-ordinate different microfinance institutions: Share costs, resources, access to international published material (e.g. CGAP, ITDG, EDI. etc.).
- Explore possibilities of sharing information on borrowers in the form of credit bureau so that better clients can access credit more readily.
- Link MFIs to formal financial institutions, e.g. banks, to facilitate the “graduation process”. This is possible if MFIs will be willing to share data of potential borrowers with banks to assist clients who want to borrow amounts above their limits.

5.4 Identification of Strategic areas of Support

Given a co-ordinated approach among Government and donors, the following areas of support to enhance linkages should be addressed:

- Between service providers (including international and national institutions, and practitioners with hands-on experience) to enable them to increase the level of exposure to best practice, including curricula, methodologies and experiences.
- Between service providers and MFIs for dissemination of basic principles and best practices in microfinance, methodologies and experiences.
- Between MFIs to enhance possibilities for continuous flow of information and exchange of resources.

6 Some Elements in a Co-ordinated Strategy for Capacity Building Initiatives

Following K-REP's analysis, we can say that most players in the rural and microfinance sub-sector suffer from capacity shortfalls. Following recent reform, the 'new' sub-sector is in its infant stage and will have to carry the burden of many years of poor performance and practice. Fuelled by political intervention, easy-access money from donors and poorly equipped institutions, the image of "credit" became confused with gifts. If microfinance is to develop and offer sustainable financial services to the majority of Tanzanians, co-ordinated action is needed by actors in the super-structure (i.e. Government and donors) in order to re-establish a sound environment. In this respect, a co-ordinated approach to capacity building initiatives should be given the highest priority.

6.1 Methods to create a demand driven system for capacity building initiatives

Truly *market driven* demand for capacity building initiatives in Tanzania is very limited. Although the need for initiatives is obvious, few indigenous institutions can afford to pay for capacity building inputs based on cost recovery¹¹. In the short term it is doubtful if capacity building initiatives within the sub-sector can derive from market demand alone. Nevertheless, if the objective is to create a dynamic system, a more business-like approach must be embarked upon.

6.1.1 Supplier-led initiatives

We have spoken of the need to build capacity in the capacity builders. It is therefore reasonable to dedicate, or target, some institutions and provide them with initial resources in order to develop their own capacity. Dedication, however, should depend on institutions' potential to enhance a unique competence (e.g. OICT), a willingness to share a proven methodology and track record (e.g. PRIDE), capability to provide hands-on counselling (e.g. MEDA/UCP), or extension of a unique networking position (e.g. the Co-operative College and its links to SACCOs).

¹¹The fundamental reason for this is structural. As largely public sector creations, MFIs (and service providers) lack *equity*, funds which managers and shareholders have discretion to use for the development of their own institution, rather than merely for the immediate benefit of policy-nominated target groups ('beneficiaries'). It is part of the notion of best practice that institutions must not only build equity itself, but the ability to perceive and plan for its long term ('sustainable') uses in financial and institutional growth.

Support should be allocated based on documented improvements. Relevant potential service providers are:¹²

Educational institutions offering training in formal financial issues: the University of DSM - Faculty of Commerce and Management, the Institute of Financial Management, the Co-operative College, the DSM School of Accountancy, the College of Business Education, the Institute of Development Management, the Institute of Accountancy - Arusha.

Other institutions: ESAMI, REDI, OICT, MEDA and the Dr Amon J. Nsekela Bankers' Academy (former NBC training facility, future status unknown). In addition, practitioners from "best practice" MFIs should be regarded as an important resource.

Following the proposal to move towards cost-recovery and a market-driven approach there would seem to be three basic instruments available.

6.1.2 Tenders

Tenders are a well established instrument in public sector funding and a relevant precedent exists in promoting a market in service provision. The Institute of Bankers has contracted educational institutions, on the basis of tender, to tutor its members' staff in the well-established London Institute's distance learning curriculum. The principle of cost recovery is included, with member banks meeting the cost of provision. Some banks have required staff to meet the cost themselves, with the promise of reimbursement on successful completion. This is a good example of an incentive program.

