

INNOVATIVE LENDING METHODS AND THE GROWTH OF MICROFINANCE INSTITUTIONS IN RWANDA: A CASE STUDY OF URWEGO OPPORTUNITY BANK

Tumwesigye Dennis, Dr. Patrick Mulyungi

Jomo Kenyatta University of Agriculture and Technology

Abstract: The researcher sought to determine the effects of digital credit services on the growth of Urwego Opportunity bank in Rwanda, to establish the effects of flexible lending services on the growth of Urwego Opportunity bank in Rwanda and to determine the contributions of specific course lending methods on the growth of Urwego Opportunity bank in Rwanda. The researcher used descriptive survey when conducting this study. The study focused on Urwego Opportunity Bank in Kigali city. Urwego Opportunity Bank MFI has eight branches in Rwanda. However, four of them operate within Kigali City. The researcher collected 89 clients and 11 employees. The researcher used cluster method to collect information from the clients whereas stratified sampling was used to collect information from the employees. The exercise was conducted in 2 days. Qualitative data was entered into appropriate analysis programme, preferably statistical package for social sciences (SPSS) from which analysis were done using proportions (percentages), rates and descriptive statistics. Descriptive statistics were used to estimate the mean and standard deviations of certain variables to ascertain how close or wider the sample statistics were spread from the mean. Qualitative data was entered into a compilation sheet whereby the information from various respondents were tabulated. Responses which showed similarities were given a theme. Each theme was transferred into one sheet from which final analysis was done in relation to objectives of this study. The study found that that mobile phone applications are one of the main products used to reach out to more clients in MFI. Although MFI have tried to innovate ways of reaching out to clients, majority of the clients still have reservation for adopting the new changes. This was observed when the respondents were asked to state the maximum amount they can deposit using mobile banking and 62.8% stated that they are willing to part with any amount not more than 50,000 Rwandan francs. The study found that product innovation in MFI is very important in ensuring that they reach out to as many as possible clients. This is evident by the response rated at 36.4% of the respondents who supported it arguing that MFI should be in a position to introduce a new good or service to the market. Another important aspect is process innovation whereby a new production process or methodology should be effective and efficient. This was supported by 36.4% of the respondents who stated that process development is equally important as the product development. The study indicates that in average there are similarities between the outcome of the employees who believe that innovative ways of reaching out to customers are effective and efficient, withdrawal and deposit in Letshego Microfinance due to its innovative products as indicated, easy ways to check balance in their accounts, easier ways of opening an account, quick access to MFI services, error free records innovative services, 24hour online services, security of innovative products and time saving. The study recommends that there is a need to put much attention into the technological innovation, infrastructure building, institutional development, and human capital formation which directly increase the productivity and human resources. There is also a need to ensure an appropriate regulatory and prudential framework for the market of Microfinance including capital adequacy ratios, asset quality indicators and unsecured loan limits. It is important to provide a specialized credit bureau for Microfinance that can help financial institutions to have necessary information on clients in order to minimize risks.

Keywords: Innovative lending methods, growth of microfinance institutions.

1. INTRODUCTION

Innovation in banking sector has really improved over the recent years in most parts of the world. Financial institutions are seeking alternative banking channels to enable them to reach more and more clients as well as increase financial inclusivity especially those who live in the rural areas. According to Rangarajan Committee report (2008) Financial Inclusion is defined “as the process of ensuring access to financial services, timely and adequate credit where needed by vulnerable groups such as the weaker sections and low income groups at an affordable cost”. However, it is observed that financial exclusion is highly witnessed in developing countries especially Asia and African countries.

According to Ledgerhood (2009) there has been many more Microfinance Institutions (MFI) which has failed than those which have succeeded. He pointed out some of the challenges citing that some of MFIs target a segment of the population that has no access to business opportunities because of lack of market, inputs and demands, others never reach either the minimal scale or the efficiency necessary to cover costs, many of them also face non-supportive policy frameworks and daunting physical, social, and economic challenges, internal management challenges, and finally replication of successful models has at times proved difficult, due to differences in social contexts and lack of local adoptions. Such sentiments are also in line with beliefs of the traditional banking institutions who consider this group of people being served by MFIs as “too risk to trade with”. However, traditional banking institutions have recently been providing some of the products offered by MFIs to its clients considering that there are many MFIs which have developed to becoming banks.

