MICROFINANCE AND POVERTY REDUCTION IN SELECTED MICROFINANCE INSTUTIONS IN NAIROBI KENYA

BY

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BEC/43426/101/DF

A RESEARCH REPORT SUBMITTED TO THE COLLEGE OF ECONOMICS AND MANAGEMENT IN PARTIAL FULFILMENT OF THE REQUIREMENTS FOR THE A WARD OF BACHELOR OF ARTS IN ECONOMICS OF KAMPALA INTERNATIONAL UNIVERSITY

April 2013

DECLARATION

I, MAINA JOSEPH NDUNGU declare to the best of my knowledge that this research project is my original work and has not been presented to any university or any other institution for any award.

Signature.....Ndungu.........

Date.....02/04/2013.....

APPROVAL

I certify acknowledge that this work was done under supervision and has been submitted with my approval.

Signature..

DR. Derick Ssekajugo

Date............2/04/2013..........

DEDICATION

This research project is dedicated to my parents more especially my mum Mrs. Mary Wangechi who worked tirelessly to see that I completed my course successfully and moral support I needed through this entire course. I would also like to dedicate this research project to my supervisor who was cooperative and dedicated to see that I completed this research project successful. Also to my brothers and my sisters who are actually following the path that I have taken.

ACKNOWLEDGEMENT

First and foremost I thank Almighty God who has provided me with strength that I require both spiritually and mentally this research project would not be complete and successful with my own efforts only. I am grateful to my supervisor Dr. Derick Ssekajugo who went through my work and corrected me where I made mistakes, his time, kind guidance and constructive criticism during this report. I owe gratitude to my mum for giving me financial and moral support I need.

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ABSTRACT

The purpose of the study was to show the relationship between microfinance and poverty reduction and how microfinance has led to reduction of poverty in Kenya. The main or general objective of the research was:

I. To establish the contribution of micro-finance services in poverty reduction in Kenya.

II. To identify the various micro-finance services offered by micro-finance institutions in Kenya.

III. To identify the problems that hinder micro-finance services in Kenya.

The target population that was accessible was 50 out of the total population of 400 recorded clients and staff of Nairobi branch, 44 was selected in order to achieve the required sample, this sample was obtained using slovene's formula. Primary data was collected using questionnaire method administered to staff and clients analyzed through the use of descriptive statistics and MS Excel and data was presented using tables and pie charts. The sample population was picked using stratified random sampling. This technique was used because it provided for inclusion in the sample of the various sub groups in the target population.

The research instrument used were questionnaire where there these were structured and non-structured and they aimed at getting all the necessary data from respondents. This method was used because it is helpful in obtaining specified quantitative and qualitative information with accuracy and completeness, interviews where the researcher used interviews to acquire information that was not easily obtained through questionnaires. Interviews were used because it saves time when the interview schedules are structured and you get the first hand information from the respondents and it enabled the researcher to probe more for clarification, documentary review was also used where it involved reading documents related to clients drop out and microfinance.

The researcher used both the questionnaire and the general objectives to analyze the data, where he used gender that is both male and female where most of microfinance clients were female where 61% were women and above 38% were men. This shows that the initial objective of microfinance institutions of empowering the poor and rural women for self-sustaining and improve their standard of living, the researcher used marital status of single, married, window and divorced to analyze data, age group was also used, education level, duration in the organization of staff, services offered by microfinance institutions, effect of

microfinance services on poverty reduction and problem that hinder microfinance services, all based on questionnaire and objectives.

The findings of the study revealed that many people were helped with microfinance services such as savings, loans, advisory services, insurance services among others. According to the findings these services helped people of Kenya in increasing their investment in small businesses which in turn creates their income and later will lead to a better standard of living. The findings of the study also revealed that microfinance services helped people of Kenya in reducing their level of poverty with over 74% of the respondents agreed though there a significant proportion is living below the poverty line. The study revealed that microfinance institution has promoted women's empowerment in the society with 75% such business and more women become self reliant and they are in position of running their own business independently. However, not all women have been in full position of self reliance, thus more needs to be done since some of the women are still poor. The study also revealed that microfinance institutions played a big role in linking their clients to the agricultural sector with over 68% of the respondents agreed by offering them agricultural loans.

Conclusion, microfinance institutions play a major role in reducing poverty level to a lower level especially it helps low income households who are the most susceptible to poverty problems. Microfinance institutions provide services that are regarded important tools in alleviating poverty such as saving services, loan services, advisory services and insurance services. There is clear evidence that microfinance services have done a tremendous work in uplifting people's income and their standard of living though there are problems facing microfinance institutions in their bid to eradicate poverty such as people's inability to offer collateral security, lack of knowledge of microfinance institutions by the poor and shortage of funds that would be given to the poor.

The recommendations that were put forward where there is need for micro-finance institutions to increase the amount of loan they offer to the society especially the women as it had been found out by the study that the amount given was not enough to establish viable enterprises and promote socio-economic development, the government should provide and maintain the basic infrastructure at reasonable cost to consumers, such as communications, education and roads, there is a need for employment programs, Legal and institutional reform.

CHAPTER ONE

INTRODUCTION

Background of the study

Poverty alleviation has been a key development challenge over decades. It remains a matter of growing concern in many developing countries of the world. Today, as other continents continued to register sustainable economic growth and development, Africa was not only lagging behind but was trapped in vicious circle of borrowing and donor dependency syndrome which some critics pointed out as one of the causes practically sabotaging real development. Africa has been continuously failed to focus its development efforts on the optimum utilization of the immense natural resources that many countries were endowed with to turn it into wealth to propel their economies and people towards a high level of economic and social development and as a consequence to eliminate persistent poverty (Hulme D, 2000).

Although Africa was not the poorest continent, it was the only region where poverty was constantly on the increase. As result, millions of people lived each day in abject poverty. Children went without food, their bodies stunted by malnutrition which was wide spread. Lufumpa (1999) pointed out that in mid-1990s close to 50% of Africa's population of 700 million lived in absolute poverty and the majority of the poor live in rural areas.

One of the biggest problems of Kenya like many other countries in Africa was poverty. The country ranks 53 out of the 174 poorest countries in the world. (UNDP, 2006). Poverty was not only wide spread in rural areas but poverty is in the urban areas and yet this core problem was not yet been given the necessary attention it deserved. The majority of the people who lived in rural areas are women and children and many were dependent on agriculture. However, a large sector of agriculture was still subsistence and women are dominating using poor technology. The poor in rural areas were most cases not reflected in the macro-economic intervention and because of this scenario poverty was growing. Society holds women responsible for all the key actions required to end hunger, family nutrition, health, education and increasing family income. Yet women were still enslaved by customs and traditions which systematically deny those resources and freedom of action to carry out their responsibilities. The rural women were operating mainly in the informal economy where the whole context for their lives and economic activities do not produce enough surpluses to lift their standard of living. As a consequence they lacked the ability to generate incomes, to save, to start economic activities and to access credit from the formal sector was heavily restricted due to lack of collateral. The poor were traditionally disregarded as "un bankable" and "un creditworthy"

Therefore the problem of microfinance was to enable the poor people to pull out of their poverty situation was critical. Although micro-finance was a vital component in poverty alleviation, there was a general consensus among its proponents that it was not for everyone. One wonders who these poor people were to benefit from the intervention. In order for micro-finance to produce results, it required the support of other factors, most importantly, entrepreneurial skills, proper functioning infrastructure like capital market, financial services like insurance and working institutions. Therefore, Yunus (1999) believed that he can eradicate poverty using a simple model of microfinance that was put into question in the development debate.