Donors and governmental institutions promoting a capacity building initiative would advertise their project through the media and special invitations to relevant institutions. Although proposals would be developed in conformity with the policy and guidelines of the funding agency, the institution responsible for implementation would be exposed to competition and a critical examination of its own capacity to produce a convincing product. The benefits of a tender approach are its transparency in terms of criteria for funding and selection of institutions to be contracted; bidders have to work out the proposal by themselves, and document a track record proving their own capacity. By transferring responsibility for producing an implementation plan to the contractor, we have the beginnings of a price mechanism and (possibly) a reduction in cost to the public sector of program design.

The down-side, familiar to all consultants and those that use them, is that bidders may be tempted to promote their own capacity beyond reality. At the limit, ghost and briefcase institutions staffed with professional fund recipients could make a living based on fancy proposals, or the market could be distorted by political influence.

¹² The list is taken from K-REP's work, which the team has not been able to re-assess comprehensively. K-REP particularly recommends the following institutions as suitable for the development of curricula: REDI, ESAMI, K-REP themselves and the Cooperative College, as well as practitioners in "best practice" MFIs. The team would add OICT.

A tender approach should be developed incrementally, starting with small and transparent projects. In time, a short list of credible bidders would be established, based on assessment of capacity and performance.

6.1.3 Awards schemes

The Tanzania Enterprise Awards Scheme (TEAS) was launched at the time of the mission, as part of the DFID-funded regional program "British Aid to Small Enterprise". It offers a model for a responsive, rather than targeted or dedicated, approach and aims to develop the capacity of key individuals and organisations engaged in micro and small enterprise development. The scheme is to be promoted through the media and mail shots. Any relevant institution or person can apply, providing details about the institution, capacity inputs proposed and how the outcome will support long term improvements in the organisation. A committee decides upon support. Eligible institutions include: financial institutions, business training, consulting and counselling organisations. Most types of human resource development (short courses, seminars, conferences, study tours, exchanges etc.) are eligible for support, though long courses leading to a formal qualification are excluded. Selection criteria are designed to be as flexible as possible and, at this early stage, do not include any mandatory cost-sharing.

A similar scheme has been operating successfully in Kenya for four years and has proved flexible in responding to different and immediate needs. Applicants have at least to contribute in defining their needs and proposed activities and the risk is very low. Negative effects are said to be negligible, though real output is difficult to measure.

An awards scheme approach is better suited to small projects. It can also be a means for individuals and organisations (ie. more than one person from the organisation) to access international best practice. It is possible that larger MFIs - perhaps including the co-operative movement as a whole - could be assisted to introduce their own, internal awards schemes, giving the institutions the opportunity to select the candidates best suited for staff development, as well as putting an incentives scheme in place.

6.1.4 Vouchers

None of the approaches above gives direct purchasing power to the consumer of services, though an award scheme does allow choice. A voucher scheme seeks to do away with the need for the evaluation of individual proposals. Individuals or organisations receive a voucher from a funding agency and then have an opportunity to attend a training course etc. based on their own selection of provider and a match between cost and the nominal value of the voucher. The service provider gets the voucher and redeems its value from the funding agency, subject to some quality checks - often minimal and confined to a trainee, say, signing off on a certification of attendance and satisfaction of outcome.

Vouchers have already been used in Tanzania, as a means to re-orient civil service retrenched and equip them with appropriate business skills. They received five vouchers for counselling (value: TSh 500 each) and one voucher for training (value: TSh 100,000). Reported experience was mixed. Outreach appears to have been small

(approximately 3,000 persons, less than 10 percent of expectations). An incomplete and arbitrary assessment of capacity providers resulted in poor services received. No quality controls were put in place and it was not possible to ensure that the people trained really received services promised. In some cases "a practice of shortcuts" was observed, where the trainer and trainee agreed to skip the training and share the value of the voucher. Cumbersome procedures for payment to suppliers led to delays in redemption (in many cases lasting for two years), frustrated the whole system and resulted in a rapidly growing lack of confidence - from retrenched as much as from suppliers.

