Original Research Paper

A comparative study on the uptake of outreach programmes, transaction costs and financial literacy by microfinance institutions in Uganda

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This study was undertaken to examine the relationship between financial literacy and transaction costs incurred by MFIs; to examine the relationship between financial literacy and outreach of MFIs; and to examine the relationship between transaction costs and outreach of MFIs. Clients of the MFIs participated in this study. Besides, the study took a cross-sectional research design and quantitative research paradigm. Correlation was conducted to assess the level of association between the variables under the study. Results indicated a significant positive relationship between financial literacy of clients and the transaction costs of MFIs ($r = .182$, $p > .05$). It was also observed that financial knowledge, financial skills and financial actions are not strongly related to outreach of MFIs ($r = 0.85$, $P > 05$). Results also indicate that transaction costs of MFIs have a significant relationship with their outreach ($r = .525$, $p < .05$).Findings indicate that MFIs are incurring high transaction costs to serve clients; this in turn is affecting their abilities to reach clients. The main conclusion that could be drawn from the above findings is that MFIs have not fully put into place measures to increase the financial literacy of their potential and current clients which will in the long run reduce on the transaction costs incurred. Arising from the above observations, the following recommendations were made; It is suggested that MFIs come up with village groups techniques, MFIs also need to team up with other development partners like the government and come up with financial literacy training programs for clients, and MFIs also need to increase on the group sizes and cover further areas as this will enable them to increase on their breadth, depth and number of clients.

Key words: Transaction costs, outreach, financial literacy, microfinance institutions,Uganda

INTRODUCTION

Microfinance institutions have failed to adequately reach poorer populations for a number of reasons, including the limited understanding and awareness of financial services by the poor Financial Inclusion Strategy (2010-2015). According to Bank of Africa annual report (2010), one of the challenges facing the Ugandan population is limited access. Mwaniki (2006) emphasizes that high transaction costs are one of the major factors limiting the expansion of micro finance, especially rural financial services. The

institutions that wish to serve the poorest will continue to face both prohibitively high risks and transaction costs in this market segment. Fernando et al., (2003).

To assess current levels of financial literacy and explore means to improve it, a construct is needed to measure consumers' ability to make effective financial decisions. Despite its importance, the academic literature has given little attention to how financial literacy is measured Sandra (2010). The financial literacy levels in Uganda are still low

Table 1. Background information of employees of MFIs

Item	Description	% Frequency
Age of respondents	Below 25 years	9.5
	25 - 35 years	61.9
	35 - 45 years	20.6
	Above 45 years	7.9
Qualification of respondents	Bachelor	95.6
	Masters	4.4
Work experience	Less than 1 year	19.5
	1 – 5 years	36.5
	6 – 10 years	21.8
	Above 10 years	21.8
Gender	Male	61.0
	Female	38.0

Source: Primary data

at all ages and social groups, something that is claimed for the low levels of financial inclusion and low saving rates. Financial literacy is critical for promoting access to finance by creating incentives and environments that promote desired financial behaviors such as saving, budgeting, or using credit wisely. Margaret et al., (2009) According to Christine (2010) lower financial literacy increases the need to train clients and explain how each product and service works. This needs to be taken into account when designing products and processes, making such very small loans involves high transaction costs, in terms of screening, monitoring and administration costs, per loan. Several authors therefore argue that the unit transaction costs for small loans to the poor are high as compared to unit costs of larger loans (Hulme and Mosley, 1996; Conning, 1999 and Sharma & Zeller, 1999). Here the argument is higher outreach means higher transaction cost in order to get information about creditworthiness of clients and training them on the procedures to be followed. It is of interest, therefore, to investigate the nature of the relationship between financial literacy, transaction costs and outreach of microfinance institution**s.**

RESEARCH METHODS

Measurement of variables

Financial literacy

This variable was measured using knowledge, skills and actions. (Kefela, 2010).

Transaction costs

This variable was measured using Group Development Costs, Monitoring Costs and Administration Costs, (Agarwal, 2006).

Outreach

This was determined according to these scholars (Tugyetwena, 2007; Christen, Robert, 1995, 2001; Fernando, 2006) and was later be modified to suit the study environment.

Validity of the instruments

All items were anchored on a five-point likert-type scale ranging from 5(strongly agree) to 1 (strongly disagree). Questionnaire was validated through expert interviews.

Reliability of instruments

The researcher tested the reliability of the instrument (using internal consistency approach) to find out whether it consistently measured the study variables on the scales used (Anastasi, 1982 & Nunnally, 1978).

Data analysis

The data was collected and entered using Epi-Info version 6.04b statistical package and then exported to a Statistical Package for Social Scientists (SPSS version17) for analysis. This generated frequency tables for demographic and descriptive data. The relationship between the study variables was established using correlation.