In the case of Kenya, the issue of the importance of improving access to the poor was identified as a key development strategy right from the 1960s. The formal banks that were inherited from the colonial government were judged to be serving the trade sector and neglecting the agricultural sector that was the backbone of Kenya's economy employing over 80% of the population especially in the rural sector. This motivated the government to set up state owned banks like the former Kenya Commercial Bank Ltd whose mandate included among others to provide credit to the rural sector including agricultural credit. This was under the policy of sectoral allocation of credit and controlled interest rates which were administratively fixed by the Central Bank (Mwabu, 2000).

The credit to the poor engaged in agriculture was extended mainly in kind through the supply of productive inputs like fertilizers, high yielding seeds and tractor hire services under special bank schemes like Rural Farmers Scheme. The recovery performance of these credit schemes was poor partly because of the perceptions that these were government grants, and also because of the lack of the linkage between production and marketing. There were however concerns that this directed credit was not reaching the poorest of the poor as it were the non-poor with good political connections who mainly accessed this credit. The co-operative movement which emerged in the 1950s was also geared to providing financial services to the agricultural rural sector to boost their productive. However, the mismanagement which engulfed the cooperatives in Kenya led to their collapse in the 1990s (Mwendwa, 1999).

To enhance the efficiency of the micro-finance sector, the Micro-finance Development Institutions (MFDI) Act (2003) was enacted which provides opportunities for Microfinance Development Institutions (MFDIs) to be licensed and allowed to intermediate public savings.

Statement of the Problem

One of the most compelling challenges facing Kenya is the problem of poverty. Poverty was not only on a steady increase but also wide spread in rural areas (Mwabu, 1999). In the quest for solutions to the country's development challenge and poverty alleviation, micro-finance devices was becoming one of the most popular options as credit has been identified as barrier facing the poor (Ndungu, 2000). While many factors contribute to poverty, it was most obvious manifestation is insufficient household income. Both the extent of income-generating opportunities and ability to respond to such opportunities were determined to a great degree by access to affordable financial services. Increased the access of the poor households to micro- finance was therefore being actively pursued world wide. Improved access to micro-finance services would enable the poor to smooth out their consumption, manage their risks better, build their assets, develop their micro-enterprise, enhance their income-earning capacity, and enjoy an improved quality of life. (Mpuga,2004). While there could be several contributory factors to poverty reduction, micro-finance services may have played a major role. Hence the needs for this study appraising micro-finance services and poverty reduction using the case FAULU (KE) in Kenya. Thus the researcher was intending to identify the contribution of microfinance services towards poverty reduction in Kenya.

Purpose of the study

The purpose of the study was to determine the effect of micro-finance services on poverty reduction in Kenya.

Objective of the study

IV. To establish the contribution of micro-finance services in poverty reduction in Kenya.

V. To identify the various micro-finance services offered by micro-finance institutions in Kenya.

VI. To identify the problems that hinder micro-finance services in Kenya.

Research Questions

I. What are the contributions of micro-finance institutions in poverty reduction in Kenya?

II. What are the various micro-finance services offered by micro-finance institutions in Kenya?

III. 'What are the problems that hinder micro-finance services in Kenya?

Scope of the Study

The study was based on micro-finance services and poverty reduction in Kenya and Faulu (KE) Ltd was used as the case study. The research will be conducted at Nairobi branch as one of the micro-finance institutions in Kenya so as to ascertain the actual contribution of micro-finance services towards poverty reduction in Kenya. The study was take place over the two coming years 2013-2014.

Significance of Study

The study was to help in determining the contribution of micro-finance services on poverty reduction in Kenya. Similarly, the study was to contribute in identifying the problems currently faced by micro-finance institutions in their efforts to eradicate poverty. The study was help in suggesting possible solutions to the problems hindering micro-finance institution's operations. Furthermore, it was to help policy makers in particularly the government of Kenya on how to work closely with micro-finance institutions so as to eradicate poverty. The study was to help the researcher to gain an insight in the microfinance industry as well as a requirement for completing the course.

Operational Definition of key terms

Microfinance institutions refer to the provision of broad range of financial services to the poor people especially in rural areas in order to finance their businesses and elevate them from poverty level while Poverty refers to lack of basic necessities of life and opportunities for human development.

CHAPTER TWO
LITERATURE REVIEW

The Microfinance Services

According to Juan (1998), Microfinance is the provision of financial services (especially savings, credit, and insurance) to poor people excluded from the financial sector and particularly the working poor, the micro entrepreneurs with no access to banks and traditional financial institutions.

More broadly, it refers to the provision as many poor and near-poor households as possible have permanent access to an appropriate range of high quality financial services, including not just credit but also savings, insurance, and fund transfers.

According to Dichter. (2003), Kenya is endowed with a variety of microfinance operators offering a broad range of products. The services offered range from Village banking, provision of working capital or start up funds, business loans. Solar power loans, Money transfer in association with international transfer organizations, home investment loans, back to school loans among others.

Loans

According to Rutherford (2005), traditionally, banks have usually not provided financial services to clients with little or no cash income or people without collateral security. Banks must incur substantial costs to manage a client account, regardless of how small the sums of money involved.

According to Obwona, (1998), MFIs give loans to the poor so as to improve their small businesses and enable them compete favorably with the rich large scale companies. In Kenya, the vast majority of the poor have severely limited access to credit and other financial services. Thus MFIs tries to bridge this gap by availing credit services nearer to the poor. With the recent Economic liberalization measures, the creation of sustainable mechanisms for providing financial services to the low-income households particularly those in rural areas has become a critical element in the enhancement of Rural Development and poverty Alleviation. However, MFIs vary considerably in visibility, effectiveness and efficiency as well as the scale of operation and have attributed variously to the provision of credit to the rural poor (Barnes, 1998).

Savings

Micro savings allow individuals to store small amounts of money for future use without minimum balance requirements. Micro saving accounts is opened by the saver for life needs such as weddings, funerals and old-age supplementary income.

Concept of Poverty

Poverty is the state of one who lacks a certain amount of material possessions or money. Absolute poverty or destitution refers to being unable to afford basic human needs, which commonly includes clean and fresh water, nutrition, health care, education, clothing and shelter. About 1.7 billion people are estimated to live in absolute poverty today. Relative poverty refers to lacking a usual or socially acceptable level of resources or income as compared with others within a society or country (Barker, 1995).

For most of history, poverty had been mostly accepted as inevitable as traditional modes of production were insufficient to give an entire population a comfortable standard of living. After the industrial revolution, mass production in factories made wealth increasingly more inexpensive and accessible. Of more importance is the modernization of agriculture, such as fertilizers, in order to provide enough yields to feed the population.

The supply of basic needs can be restricted by constraints on government services such as corruption, debt and loan conditionalities and by the brain drain of health care and educational professionals. Strategies of increasing income to make basic needs more affordable typically include welfare, accommodating business regulations and providing financial services. Today, poverty reduction is a major goal and issue for many international organizations such as the United Nations and the World Bank.

Poverty in Kenya

Kenya has made enormous progress in reducing poverty, slashing the countrywide incidence from 56 per cent of the population in 1992 to 31 per cent in 2005. And, at 12 per cent, the reduction of poverty in urban areas has been even more marked. Notwithstanding these gains, however, poverty remains firmly entrenched in the country's rural areas, home to more than 85 per cent of Kenyans. About 40 per cent of all rural people – some 10 million men, women and children – still live in abject poverty. (Wright, 2001).

Kenya's poorest people include hundreds of thousands of subsistence farmers living in remote, scattered areas throughout the country. Remoteness makes people poor as it prevents them from benefiting from the country's steady economic growth and dynamic modernization. In these remote rural areas, smallholder farmers do not have access to the vehicles and roads they need to transport their produce to markets, and market linkages are weak or non-existent. Farmers lack inputs and technology to help them increase their production and reduce pests and disease. And they lack access to financial services that would enable them to boost their incomes by improving and expanding their production and by establishing small enterprises.