The attractive aspect of vouchers is, ideally, the "no cure - no pay" delivery system, and the means to put funding for capacity building in the hands of the client MFI rather than the provider, building a market among suppliers. The negative aspects are highlighted above. There is the further problem in this context that, while the universe of retrenched civil servants is easy to define and classify, as well as offering a direct voucher-delivery system through their former places of employment, no such data base exists for would-be MFIs (except for the SACCOs).

An evaluation would have to be made of who and which institutions would qualify to receive vouchers. Would individuals be eligible? It will be useful to learn of the experience of a contemporary voucher program in Kenya, funded by the World Bank and targeting *Jua Kali* MSEs. This project supplies vouchers to individuals and has, presumably, confronted these issues. For a real market to emerge, there should be many suppliers and good product/price information available to customers. These conditions, as we have established, do not exist in the specialised world of microfinance. A carefully planned voucher scheme would include a short list of pre-qualified suppliers, whose performance would be regularly re-assessed, creating the 'loops' referred to in section 4. Procedures for voucher redemption would be simple and speedy. Without these features, confidence in the system would be difficult to achieve.

To summarise: **Tenders** are best suited to encourage development in capacity provider institutions or big MFIs. Potential suppliers are limited, allowing transparency. As larger organisations, the procedures involved in a tender ought to be within their capability. **Vouchers** are best suited to support MFIs as organisations and offer them an opportunity to select the most appropriate capacity building services. **Awards** are best suited to support individuals in different organisations and offer them an opportunity to attend short courses or special events.

All capacity providers visited during the mission have expressed an interest and willingness to engage in a more business-like and market driven system of capacity provision. A few institutions (e.g. two or three financial NGOs and ESAMI) already have experience in market behaviour. Appropriate consulting companies (both in Tanzania and abroad) are expected to operate in a market driven system. Others (e.g. educational institutions) have very limited experience, as do most MFIs, especially small institutions. In the current context it is therefore unlikely that a purely market-driven approach will serve as the only method in order to create a dynamic system of capacity building initiatives. Before a market takes off, both sellers and buyers of capacity inputs need to acquire experience of market operations and behaviour.

6.2 Criteria for selection of means and institutions

This mission aims to set common standards for public sector support to the sub-sector. In the context of capacity building this will mean the adoption of some general criteria for choosing institutions worthy of support. In addition to the guidelines proposed in the summary, the following ideas, or "rules of the game", merit careful consideration:

- The bidder/applicant/voucher recipient should have a proven **track record** of at least two years of operations in the rural and microfinance sub-sector. This need not exclude new entrants, who could establish a track record by reference to the CVs of key personnel with a relevant background. What we seek is to raise standards, by excluding totally untried institutions run by people with no experience. There are instances in which this requirement would need to be interpreted broadly. A conference for parliamentarians has been suggested and, in this case, it is the evident track record of political leadership which is relevant.
- Institutions seeking support should be able to produce **current financial statements**. It is clear that we should not expect too high a standard but it is surely wrong to support an institution entering into financial commitments with both private individuals and tax-payers, unless the institution can demonstrate at least a basic grasp of accounting (and the notion of accountability). This requirement would have the important virtue of serving as a test of the present capability of the institution itself and a guide to its capacity building needs. Note that this implies an ability to read financial statements on the part of funding agencies - a crucial and historically damaging capacity shortfall in the superstructure. This criterion is not appropriate for individual applications, unless sponsored by their institution.
- Funding agencies have to make a judgement of the **quality of the proposal**. Whether by tender, approval of applications for awards or short-listing for voucher-eligibility, a judgement has to be made at some point as to the appropriateness of the proposed capacity-enhancing input to the present status of the institution and its development plans. Different programs will have varying requirements in detail but these should always be referred to and compared with standards of best practice. Considerations will include proposals for quality control, monitoring, reporting and plans for innovative product development.
- A particular measure of quality is the extent to which proposals **integrate strategies for addressing gender and equity issues**. Ritual phrases about women and the poor(est) are not enough. Indeed, 'best practice' rejects targeting in the old way. Rather, institutions can seek to design both their financial products and their own operations (procedures & staffing) in such a way as to make themselves more responsive and accessible to disadvantaged populations. This issue is complex; all the evidence suggests that rural financial markets - like any other - are stratified and it would be a mistake to concentrate only on the needs of, say, women with a small trading enterprise. The point is like that about financial statements. By requiring institutions seeking support to state their understanding and approach to these issues, we have an initial measure of existing capacity, a baseline against which to monitor the impact of the proposed intervention.