Ethical considerations

In an attempt to produce a quality and reliable study, the researchers first sought for permission from MFIs to allow them undertake the study. Data were collected by the researchers themselves. This was done in order to avoid any collection of information through unethical means such as research assistants who fill questionnaires themselves instead of taking to respondents.

PRESENTATION OF RESULTS

This section contains presentation and interpretation of study findings. The section also contains findings on characteristics of respondents.

Background information

The results in Table 1 below highlight the gender distribution, age distribution, education level and duration at MFIs of the respondents who participated in the study.

Findings in Table 1 indicate that majority of the employees of MFIs were male (61.0%). Their age structure is such that; most of them were aged between 25 and 35 years, followed by those in the 35 to 45 age bracket (20.6) and the minority were either below 25 years (9.5%) or

Table 2. Percentage distribution of the duration of existence of the MFIs

Item	Description	% Frequency
Duration of existence	1 - 5 year	15.4
	6 - 10 years	33.3
	11 - 16 years	46.2
	Above 16 years	5.1

Source: Primary data

Table 3. Outreach

Variable	Majority opinion	Percentage
We cover the biggest geographical area within our locality	Disagree	51.9
The products we offer enable us to reach a large public	Agree	63.3
We consider the geographical location of our clients	Agree	45.6
We give small size loans and hence many clients are served	Agree	82.3
Most of our clients are urban based	Agree	61.5
Our clients are aware of all the products that we offer	Agree	65.8

Source: Primary Data

above 45 years (7.9%).

The findings further revealed that most of the employees held first degrees (95.6%) and the rest had a second degree.

Findings about the duration of service at their respective MFIs, most employees had worked for between 1 – 5 years (36.5%), followed by an equal percentage of those who had worked for between 6 – 10 years and above 10 years (21.8%). And the least percentage of 19.5% had worked with the MFIs for less than 1 year.

Duration of existence of MFIs

The results in Table 2 below highlight the percentage distribution of the duration of the existence of MFIs that were selected for the study:

Findings about the length of operation of the MFIs as per Table 2 indicated that most MFIs had been in operation for between 11 – 16 years (46.2%), followed by those of between 6 – 10 years, (33.3%), 1 – 5 years, (15.4%) and above 16 years, (5.1%).

Outreach of MFIs

The results in Table 3 below highlight the percentage distribution of MFIs' breadth of outreach.

Besides the disagreement of the majority of the MFIs' about who covered the biggest geographical area within the locality (51.9%), there has been agreement about all aspects about the breadth of the outreach of the MFIs, including; the products offered enabling MFIs to reach a large public (63.3%), consideration of the geographical location of clients (45.6%), offering small loans that enable serving many clients (82.5%), most clients being urban based (61.5%) and clients awareness of all products offered (65.8%) as seen in Table 3.

Depth of outreach in MFIs

The results in Table 4 below highlight the percentage distribution of MFIs' depth of Outreach.

Besides disagreement to regularly targeting women by most of the MFIs (65.8%), Table 4 reveals that majority of the MFIs agreed to; targeting rural locations (48.1%), extending services more to the poor than the rich (46.8%), putting emphasis on lifting the status of societies that they serve (82.3%), serving the marginalized (68.4%) and having a small average loan size that touches the poor (83.5%).

Number of clients in MFIs

The results in Table 5 below highlight the percentage distribution of MFIs' number of clients.

Regarding the number of clients reached, findings in Table 5 revealed that most MFIs agreed to; their number of active clients increasing (68.4%), always aiming at keeping their existing clients (59.4%), regularly updating their packages to meet the needs of all clients (54.4%) and always opening new branches to reach more clients (48.1%).

Regression analysis

Multiple regression analysis was used to determine

Table 4. Depth of outreach

Variable	Majority opinion	Percentage
We target the rural locations for our services	Agree	48.1
We regularly target women	Disagree	65.8
We usually extend our services more to the poor than the rich	Agree	46.8
We always put emphasis on lifting the status of the societies that we serve	Agree	82.3
We regularly serve the marginalized (un educated and less educated)	Agree	68.4
We always have a small average loan size that touches the poor	Agree	83.5

Source: Primary Data

Table 5. Number of clients

Variable	Majority opinion	Percentage
Our number of active clients has always been increasing	Agree	68.4
We always aim at keeping our existing clients	Agree	59.4
We regularly update our packages to meet the needs of all our clients	Agree	54.4
We always open new branches/outreach centers to reach more clients	Agree	48.1

Table 6. Regression of financial literacy of clients and Transaction costs of MFIs with Outreach of MFIs

Outreach	Unstandardized Coeff.		Standardized Coeff.	t	Sig.
	B	Std. Error	Beta		
(Constant)	1.834	.507		3.616	.000
Financial literacy	.006	.027	.019	.214	.831
Transactions Cost	.714	.107	.461	6.697	.000
R Square	.294		F Statistic		32.921
Adjusted R Square	**.275**		Sig. (F Statistic)		.031

Source: Primary data

whether and how the study's independent variables and their components predicted the outreach of MFIs. Independent variables were financial literacy and outreach. Results obtained are shown in Table 6.