The poorest regions are the north and north-east of the country, where outbreaks of civil strife have disrupted small farmers' lives and agricultural production. These are fragile, dry and sub-humid regions where the extreme variability of rainfall and soil fertility means that farming presents a challenge. Production falls short of minimum household needs, rendering the inhabitants particularly vulnerable to food insecurity. Nationwide, about 5 per cent of all rural households continue to be affected by food insecurity. (UNDP, 2005)

Why are Kenya's rural people poor?

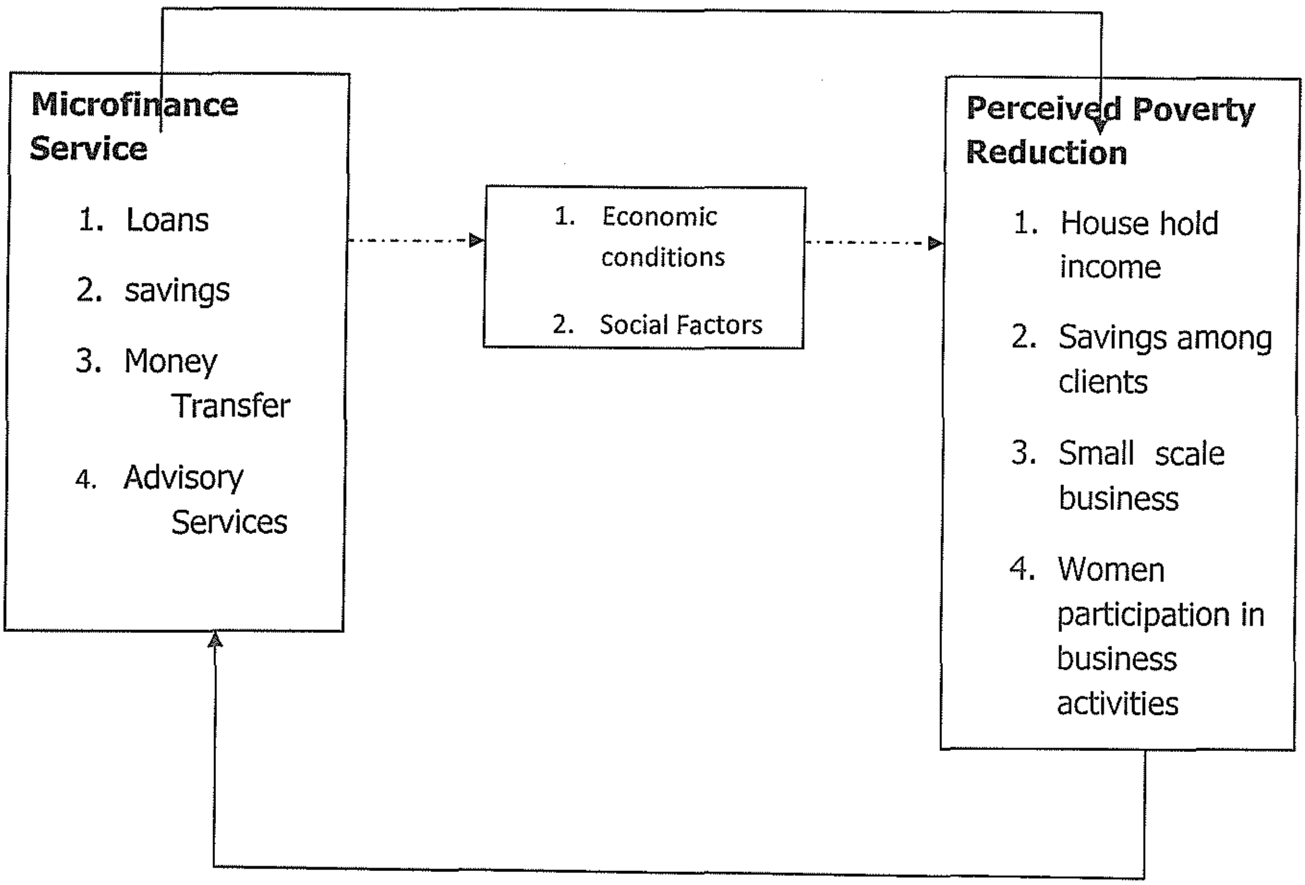
Health and social issues make a significant contribution to rural poverty in Kenya. The population of about 30 million is growing at a rate of 3.2 per cent/annum, doubling every 20 years. Although the country has been able to dramatically reduce the incidence of HIV/AIDS among the population, the pandemic has caused the death of large numbers of young adults and orphaned approximately 1 million children. The lack of health care, poor infrastructure like roads, schools as well as financial institutions like Banks, lack of enough employment opportunities due to inadequate capital intensive investments, environmental changes like deforestation, overgrazing and soil erosion, lack of enough quality information in markets, productive technologies, services, policies and rights, Land scarcity and legal protection of property rights, Government restriction on foreign trade and other social services puts rural women at a particular disadvantage. They work far longer hours than men, have limited access to resources and control over what they produce, and, among their many other tasks, they bear the double burden of ensuring their households are fed adequately and caring for the sick and elderly and for orphaned children. (Yunus, 1999)

Microfinance Contribution on Poverty Reduction

Microfinance Providers in Kenya reach low-income households in both rural and urban areas, but not the poorest of the poor. The average client is female, married, and sufficiently literate and many of whom are dependents (Barnes, 1998). Commerce is the main activity of clients, followed by agriculture, services and manufacturing. Most users of MFI services appear to be non poor. but not wealthy, they tend to come largely from households that can usually meet their daily needs, have access to primary education and basic health services, and have accumulated some assets. They tend to spend a high proportion of their earnings on basic needs such as food and education of children. These groups of clients are in the "comfort zone". They enjoy a relatively stable income source and sufficient livelihood diversification, allowing them to service regular repayments even when faced with small crises. However, they remain vulnerable to shocks, and access to microfinance has proven to play an important role in managing this vulnerability (Mutesasira, 1999).

Conceptual Framework

Microfinance programs and activities strengthen businesses and improve the welfare of the poor and their households. This is through the funds and advice obtained from the Microfinance institutions. However. Fernando, (2005). Microfinance services, if coupled with high interest rates, they destabilize the little income of the poor and they end up losing the little they have. (Vogel,1999):



Source: Schrieder, (1999)

The above framework illustrates how microfinance services can have a direct impact on poverty. However, this can be influenced by the social and economic forces. Social forces in this regard may include, the nature of families that is to say if they are extended families where there is a lot of dependency, then even if one obtains microfinance loans it still remains difficult to develop easily (Fernando, 1985). The economic factors in this regard include interest and the nature of the economy at large. For example if the microfinance loans are accessed at high interest rate then it is very difficult to remain with savings after business transactions. However, the situation is different if the interest rate is low and the business people can easily access markets, then high returns are expected which in which may have an impact on the financial status of such clients of the MFDIs (Paul 2004)

Reduced vulnerability to economic risks

According to Barnes (1998), the poor are very vulnerable to risks (such as illness or death of a household member, medical expenses. funeral costs, crop failure, the loss or theft of a key asset, or a dramatic change in prices), and microfinance services in Kenya have proven to help the poor to protect against these risks. Individuals and households pursue strategies to protect against risks ahead of time. As MFIs provide loans for working capital and to purchase productive assets, clients are able make their enterprises more competitive and increase profits (although in most cases only to a limited extent), diversify their income sources and broaden their asset base. Participation in microfinance programs also appears to enable clients to build the households' human assets. For example by investing into children education or household members health.