- To return to the question of a *market* in capacity building. We have argued that this is only meaningful if services are priced and that we should be aiming for full cost recovery in the delivery of services but, also, that this is not immediately practical. It follows that the criteria should include a willingness to bear part of the cost, as an interim step towards full cost recovery. Applications for support should, therefore, include a **proposal for cost-sharing**. Again, by insisting on this, funding agencies will be able to begin to assess effective demand.
- The need to forge linkages has been discussed. Criteria for support may include a weighting towards proposals which **create or strengthen linkages**. Institutions which are able to show progress (existing or planned) toward co-operation with potential partners may be preferred to those which continue to work in isolation.

These criteria are recommended for consideration; they are not yet agreed. What is important is a broad consensus between government and donors as to what counts as best practice and that these standards are transparent and disseminated to all relevant institutions. They should be flexible (methodology-neutral) enough to accommodate a wide range of initiatives but binding enough to impose some discipline on the sub-sector.

6.3 Performance indicators for capacity building initiatives

Detailed performance indicators will depend on the context of individual funding programs and, at this stage in the process, it is premature to define them too closely. It is also the case that *capacity building* is so nebulous a concept that it can be made to mean all things to all people. A particular problem is separating the impact of capacity building initiatives, *per se*, from the performance of the sub-sector as a whole. The table on the following page identifies some key performance indicators which are robust enough to be relatively easy to verify.

Table 6.1: Some proposed performance indicators for different actors

Output	Indicators (OVI)	Means of verifications	Assumptions
<p><i>Superstructure (donors and Government):</i></p> <p>Co-ordinated and demand driven support to capacity building initiatives in the sub-sector</p>	<p>Number of projects processed using different approaches</p> <p>Aggregate financials for the sub-sector</p>	<p>Reports on each support initiative provided by the relevant donor</p> <p>Supervisory agency estimates (not yet feasible)</p>	<p>The political will to co-ordinate and a common acceptance of a framework for intervention</p>
<p><i>Intermediate level 1 (service providers):</i></p> <p>Improved quality of services and methods of delivery</p>	<p>Number of clients served (individuals and corporate)</p> <p>Diversity of activities engaged in, in addition to formal training</p> <p>Appropriate rating from clients served</p> <p>New products developed & delivered</p> <p>Cost recovery as % of turn-over</p>	<p>Evaluation reports from participants</p> <p>Changing prospectus</p> <p>Audited financial statements</p> <p>Quarterly reports</p>	<p>Donor and Government facilitation</p> <p>High transparency in all transactions</p>
<p><i>Intermediate level 2 (MFIs):</i></p> <p>MFIs operate on a sustainable basis, provide extensive outreach and develop appropriate financial products</p>	<p>Increased volume financial operations</p> <p>MIS: ability to produce accounts/ loan track regularly</p> <p>Procedures for addressing systems failures</p> <p>Changed diversity of financ. Products</p> <p>Changes in practice: gender and equity</p>	<p>As defined by individual proposals</p> <p>Monthly & annual financial statements</p> <p>Audits & surprise checks</p> <p>MIS & ops.manuals regularly updated to address failures</p> <p>Current prospects</p>	<p>Suitable human resources are available for MFIs</p> <p>Existing market for micro financial services</p> <p>Clients attitude and honesty</p> <p>Appropriate legislation in place (including property rights and ownership)</p>

