

## Assessing the Institutional Framework for Promoting the Growth of Micro and Small Enterprises (MSEs) in Tanzania: The Case of Dar es Salaam

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**This brief examines the institutional framework for supporting the growth of micro and small businesses in Tanzania. Findings indicate a high demand for business support among MSEs but only limited use of services, such as loans from financial institutions, due to the complexity and stringency of conditions to access these services. On the supply side, the capacity of MSE support institutions to provide effective services remains limited.**

**Based on the evidence collected the following recommendations are made to improve delivery of support services to MSEs: i) greater collaboration and coordination between public and private support institutions; ii) strengthening of information systems linking MSEs with existing support institutions and services; iii) establishment of referral and credit bureaus; iv) provision of fiscal incentives to private support institutions to enable them to lower fees and expand their service base.**

### Introduction

The link between institutions and development outcomes has become a “hot topic” in the international development debate. Recent literature has shown that institutions can contribute to growth and economic development through their role in stimulating investment, managing ethnic diversity and conflicts, encouraging better policies, and increasing social capital (Adebisi, 2004; Jütting, 2003).

Since the late 1980s, Tanzania has introduced significant political and economic reforms towards establishing a market-led economy. However, following the successful stabilisation of the macroeconomic environment, the effectiveness of institutions in supporting the growth of business enterprises remains a major concern for private sector development (Wangwe, 1999). This raises questions as to whether existing institutions have the capacity to deliver adequate and relevant services to promote the growth of domestic enterprises.

This study, conducted in Dar es Salaam in 2006 and 2007, examines the institutional framework for promoting the growth of micro and small enterprises<sup>1</sup> (MSEs) by assessing the demand for support services among MSEs and the capacity of key support institutions to supply services. Representatives from 83 MSEs and 53 MSE support institutions were interviewed. The study covered institutions from the public sector (central government ministries and agencies as well as local government authorities) and the private sector (including microfinance institutions, commercial banks, business associations and NGOs).

<sup>1</sup> Micro enterprises are defined as businesses with up to 5 employees and small enterprises are those with between 6 and 50 employees.

## Key Findings of the Study

### Demand for MSE Support Services

Tanzania has approximately 2.7 million enterprises, of which approximately 98% are MSEs (IFC, 2005). Potentially, a huge demand exists for quality MSE support services. Therefore, the study asked participating MSEs what types of services they most needed, and whether they were aware of or were already using support services.

### Types of Support Services Needed by MSEs

The types of services most frequently cited as needed by the enterprises surveyed were government support (100% of respondents), a conducive business environment (99%), financial services (98%) and market services (94%). Services to improve technical skills (49%), networking (36%) and management skills (35%) were less commonly reported. The kinds of government support mentioned included tax incentives, loans, guarantees, grants, market information, and an improved regulatory environment.

### MSEs' Awareness of Services Offered by Support Institutions

Awareness about services provided by support institutions varied depending on the type of service. Though a large majority of MSEs interviewed were aware of financial services (for example, savings, loans and credit) from banks, microfinance institutions and government agencies, many were unaware that these entities also provide information, advisory services and training. Services provided by non-financial service providers, such as consultants, associations and NGOs, were little known by respondents. Of note, almost two-thirds (62%) of the enterprises interviewed were aware of the government's responsibility for regulations, but only 34% and 24% of respondents were aware that the government was responsible for policy coordination and administration of standards respectively.

### Use of Support Services by MSEs

Use of support services was generally low. Around one-quarter to one-third of MSEs reported using the services provided microfinance institutions –

loans and credit (31% of respondents), training (24%) and advisory services (24%) – which were higher levels of usage than those reported for services from banks. However, these results indicate that MSEs have limited access to financial support institutions. The most common reason cited by respondents for not accessing loans from banks and microfinance institutions was a lack of information about these services. Bureaucratic procedures, high interest rates and lack of collateral were other barriers to loans reported by MSEs.

**Table 1: Proportion of MSEs using services provided by support institutions**

Type of Service	MSE Support Institutions			
	Banks	Micro finance institutions	Support services providers	Govern.
Loans and credit	18	31	8	5
Training	7	24	21	20
Advisory services	5	24	21	20
Information	3	2	7	5
Lobbying	0	0	2	4
Facilitation of trade fairs	0	0	4	6
Policy coordination	0	0	0	26
Regulations	0	0	0	59
Standards	0	0	0	16

## Supply of MSE Support Services

### Types of Services Offered by Support Institutions

The types of support services available to MSEs in Dar es Salaam was also assessed. The study asked representatives of support institutions in both the public and private sectors to identify the services they offered to MSEs.

The main players in the public sector are central government ministries and agencies as well as local government authorities (LGAs). In principle, the government is responsible for formulating policies and establishing the institutional framework for businesses, setting and enforcing regulations and standards, and providing appropriate incentives to encourage the development and efficient functioning of the private sector. The government ministries and agencies and LGAs interviewed reported policy

coordination and management as one of their core activities. Central government agencies and LGAs also reported their central role in setting and enforcing regulations. In addition, most LGAs and some central agencies offered financial, training and advisory services, and lobbied and advocated for small business interests.

The principal MSE support services reported by private sector institutions included financial services, advisory services, business linkages, training, and market promotion. Most services offered by the private sector are operated on a commercial basis, except for those provided by non-government organisations, such as associations, self-help organisations and not-for-profit entities. Some public-private partnerships in providing support services were identified.