Group-based lending schemes provide clients with an opportunity to build their social assets by reinforcing reciprocal relationships and social networks. Membership of microfinance groups links individuals, households and enterprises into a vital web of business and personal relationships that enables members to better cope with the challenges of life. However, in some cases membership to groups can also become a social liability, especially where there is a consistent pattern of non-payment and mounting peer pressure. Access to financial services also allows the poor to cope with shocks or economic stress events once these take place.
Clients use microfinance loans to re-stock their businesses and to smooth consumption. (Baydas, 1997)

Strengthening linkages of clients and their households to the agricultural sector

Microfinance clients are actively involved in the agricultural and natural resource based marketing chain. Loans to micro entrepreneurs strengthen their position in the agricultural sector. Microfinance program participation results in clients expanding the amount of land they cultivate and diversifying the crops they grow for sale and domestic consumption. Clients of Microfinance are more likely than non-clients to increase their remittances to rural dwellers (Barnes, Morris and Gail 1998)

Gender and Empowerment

The vast majority of clients of Kenyan MFIs are women loans to female clients which constitute around 75% of the loan portfolio and 80% of the savings portfolio. Some microfinance provides like FAULU, PRIDE only target female clients. Most MFIs focus on women for two reasons. First lending to women is thought to benefit the whole family and strengthen the role of women in society. The second reason is that women, like in most other parts of the world, have proven to be better re payers. In some cases, women groups of female only MFIs accept men if they replace their deceased wives. However, it is not uncommon that a loan is in the husband's name hut the woman is running the business. In most microfinance institutions, especially in those only targeting women, at least half of the workforce is female. While MFIs increasingly recruit female credit officers and women constitute approximately half of senior management (varying form organization to organization), board members are still mainly men (MFPED 2000).

Increased Employment Opportunities

Through granting loans, MFIs have increased employment opportunities to different people. This is because loans enhance and boost up Business, hence leaching to Expansion and diversifications large businesses employ more people and even people who start up small businesses also employ some people. Similarly, MFIs as well also provide employment to the entire professionals in different sectors (FAULU (KE), 2004).

Advice on how to use obtained funds

MFIs provide financial advice to clients. This involves type and kind of viable projects that people can start up so as to yield high returns in a short period possible. This is because most people have been having problem on how to choose projects in which they are to invest their funds and they end up losing almost all their funds. Thus with provision of such advice, MFIs tend to reduce on poverty (Microfinance Competent Centre, 2001).

Reduction of Income Inequality

In FAULU (KE) 80% are women clients. This is because Women status has been left behind for long and most women are poor compared to men, According to (CEEWA-U, 2003), the reasons for targeting poor women include an interest to influence the welfare of the household incomes, desire to reach directly to the poorest of the economically active.

Poverty Alleviation

In Kenya like any other developing country, Microfinance Credit Institutions are reaching out to millions of people as a means of improving their livelihood, and bettering their communities.

According Central Bank of Kenya report (2001), the impact of Microfinance in poverty reduction is evidenced from the fact that there has been a tremendous reduction in general poverty from 80% in 1992 to 58% in 2000; house hold poverty is estimated to reduce to 30% by 2007 in rural areas.

Increased Investment, Savings and Schemes

Through the activities of Microfinance Institutions, people have learnt how to save their Money, which in turn is used for investment. For instance, those institutions that build up cash reserves through foregoing income. saving is possible by making deposits out of income by avoiding current use in order to draw a sum of these savings in the future for development purpose (Hanning, 1999).

Services Microfinance Institutions (MFIs) Offer

According to Dichter,(1998), Microfinance institutions offers different services including loans, savings, insurance, advisosary and money transfer services, and other basic financial services to the poor.

There are different types of loans, these are categorized differently. Micro Leasing, This option enables you to increase your business capacity and productivity. Through this Micro Leasing you can acquire equipment, machinery and motor vehicle, back to school loans short term loan facility that coincides with the new terms, semesters of institutions, extended to parents investing in education. The back to school loan is easy to access, the loan amount depends on the ability to repay repayment period of up to 4 months and there is no compulsory savings on the loan required. Other loan services include, Housing Loans that build your dream house, repair your present one or buy a plot of land with the Housing Loan. This facility is open to any individual irrespective of income level. Another type of loan is agricultural loan in which clients are offered to cater for their agricultural needs. (GTZ 2007)

What are Micro savings and Micro insurance, and how can they help the World's Poor?

For micro savings to work, they have to drastically cut banking costs. Low-income clients will typically have account balances under $80 and make frequent deposits under $5. No standard bank with branches and tellers could afford to maintain such accounts because the cost of each transaction is near $1. But Christen believes "there's a historic opportunity to reduce transaction costs through agent banking," where local petty shop owners double as deputized bank tellers while using mobile money and point-of-sale devices to transact cash, confirm identities, and keep books up to date. He predicts that transaction costs could go as low as 15 cents with this model.

As such platforms expand in scale while lowering costs; Christen envisions a rich ecology of private firms, government infrastructure, and non-profit organizations delivering new financial services to ever more remote regions. Christen has a quarter of a century of experience with microcredit behind him, but it's only recently that he's considered efficient micro savings possible. He focused on the challenge of lowering transaction costs.

Another class of services gaining momentum is micro insurance. Women routinely save 10-15% of their monthly income for health emergencies that can wipe out savings, said Mary Ellen Iskenderian, President and CEO of Women's World Banking, a network of worldwide microfinance institutions. Her firm is starting a micro insurance trial in Jordan where a premium equal to one day's wage per month - or 3% of income - provides health insurance that pays out for every night the client spends in a hospital, including stays associated with childbirth. According to Iskenderian, the insurance provides a sense of security to women who then feel less need to stash away cash, and in turn are able to apply income towards other expenses like education. Compared with credit as a way to handle emergencies, Iskenderian says, "micro insurance is a more efficient use of capital."

Problems Hindering Microfinance Services

Although the importance of microfinance in the process of poverty reduction is realized, it faces multiple problems. This is because offering credit to the poor is a complicated process and the sector is still in its experimental stage.

Problems are divided into two sets; challenges faced by Microfinance Institutions (MFIs) and challenges faced by micro entrepreneurs.

Perceived High Risk of Micro Entrepreneurship and Small Businesses

Micro entrepreneurs usually have no collateral to offer to microfinance providers against loans, they usually lack an alternate source of income, and have little, if any, formal education or training in the area of their business. As a result, commercial banks attribute a high credit risk to micro entrepreneurs and steer clear of this sector.

Microfinance institutes (MFIs) are compelled to compensate for this risk by charging interest rates on loans. Fortunately, the challenge can be resolved through the idea of group lending (social collateral against loans) which ensures good repayment rates.

High Costs Involved in Small Transactions/Microlending

The small size of micro enterprises increases the transaction cost for MFIs because they cannot process loans in bulk (unless good management information systems are in place). This denies MFIs the benefit of economies of scale; hence, they are forced to cover their costs through high interest rates on loans.

There is, however, a possible solutions to this problem – by improving the technology model used by microfinance institutes, their operational costs can be significantly lowered and efficiencies may be gained during automated loan processing.

Lack of Debt and Equity Funds for MFIs to Pass on to the Poor

Capital availability for microfinance is hardly a problem owing to the rapid growth in the microfinance sector, which has been fueled by attention from the media and development agencies. Even though there are plenty of financing options available for MFIs, there is an emerging shortage of money because of the current financial crisis across the globe. Another reason for this shortfall is the lack of awareness of funding sources by MFI managers.

Difficulty in Measuring the Social Performance of MFIs

Microfinance is delivering the economic returns its proponents promised, but there are only a handful of tools available that measure the social return of loan programs for the poor. To add to the problem, the tools use proxies to estimate the amount of poverty and social change surrounding micro entrepreneurs. This makes the gathering of funds a challenge because donors may question the actual impact made my microfinance.