7 Conclusions and recommendations

To avoid duplication, recommendations are included in the Summary, under “Guidelines”. The most striking conclusion is that, despite the overall sector goal of *sustainability*, which embraces the concepts of a full cost recovery, or profit-making, market in financial services, reaching this goal entails public subsidy to accelerate the installation of ‘capacity’. The team is uneasy with this conclusion, not so much because of the obvious theoretical contradiction (which has been successfully overcome in other countries) as for the uncertain practical boundary it leaves between the ‘market’ and public sector support. Perhaps the most that can be said is that we should never lose sight of the overall goal, constantly referring any new measure to it, as the paramount criterion.

8 Appendices

- Appendix 1 Institutions and organizations visited and officials met by the capacity building team during the mission
- Appendix 2 “Emerging guidelines”, as developed in the Workshop
- Appendix 3 Reports and Proposals from the Mission

Appendix 1 Institutions and organizations visited and officials met by the capacity building team during the mission

In addition to people and institutions represented on the mission and at the Workshop, the Capacity Building team visited and met:

Date	Time	Institution/Organization Visited	Officials Met
12.09.97	Afternoon	Cooperative College – Moshi	Prof. S.A. Chambo: Principal Prof. M.J. Sizya: Director Research and Consultancy Ms. Margaret Msonganzila: Head, WID Department Mrs. F.A. Macha: Head, CC Kilimanjaro Wing
13.09.97	Morning	Kilimanjaro Cooperative Bank	Mr. Soevan Salm: General Manager Prof. A. Mwakabumbe: Chief Auditor Mr. Tawete: Regional Desk Coop. Officer SACCOs Mr. Bahati: Moshi District Officer SACCOs Mrs. Moshi district Officer SACCOS
	Mid Day	Mwika SACCO	Vice Chairman, Committee Members, Treasurer/Manager
	Afternoon	Marangu West SACCO	Chairman, Vice Chairman, Committee Members, Treasurer
15.09	Morning	PRIDE Tanzania	Mr. Rashid G.A. Malima: General Manager Various MIS Staff and Auditing Staff.
	Afternoon	PRIDE Tanzania: Arusha Branch	Branch Manager: Credit Officers and Members of a MEC in training session.
		REDI	Mr. Smuts Bomani: Director Mr. Nelson W. Waruinge: Training Manager Mr. Peter L. Lengewa: Trainer/Technical Assistant Mr. Bernard M. Wamburi: “ “
		ESAMI	Dr. Bachu, Senior Consultant

16.09.97	Morning	FAIDA	Mr. Henri van der Land: Programme Co-ordinator
18.09.97	Morning	British Council:(TEAS)	Ms. Sharon Garnett: Assistant Director
	Mid Day	MEDA: UCP	Mr. Nick Ramsing, Consultant
	Afternoon	OICT	Dr. R. Monji: ILO Consultant Mr. Anthony Getambu: Technical Adviser Mr. Altermius Millinga: Executive Director
		Akiba Bank	Mr. H. Tijink, Managing Director Mr. C.J. Knight: Director of Banking Operations
22.09.97	Morning	NORAD	Mr. Morten Heide: Second Secretary (Resident Economist)

Appendix 2 “Emerging guidelines”, as developed in the Workshop

Selection of providers of capacity development should be market based -- the institution receiving assistance should have choice across potential providers of capacity building services. Funds for capacity building should be placed in the hands of the client MFI, rather than the provider.