### Conditions Imposed on MSEs to Access Services

The study found that most support institutions impose conditions on enterprises prior to delivering services, including: provision of collateral (e.g., land and buildings) as security for loans, cost sharing in the form of equity, proof of enterprise's legal status, business experience of owners, and inclusive gender representation (Table 2). While, in general, conditions for obtaining business services are inevitable, the proliferation, complexity and stringency of terms can represent significant barriers to MSEs. In some cases, institutions impose blanket conditions on MSEs and large-scale enterprises which can impede the majority of MSEs from

**Table 2: Conditions imposed by support institutions on MSEs to access services (% of respondents)**

Type of institution	Collateral	Cost Sharing	Business Experience	Gender Rep.	Legal status	No Conditions
Government ministries	0	0	25	0	25	25
Local governments	100	100	100	0	67	0
Government agencies	29	36	21	29	0	7
Commercial banks	100	100	100	0	100	0
Microfinance institutions	63	44	69	31	50	0
Private service providers	0	83	0	0	0	0
Business associations	0	20	0	0	0	20
NGOs	0	0	0	0	0	0
<b>Overall percentage of institutions reporting condition</b>	<b>42%</b>	<b>49%</b>	<b>43%</b>	<b>17%</b>	<b>30%</b>	<b>6%</b>

accessing support services. The study also revealed that public institutions (such as municipal councils and central government agencies) impose similar conditions for loans as financial institutions.

Furthermore, compliance costs as well as the lack of administrative, technical and/or scientific capacity of MSEs to meet conditions can present potentially insurmountable barriers in the short or medium-term. The combined impact of lack of resources and institutional weaknesses among MSEs act to further marginalise struggling businesses.

### Strategies to Reduce Barriers to Services

Given that MSEs commonly face barriers in accessing services, support institutions were asked what strategies they employed to facilitate service delivery. All respondent institutions employed supplementary services.<sup>2</sup> Due to the prohibitive costs of information collection and dissemination as well as capacity constraints of individual support institutions, partnerships between institutions makes a lot of sense. Hence, networking by support institutions was another common strategy used to improve service provision. Some support institutions also required clients to form groups or be members of cooperatives. These entities would then act as guarantors of loans or credits to individual MSEs. Advertising and regulation enforcement were other strategies identified by support institutions. They were, however, employed by less than a third of the institutions surveyed. Limited advertising of services could be responsible for MSEs' lack of knowledge of support services available.

### Capacity of MSE Support Institutions

The study also applied a self-assessment tool to examine four key aspects of support institutions' capacity to provide services to MSEs: financial capacity, human resources, information systems, and equipment and facilities. Less than half (47%) of respondents assessed their institutions as having 'strong' or 'very strong' financial capacity, which implies that the majority of the support institutions do not have sufficient financial resources to operate their programmes at desired levels. With respect to human resources, most institutions reported vacancies and are experiencing difficulties in motivating and

<sup>2</sup> For example, a bank may provide training in financial or business management to a prospective client prior to approval of a loan.

retaining staff due to inadequate incentive packages. The need for staff development was highlighted.

Respondent institutions pointed out that to create an appropriate organisational culture to deliver the types of services needed by MSEs, they would need to either hire new staff or re-orient existing staff. Overall, 70% of institutions reported having appropriate management information systems, but expressed that their systems could be improved to better serve MSEs, for example, systems could be upgraded to track and analyse client performance. Less than half (43%) of respondents felt that their institutions had adequate equipment and facilities. Three-quarters of the institutions reported the need for transport facilities (such as more vehicles) and promotional facilities (such as office accommodation, show rooms and posters) to provide more efficient support to MSEs.

Effective service delivery also depended on the general business environment in which MSEs and the support institutions operate, including government support for MSEs development, entrepreneurial skills and trustworthiness of MSEs, and cost sharing mechanisms. Support institutions ranked the need for talented MSEs as the most important 'external' need. This was cited by 83% of respondents. Support institutions prefer to deal with MSEs that can assume and manage risks related to business activities. MSEs also need to be trustworthy, particularly related to loan repayments. Almost three-quarters (74%) of respondents also felt that government support for MSEs was needed, and over half (51%) indicated that cost sharing by beneficiaries was important to show the commitment of MSEs to their own businesses, and allow wider coverage of services given limited resources.

## Conclusions and Policy Implications

The findings indicate a high potential demand from MSEs for support services. Indeed, most enterprises were aware of financial services offered by banks, microfinance institutions and government entities, but were unable to access services due to the stringency of conditions for loans. MSEs frequently lack the capacity to meet conditions hence limiting their ability to grow competitively. On the other side, MSE support institutions also faced financial and human resource constraints which limit their ability to operate programmes.

A number of policy implications emerge from the study findings. First, collaboration between public and private support institutions needs to be strengthened to improve service delivery to MSEs. Second, to reduce information asymmetry, information systems are required to inform support institutions of potential and existing MSEs, and also inform MSEs of potential services and existing support institutions. Third, the establishment of referral and credit bureaus may represent one strategy to improve MSEs access to financial services. Fourth, fiscal incentives for private support institutions should be considered to enable them lower service fees and expand their service base.

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