Mixing Charity with Business

Since credit without strict discipline is nothing but charity (Professor Yunus), if microfinance providers fail to protect themselves against loan delinquency, they will, in effect, prioritize social objectives at the expense of financial sustainability.

Improper delinquency management is a result of inadequate implementation of corporate governance principles, and formal as well as semi-formal microfinance providers often suffer from this. As a result, looser controls over microfinance deals will lead to higher default rates.

Lack of Customized Solutions for the Poor

Inappropriate targeting of poor households by microfinance programs is a common problem because MFIs fail to understand the varied needs of micro entrepreneurs. MFIs must spend time in the field with their clients and his/her business, and then use this research to develop customized microfinance tools for each micro entrepreneur.

Generalized solutions may work for large companies dealing with large homogeneous customer groups, but microfinance providers need to serve the varied needs of individuals in each micro market segments.

Lack of microfinance training for Human Resource in Microfinance Institutions

Working in the microfinance sector is a different ball game compared to the traditional financial sector. For instance, microfinance officers and volunteers need to talk a different language, build lasting relationships with individual micro entrepreneurs, understand the unique needs of the poor, evaluate the borrower's sustainability, and grasp the cultural nuances of the borrower's communities (Yunus, 2008).

Of course, all this needs to be done by large financial firms as well, but the needs and characteristics of the two markets are very different. It's no surprise microfinance providers need special training to ensure they avoid problems such as intimidating or under-serving clients.

Poor Distribution System of Microfinance Institutions and lack of information about microfinance investment opportunities

There are over 10,000 MFIs across the world, but their reach is only 4% of the potential market. World Bank, 2001

Firstly, microfinance providers may be complacent with their client base in certain cities and feel no economic need (ignoring the social need to eradicate poverty) to spread out their distribution system to cater to the poorest of households. Secondly, micro entrepreneurs are sprawled over large geographical areas, often in remote places, which often makes them inaccessible to MFIs. This is a slight problem because even though there are over 10,000 MFIs around the world, they may not know about the existence and needs of certain micro entrepreneurs.

Dual mission of Microfinance Institutions to be Financially Sustainable as well as Development Oriented

Microfinance providers tend to forget their main objective is social development and not profit creation. The principle of 'one micro entrepreneur – one micro loan' is overlooked by profit-hungry MFIs who end up targeting the same individual for many loans and cause multiple borrowing (also known as credit pollution). This is a major problem because at the end of the day, that individual gets burdened by mounting interest payments and is pushed deeper into the folds of poverty. Poor governance on the side of MFIs as well as the micro entrepreneurs are to blame for this.

All these problems can broadly fall into either financial or operational in nature and we can therefore see that they should not be impossible to solve as the microfinance sector moves towards it optimal performance level in the next several years. In other words, despite these problems, the prospects of microfinance are quite bright.

Although the importance of microfinance in the process of poverty reduction is realized, it faces multiple problems. Offering financial services to the poor individual (the definition of microfinance) is a complex process and that in itself leads to various challenges

CHAPTER THREE
METHODOLOGY

Introduction

This chapter describes how the research was conducted. It gives an explicit description of the Research design, sample size and selection, methods of data collection, sampling methods, and data collection instruments.

Research Design

Descriptive research design was used in the study. Descriptive research design involves a systematic collection and presentation of data to give a clear insight with an aim to discover the extent of the problem. Quantitative research approaches was used to obtain the data that can be measured in numerical figures. The variables will be critically identified and helped in explaining the attitudes and behaviors of the subjects basing on the data collected.

Sources of Data

The source of data was both primary and secondary.

Primary source

Primary source refers to raw data collected through personal interviews, through questionnaires. It is also described as the data that have been observed and recorded by the researcher for the first time to their knowledge and data was collected by using interviews, surveys and observation methods.

Secondly source.

This provided data by reading related documents from the micro finance, institutions, and other related institutions like the institute of bankers, drafted Micro finance policies, Microfinance journals and any other related data.

Study Sampling Procedure

The population comprised employees, support staff, management at various levels. In order to obtain a representative sample, purposive judgment was used to identify the sample of clients and stratified sampling for staff.

Research Population

The study was conducted in Nairobi at FAULU (KE). It acts as a representative of all other branches in the Central Region. The target population is 400 but the accessible is 50.

Sample Size

From the accessible population of 50 out of the total population of 400 recorded clients and staff of Nairobi Branch, 44 was selected in order to achieve the required sample. This sample was obtained through Slovene's formula.

Data Collection Methods and instruments

Questionnaires

This refers to the collection of items to which the respondent is required to fill in the questions asked by the researcher. These were structured and non- structured and they aimed at getting all the necessary data from respondents. This method was used because it is helpful in obtaining specified quantitative and qualitative information with accuracy and completeness.

Interviews

Interview method refers to where there is person to person verbal communication in which one person or a group of persons asks the questions intended to obtain information. The researcher used interviews to acquire information that was not easily obtained through questionnaires. Interviews were used because it saves time when the interview schedules are structured and you get the first hand information from the respondents and it enabled the researcher to probe more for clarification.

Documentary Review

This method involved reading documents related to clients drop out and microfinance. It is advantageous because it enabled the researcher to get first hand information through critical examination of recorded information. It was also used to cross check information received from other research procedures.

Interpretation and presentation of data

The data was collected and processed and it involved checking the interview schedules for mistakes. The data entry was done by the secretary and verified by the researcher. For interpretation the researcher was to use simple statistical methods such as means, percentages and statistical programmes.

Data Analysis

After collecting data, preliminary data processing commences, it includes checking interview schedules, assigning serial numbers, sorting and filling. The data was to be analyzed using descriptive statistics or tools like pie-charts and frequency tables.

CHAPTER FOUR

PRESENTATION, ANALYSIS AND INTERPRETATION OF DATA

Introduction

This chapter deals with presentation, interpretation and analysis of key findings as related to the objectives and research questions "micro-finance and poverty reduction a case study of selected microfinance institution in Kenya". The findings are presented in frequency tables and percentages.

Background information of the Respondents

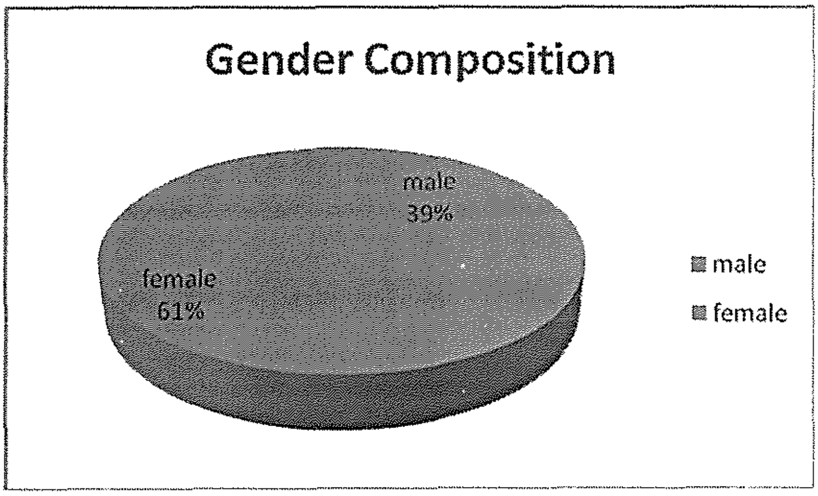
This part presents the background information of the respondents who participated in this study. The purpose of presenting this information was to find out the characteristics the respondents and show the distribution of the population in the study.