The multiple regression results in Table 6 that was generated by Pearson's analysis indicate that the independent variables explains 29.4% (R-Square = 0.294) of the variation in the outreach of MFIs. The results also show that at $p < 0.01$ level of significance; the variables linearly predict 29.4% of the variations in outreach.

Looking at the individual predator variables, transaction costs had a positive effect on the outreach of MFIs (Beta = ..714, p<.01), implying that the more MFIs spend on their activities, the higher the level of the outreach activities. The findings further revealed that literacy of clients had no significant effect on the outreach of financial institutions of the clients (Beta = .006, p>.05).

DISCUSSION

This section discusses the findings by comparing what was established in this study with what other scholars have established before in the literature review. It helps to draw conclusions as well as recommendations and other areas for future research.

It was established that 61.0% of the respondents were male and 39.0% were female. This therefore implies MFIs prefer to employ male. It was also discovered that 9.5% of the respondents were below 25years of age, 61.9% were between 25-35years, 20.6% were between 35-45years and only 7.9% were above 45 years. This also shows that most MFIs employ people between 25-35 years of age. The education level of the respondents revealed that 95.6% were at Bachelors level while 4.4% had masters' degree. This means that all the respondents had degrees. It also shows that MFIs in Uganda prefer to employ graduates.

On duration of service, it was discovered that 19.5% of the respondents had worked for less than 1 year, 36.5% had worked between 1-5 years, 21.8% had worked between 6-10 years, while 21.8% hard worked for a period above 10 years. These results clearly shows that most people that work in MFIs have served for a period less than five years and only 21.8% had worked for a period above ten years. Out of the MFIs selected, it was discovered that 15.4% have been in existence between 1-5 years, 33.3%

have been in existence for 6-10 years, 46.2% have existed for 11-16 years while 5.1% have been in existence for over 16 years. This implies that most of the MFIs had existed for 1-16 years, a good percentage of 15.4% accounts for MFIs which are just beginning while only 5.1% have existed for over 16 years. On the number operated by the MFIs, on average every MFI had approximately 23 branches, with a variation of 14 branches. This implies that MFIs have opened good number of branches that enable to reach clients.

Conclusion

The findings further indicated that financial knowledge, financial skills and financial actions have no significant influence on outreach of MFIs. Measures of outreach like targeting women, serving the rural population and serving more of the poor than the rich, were found not emphasized by the MFIs. This therefore implies that MFIs need to invest more in other areas other than the financial literacy of their potential and existing clients, as this has no influence on their outreach. The reduction in costs allocated on the financial literacy can be better placed in other areas that can create awareness.

Finding ways to reduce costs for poor borrowers is among the most important goals for micro credit. However, sometimes microfinance institutions focus too much attention on prices and forget the other factors that influence how and why the poor decide to borrow: quality of service, appropriate product terms and loan amounts, speed of delivery and access to future loans. MFIs therefore face a double challenge; not only do they have to provide financial services to the poor (outreach) but they also have to cover their costs in order to avoid bankruptcy (sustainability) (Woller, 2004).

RECOMMENDATIONS

In view of the above, the researcher was inclined to make the following recommendations:

It is suggested that MFIs with other development partners like the government, should come up with financial literacy training programs for clients, training workshops and seminars should be organized and information campaigns for example through local radios can go a long way in improving the financial literacy of existing and potential clients. This will increase on their awareness of the presence of MFIs, what the MFIs offer and how the MFIs can make customer tailored products.

Limitations of the study

The findings of this study are subject to some limitations

that provide the initiatives for future research.

One of the possible reasons for the varied results of the study is the methodology used for measuring the variables. Although the constructs have been defined as precisely as possible by drawing relevant literature and validated by practitioners, the measurements used may not perfectly represent all the dimensions.

Most of the MFIs were found to be in very rural and hidden locations. This strained the researcher to consider only those firms that could be easily reached thus causing a reduction in the response rate from 100% to 90.0%.

Areas for further research

Further research should be carried out on the tradeoff between MFIs outreach and sustainability to find out how microfinance programs can enhance their outreach to the disadvantaged and still remain sustainable.

Portfolio management, Risk management and Outreach of MFIs. How microfinance institutions can adopt better portfolio and risk management techniques that can enable them reach clients.

A similar study with a much larger sample of MFIs and a longer time period to see if the findings are different from those of the current study.

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