Provider institutions should provide management training for fees which cover costs at a minimum and generate profits in more mature organizations. Initial support to providers should be based on grants for the development of courses and full cost recovery in the delivery of training and capacity building.

Capacity building should focus on sectoral needs when possible and those should be methodology neutral. Multiple methods could be used such as study tours, twinning, secondment, part time classroom and on the job training.

There should be significant input from practitioners in the development of capacity building materials - and support for having capacity building provided by institutions which embody best practices.

Activities include:

- A survey of MFIs to assess existing capacity and types of training needed.
- Devotion of time and resources to sensitisation of staff to microfinance best practices.
- Internalization of these microfinance best practices should be phased according to absorptive capacity.
- Support creation of a forum or network for MFI linkages, to exchange experiences on best practices.
- Forge, do not force links between local business organizations and MFIs to build capacity

Hiring criteria should be merit based and should make an effort to appoint staff from outside the region. The MFI industry should make a strong effort to recruit personnel and trainers with experience in commercial and consumer finance.

Support for capacity building should be based on a commitment by the MFI to improve performance. Costs of capacity building for an MFI should be related to expected improvements in performance within a determined length of time.

Capacity building programs should:

- Integrate improved understanding of poverty and gender into the capacity building exercises.
- Promote ability of MFIs to build the capacity of their clients to manage their own financial affairs.
- Reflect the difference between the co-operative and MFI approach.
- Support development of a range of institutions capable of building capacity in MFIs, and enable them to compete with one another.

Appendix 3: Reports and Proposals from the Mission

K-REP has produced 3 reports and 7 proposals for further work in the sector. All issued in DSM/Nairobi at the 20. August 1997.

Reports:

- (1): Wangwe, S.M. & Lwoga, C.M.F: "Survey and Analysis of the Educational Institutions, NGOs and Private Companies Which can provide Training, Technical Assistance and Business Services to the Microfinance Sector".
- (2): Oketch,H.O & Ndulu,J.K and Nyagetera,B.M: "Survey and Analysis of Rural/micro finance Financial Institutions in Tanzania".
- (3): H.O.Oketch & J.IK.Ndulu & B.M.Nyagetera: "Survey and Analysis of Rural/Micro Financial Insitutions in Tanzania".

Proposals:

- (4): K-REP: "Proposal for a Capacity Building Program for Management Teams of Rural/Microfinance Institutions".
- (5): K-REP: "Proposal for Development and Promotion of Savings and Credit Co-operative (SACCO)".
- (6): K-REP: "Proposal for Legislation, Regulation and Supervision of Rural and Microfinance Institutions".
- (7): K-REP: "Proposal for an Initiative in Working with the Existing Financial Institutions".
- (8): K-REP: "Proposal for the Establishment of Pilot Community Banks".
- (9): K-REP: "Proposal for a Standardised MS Reporting and Business Plan Program for Rural and Microfinance Institutions".
- (10): K-REP: "Proposal for and Approach in Identifying and Co-ordinating Donor and Private Sources of Equity Capital for Rural/Microfinance Institutions".

Preliminary drafts from the mission sub-teams are:

- (1): "The Economic Framework for Microfinancial Services in Tanzania"
- (2): "Regulation and supervision of Microfinancial Services in Tanzania"
- (3): "The Role of Banks in Rural and Micro Finance"
- (4): "Community and Cooperative Financial Institutions"
- (5): "The Role of NGOs in Rural and Micro Finance"
- (6): "Capacity Building Initiatives for Rural and Micro Finance Institutions"
- (7): "Equity, Participation and Gender Issues in Rural and Micro Finance"
- (8): "Donor Support to the Financial Sector Programme"

They were submitted to the World Bank, DSM and summarised in:

World Bank: "Tanzania: Joint government of Tanzania and Multi-Donor Mission on Rural and Micro Finance Services". Draft Aide Memoire. DSM September 1997.