Table 1.1: Gender of the respondents

Respondents	Frequency	Percent (%)
Male	17	38.61
Female	27	61.36
Total	**44**	**100.0**

Source: Field Data, 2013

Figure 1.1



Source: Field Data 2013

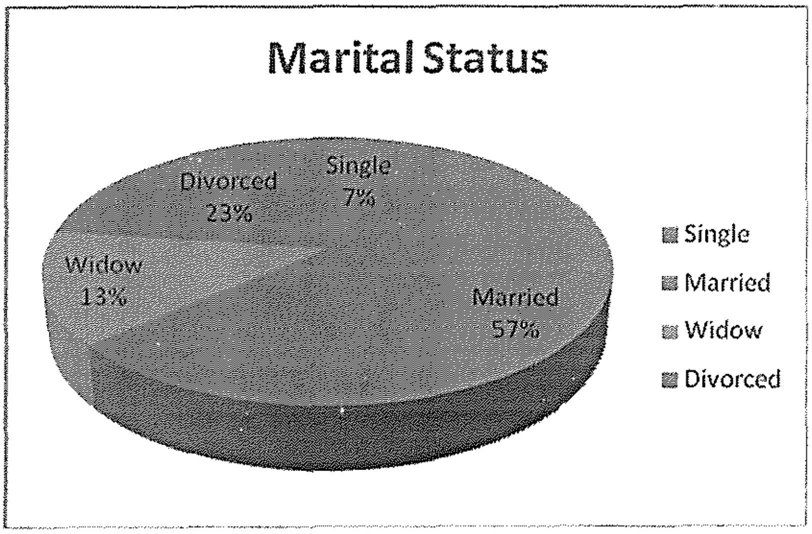
From above table, it is clearly seen that Faulu (KE) has most of it is clients as female since it serves above (61%) as women and above (38%) as men. This shows that the initial objective of microfinance institutions of empowering the poor and rural women for self-sustaining and improve their standard of living.

Table 1.2: Marital status of the respondents

Status	Frequency	Percent
Single	3	6.82
Married	25	56.82
Window	6	13.64
Divorced	10	22.73
Total	44	**100**

Source: Field Data 2013

Figure 1.2



Source: Field Data 2013

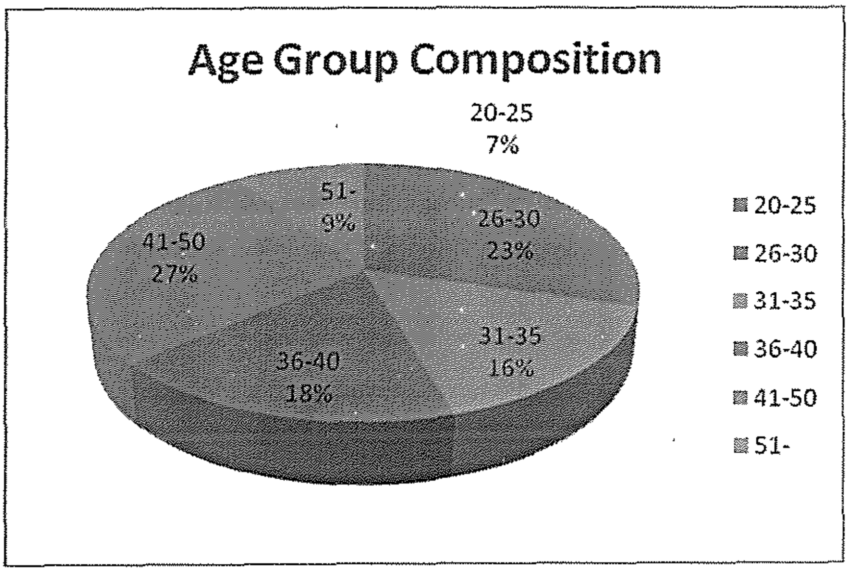
According to table 1.2 marital status of the respondents shows that married people are the clients that benefits microfinance services with a significant percentage of (56.82%). This shows that married couples have more financial needs than others. Divorced are second which also implies that married and divorced are more susceptible than other groups when it comes to those who need microfinance services. (Juan L. 2002)

Table 1.3: showing Age Group of respondents

Age Bracket	Frequency	Percent (%)
20-25	3	6.82
26-30	10	22.73
31-35	7	15.91
36-40	8	18.18
41-50	12	27.27
51-	4	9.09
Total	**44**	**100**

Source: Field Data 2013

Figure 1.3



Source: Field Data 2013

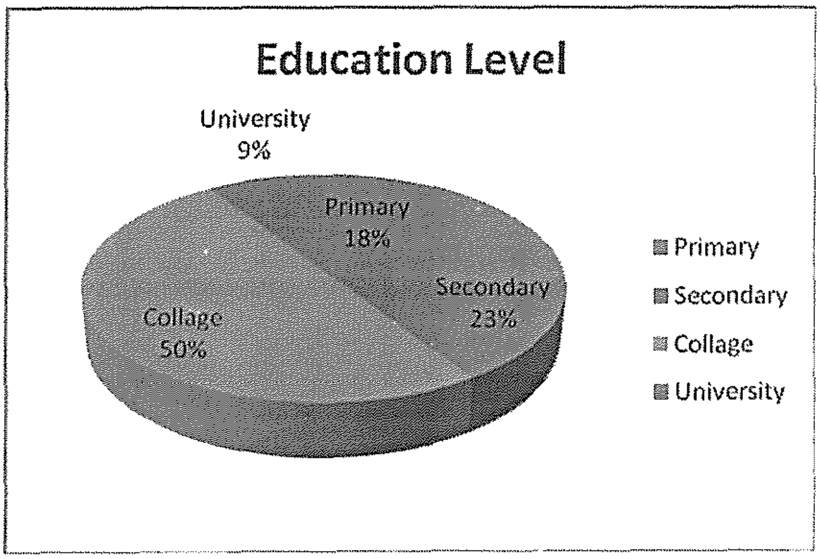
The findings indicate that the majority of the clients of Faulu (KE) fall under the age bracket of 41-50 years. This goes hand in hand with John Hatch (2000), who suggests that microfinance services are for the elders who have already established assets that can act as collateral security for easy access of loans.

Table 1.4: Educational level

Education Level	Frequency	Percent (%)
Primary	8	18.18
Secondary	10	22.73
College	22	50
University	4	9.09
Total	**44**	**100**

Source: Field Data 2013

Figure 1.4



Source: Field Data 2013

According to table 1.4 reveals that majority of the respondents had finished their O-level and college with various fields by (50%) and (22.73%) with diplomas and O-level respectively. This means that they have the skills and knowledge to manage their loans and this reduces the rate of defaulters.

Table 1.5: Duration in the organization

Duration	Frequency	Percent (%)
1-2	6	13.64
3-5	18	40.91
6-7	5	11.36
8-10	10	22.73
11	5	11.36
Total	**44**	**100**

Source: Field Data 2013

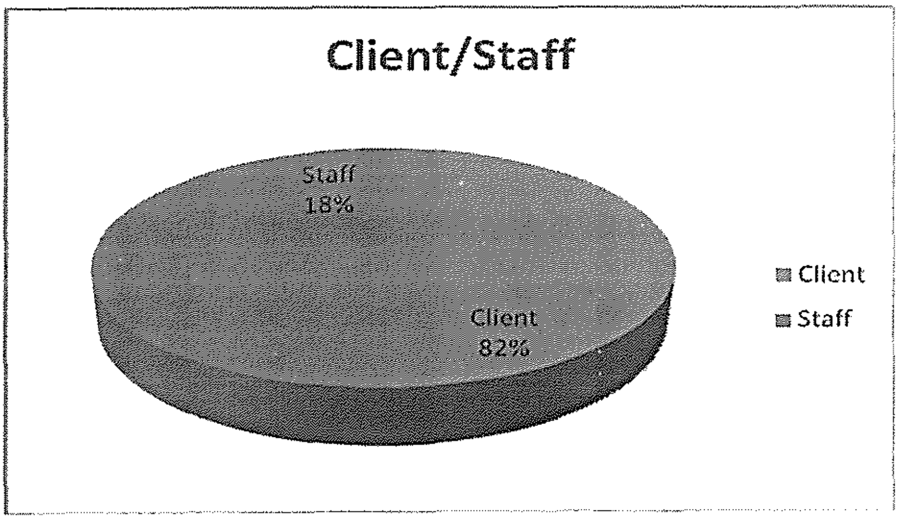
As per table 1.5 is concerned it reveals that above (40%) of clients have been a client to Faulu (KE) for 3-5 years and (22.73%) for 8-10 years .The table also shows that 6-7 and 11 and above years have similar duration of (11.36%). The table generally shows that people knew the advantage of being a client to a microfinance institution.

Table 1.6: Number of clients/staff

Client/Staff	Frequency	Percent (%)
Client	**36**	**81.82**
Staff	**8**	**18.18**
Total	**4**	**100**

Source: Field Data 2013

Figure 1.5



Source: Field Data 2013

Table 1.6 reveals that most of the respondents were clients scoring a percentage of (81.82%) and staff with (18.82%). this shows that most of the research was centered on clients since they are the beneficiaries of microfinance services.

Services microfinance institutions offer

Table 2: Microfinance Services

Respondents	**Strongly agree**		**Agree**		**Not sure or undecided**		**Strongly disagree**		**Disagree**		**Total**	
	No	%	No	%	No	%	No	%	No	%	No	%
Micro-finance institutions provide people saving services	24	54.5	18	40.9	2	4.5	0	0	0	0	**44**	**100**
Micro-finance institutions provide loans	20	45.1	17	38.6	4	9.1	2	4.5	1	2.3	**44**	**100**
Micro-finance institutions provide advisory services	12	27.3	17	38.6	10	22.7	4	9.1	1	2.3	**44**	**100**
Micro-finance institutions help people pay school fees of their children	15	34.1	16	36.4	6	13.6	4	9.1	3	6.8	**44**	**100**
Microfinance institutions provide insurance services	10	22.7	13	29.5	12	27.3	6	13.6	3	6.8	**44**	**100**

Source: Field Data 2013

According to table 2 majority of the respondents with 24 (54.5%) strongly agree that microfinance institutions provide saving services to their clients while 18 (40.9%) of the respondents agreed. 2 (4.5%) of the respondents become undecided. None of the respondents disagreed that microfinance institutions provide saving services. It is a sign that MFDIs play a major role in saving encouragement.

Table 2 shows that 20 (45.1%) of the respondents strongly agree that they are given loans by microfinance institutions. 17 (38.6%) of the respondents agreed they receive loans from MFDIs. A small percentage of 1 (2.3%) showed disagreement that they don't receive loans.
As per giving advisory services is concerned, 17 (38.6%) of the respondents agreed that they are given advisory services on how to use the loans in order to reduce their defaulting. Similarly 12 (27.3%) strongly agree that they are given advisory services. O n the other hand 4 (9.1%) of the respondents strongly disagreed loan services by microfinance institutions offer while 1 (2.3%) disagreed. A good percentage of the respondents i.e. 10 (22.7%) became undecided.

It is also evident from table 2 that a significant percentage of the respondents i.e. 16 (36.4%) strongly agreed that microfinance institutions help people pay school fees of their children and 15 (34.1%) of them agreed as well. On the other hand a small people strongly disagreed and agreed fairly with 4 (9.1%) and 3 (6.8%) respectively.
Table 2 also reveals that majority of the respondents 13 (29.5%) agreed that microfinance institutions offer insurance services to their clients though a significant number 12 (27.3%) became silent on it. On the other hand 6 (13.6%) strongly disagreed on the issue of paying school fees.

Effects of microfinance services on poverty reduction

Table 3: microfinance services and poverty reduction

Respondents	**Strongly agree**		**Agree**		**Not sure or undecided**		**Strongly disagree**		**Disagree**		**Total**	
	No	%	No	%	No	%	No	%	No	%	No	%
Micro-finance services help against poverty	14	31.8	19	43.2	7	15.9	3	6.8	1	2.3	**44**	**100**
Micro-finance institutions give entrepreneurship skills to clients	11	25	24	54.5	6	13.6	0	0	3	6.8	**44**	**100**
Micro-finance institutions give priorities to women empowerment	18	40.9	15	34.1	4	9.1	5	11.4	2	4.5	**44**	**100**
Microfinance institutions create employment opportunities	13	29.5	16	36.4	7	15.9	6	13.6	2	4.5	**44**	**100**
Micro-finance institutions link their clients to agriculture	13	29.5	17	38.6	6	13.6	7	15.9	1	2.3	**44**	**100**

Source: Field Data 2013

The findings from the research revealed that majority of the respondents agreed that microfinance services reduce poverty. This is evident from table 3 with 19 (43.2%) while 14 (31.8%) strongly agreed it. On the other side (2.3%) and 3 (6.8%) disagreed and strongly disagreed respectively while 7 (15.9%) were undecided.

Similarly the findings revealed that most of the respondents agreed that microfinance institutions provide entrepreneurship skills to clients with 24 (54.5%) showing their agreement. Small percentage of the respondents 3 (6.8%) disagreed that they gain entrepreneurship skills from microfinance institutions and 6 (13.6%) became undecided.
The findings also revealed that respondents agreed and strongly agreed that microfinance institutions give priorities to women empowerment. This is shown in table 3 18 (40.9%) strongly agreed and 15 (34.1%) agreed. A small number of the respondents 2 (4.5%) and 5 (11.4%) disagreed and strongly disagreed respectively and (4 9.1%) were undecided.

The study findings further reveals that 16 (36.4%) of the respondents agreed that microfinance institutions provide employment opportunities to their clients and 13 (29.5%) strongly agreed on it. While 2 (4.5%) and 6 (13.6%) disagreed and strongly disagreed on the issue. Few percent of the respondents i.e. 7 (15.9%) became undecided.
Table 3 also revealed that majority of the respondents 17 (38.6%) agreed that microfinance institutions link their clients to agriculture by offering agricultural loans and 13 (29.5%) strongly agreed on it. On the other hand 1 (2.3%) and 7 (15.9%) agreed and strongly agreed on agricultural linkage of clients and 6 (13.6%) of the respondents were undecided.

Problems that hinder microfinance services

Table 4: Problems hindering microfinance services

Respondents	Strongly agree		Agree		Not sure or undecided		Strongly disagree		Disagree		Total	
	No	%	No	%	No	%	No	%	No	%	No	%
The Poor's inability to offer marketable collateral for loans	17	38.6	14	31.8	8	18.2	4	9.1	1	2.3	**44**	**100**
People lack the knowledge about microfinance services	8	18.2	29	65.9	4	9.1	2	4.5	1	2.3	**44**	**100**
Lack of debt and equity funds for microfinance institutions to pass on to the poor	4	9.1	23	52.3	12	27.3	3	6.8	2	4.5	**44**	**100**
Microfinance institutions are poorly distributed	11	25	18	40.9	7	15.9	7	15.9	1	2.3	**44**	**100**
Lack of microfinance training for human resource in microfinance institutions	7	15.9	21	47.7	5	11.4	6	13.6	5	11.4	**44**	**100**

Source: Field Data 2013

According to table 4 the findings revealed that majority of the respondents 17 (38.6%) agreed that lack of collateral security of clients especially the poor hinder microfinance services while 14 (31.8%) of the respondents strongly agreed on it. This implies that the benefit of microfinance services is limited to few people who can offer security for loans. 4 (9.1%) of the respondents strongly disagreed that lack of collateral security hinders microfinance services.

The findings of the study also reveals that majority of the respondents believe that people are not aware of the services microfinance institutions offer with 29 (65.9%) agreed and 8 (18.2%) strongly agreed. This may reduce people's intention for investment, output, and standard of living. Less than 3% and 5% disagreed and strongly disagreed while 4 (9.1%) of the respondents became undecided.

The findings of the research also revealed that more than 52% of the respondents agreed that microfinance institutions lack enough fund to pass to their clients which will cause interest rate to increase and may later lead to default, while less than 7% of the respondents strongly disagreed.

Similarly the study revealed that a significant percent of the respondents 18 (40.9%) agreed that microfinance institutions are poorly distributed. This implies that most needy people such as rural people will not benefit from microfinance services and it is against the objective of microfinance institutions which is helping low income people. On the other hand less than 19% disagreed while 7 (15.9%) were undecided on the matter.
The findings similarly showed that more than 63% of the respondents agreed that the lack of training of their human resource contributes obstacles to microfinance services while 25% of the respondents disagreed. Few of the respondents were undecided with less than 12%.

CHAPTER FIVE

FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

Introduction

This chapter presents the summary of findings, conclusion, recommendation and suggestion for future research in line with the study objectives and research questions.

Summary of the findings

This research study was aimed at identifying the contribution of the micro-finance services in poverty reduction in Kenya using as a case study Faulu (KE). The research was guided by its objectives which were services microfinance institutions offer, microfinance services and poverty reduction and problems that hinder microfinance services.

The study revealed that many people were helped with microfinance services such as savings, loans, advisory services, insurance services among others. According to the findings these services helped people of Kenya in increasing their investment in small businesses which in turn creates their income and later will lead to a better standard of living.

The findings of the study also revealed that microfinance services helped people of Kenya in reducing their level of poverty with over 74% of the respondents agreed though there a significant proportion is living below the poverty line.

The study revealed that microfinance institution has promoted women's empowerment in the society with 75% such business and more women become self reliant and they are in position of running their own business independently. However, not all women have been in full position of self reliance, thus more needs to be done since some of the women are still poor.

The study also revealed that microfinance institutions played a big role in linking their clients to the agricultural sector with over 68% of the respondents agreed by offering them agricultural loans.

As per the challenges faced by microfinance institutions are concerned, the study also revealed that they are faced with challenges in their pursuit of reducing poverty. Among the challenges the researcher identified include; the Poor's inability to offer marketable collateral for loans, lack of knowledge of microfinance services by the people , lack of enough fund of microfinance institutions, poorly distribution of microfinance services among others.

According to the most of the respondents, over 60% of them agreed the existence of the challenges.

Conclusion

Microfinance institutions play a major role in reducing poverty level to a lower level especially it helps low income households who are the most susceptible to poverty problems. Microfinance institutions provide services that are regarded important tools in alleviating poverty such as saving services, loan services, advisory services and insurance services.

There is clear evidence that microfinance services have done a tremendous work in uplifting people's income and their standard of living though there are problems facing microfinance institutions in their bid to eradicate poverty such as people's inability to offer collateral security, lack of knowledge of microfinance institutions by the poor and shortage of funds that would be given to the poor.

Recommendations

From the findings of the study, it was revealed that microfinance institutions were being faced with a lot of challenges. The following are the recommendations put forward:

i. There is need for micro-finance institutions to increase the amount of loan they offer to the society especially the women as it had been found out by the study that the amount given was not enough to establish viable enterprises and promote socio-economic development.

ii. The government should provide and maintain the basic infrastructure at reasonable cost to consumers, such as communications, education and roads, because these infrastructures provide a foundation for economic activities. Community-level investments in commercial or productive infrastructure (such as market centers or small-scale irrigation schemes) also facilitate business activity.

iii. There is a need for employment programs. The government through ministry of trade and commerce should prepare employment programs to the poor for self-employment. Food-for-work programs and public works projects fit this model.

iv. Legal and institutional reforms. The legal and institutional reforms can create incentives for micro-finance by improving the operating environment for both micro-finance providers and their clients. For example, streamlining micro enterprise registration, abolishing caps on interest rates, loosening regulations governing nonmortgage collateral, strengthening the judicial system and reducing the cost and time of properly and asset registration can foster a supportive climate for micro-finance.

v. Women should be given support by the society in general and their spouses in particular in respect of finances, motivational encouragement, advice and actual involvement in the participating of the economic activities.

vi. Government should improve on the accessibility of finance by awarding several. Micro-finance institutions and commercial banks in order to improve on the competition in loan businesses.

Areas for further research

i. Understanding and dealing with high interest rate on micro credit in Kenya.

ii. Microfinance services and women entrepreneurship in Kenya.

iii. Impact of structural adjustment program on poverty and income distribution in Kenya.

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APPENDIX A:

QUESTIONNAIRE

Dear respondents;

My name is MAINA JOSEPH NDUNGU pursuing Bachelor of Arts in Economics of Kampala International University. I am conducting a research on "MICRO-FINANCE AND POVERTY REDUCTION A CASE STUDY OF SELECTED MICRO-FINANCE INSTITUTION IN KENYA". You have been selected to take part in this study by faithfully completing the attached questionnaire. Please note that you responses will be treated with confidentiality.

SECTION 1: Profile of respondents

Direction: Kindly tick the appropriate space or provide the date requested where appropriate.

1. Gender Male ☐ Female ☐

2. Marital status Single ☐ Married ☐

3. Age of the respondents

20 – 25 ☐ 26 – 30 ☐

31 – 35 ☐ 36 – 40 ☐

41 – 50 ☐ 51 and above ☐

4. Educational level

Primary ☐ Secondary ☐

College ☐ University ☐

5. How long have you been in this organization?

1 – 2 years ☐ 3 – 5 year ☐

6 – 7 years ☐ 8 – 10 years ☐

11 – And above years ☐

6. Are you a client or staff?

Client ☐ Staff ☐

SECTION 2: Services Micro-finance Institutions Offer

Please use the key below to answer the following statements by indicating: (5) strongly agree, (4) agree, (3) not sure or undecided, (2) disagree and (1) strongly disagree

Respondents	5	4	3	2	1
1. Microfinance institutions provide people saving services					
2. microfinance institutions provide people loan services					
3. Micro-finance institutions provide advisory services (I.e. how to use obtained funds)					
4. micro-finance institutions help people pay school fees of their children					
5. micro-finance institutions provide insurance services					

SECTION 3: Effects of Micro-finance services on Poverty Reduction

Please use the key below to answer the following statements by indicating: (5) strongly agree, (4) agree, (3) not sure or undecided, (2) disagree and (1) strongly disagree

Respondents	5	4	3	2	1
1. Micro-finance institutions help people against poverty					
2. Micro-finance institutions give entrepreneurship skills to clients to eradicate poverty					
3. Micro-finance institutions give priorities to women empowerment					
4. Micro-finance institutions help increase women employment opportunities					
5. Micro-finance institutions help people link to the agriculture sector					

SECTION 4: Problems that Hinder Micro-finance Services

Please use the key below to answer the following statements by indicating: (5) strongly agree, (4) agree, (3) not sure or undecided, (2) disagree and (1) strongly disagree

Respondents	**5**	**4**	**3**	**2**	**1**
1. the poor's inability to offer marketable collateral security for loans					
2. people lack the knowledge about micro-finance services					
3. lack of debt and equity funds for micro-finance institutions to pass on to the poor people					
4.micro-finance institutions are poorly distributed					
5. lack of micro-finance training for human resources in micro-finance institutions					