Such scenarios has set precedence for scholars to conduct studies in this field in order to provide a profound understanding of success factors contributing to a micro-finance institution (MFI) in a developing country. According to Ngumbo, (2012) a key success factor can be a specific skill or talent; a competitive capability and something a firm must do to satisfy customers. MFIs provide various products ranging from cash loans, money transfers, direct deposits, savings and insurance particularly targeting the poor people in the society. MFIs are characterized by short repayment periods graduated increase of loan size, sustainability and non-conventional collateral. Rwanda has a sizeable Small and Micro Enterprise sector which the government is seeking to promote. This sector is estimated to employ 3.2 million people. In spite of this the sector has a problem in accessing financial services.

2. STATEMENT OF THE PROBLEM

The concept of financial innovation is fundamental as it spurs growth of MFIs worldwide. Presently, innovation is a continuous process geared toward providing a wider range of financial products and financial intermediation which is a crucial factor in determining competitiveness and the progress of financial institutions (Mohanty & Panda, 2004). Studies have been conducted to assess whether innovative lending methods promotes financial inclusion in other countries but there few studies which have been done in Rwandan context to assess whether micro finance innovation present opportunities to seize new markets from the unsatisfied or unbanked market segment in Rwanda. Amid the witnessed economic growth, increased population and the technological advancement over the last decade, only a few innovative MFIs have recorded remarkable growth, while the majority has remained sluggish. The Micro Finance Institutions are expected to grow in size, products, merge or have partnerships with other industries geared towards growing firms’ products portfolio, the markets share and the profitability. Although innovation in financial sector is considered as the way to go in as far as financial inclusion is concern, very few studies have been conducted to establish the relationship of these two variables from MFI perspective. Most of the existing studies have repeatedly focused in commercial banks. It is therefore not evident as to whether innovative microfinancing increase financial outreach. This study sought to assess the measures undertaken by MFI in Rwanda to increase their outreach in order to address such challenges of financial inclusivity in Rwanda.

3. OBJECTIVES OF THE STUDY

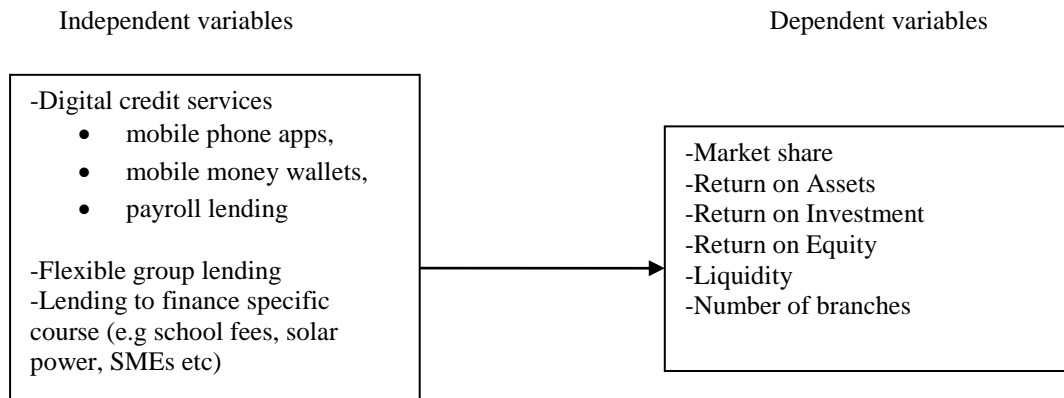
The general objective of this study was to assess the impact of innovative lending methods on the growth of MFI in Rwanda, a case study of Urwego opportunity bank.

The specific objectives were:

- 1) To determine the effects of digital credit services on the growth of Urwego Opportunity bank in Rwanda
- 2) To establish the effects of flexible lending services on the growth of Urwego Opportunity bank in Rwanda

- 3) To determine the contributions of specific course lending methods on the growth of Urwego Opportunity bank in Rwanda

4. CONCEPTUAL FRAMEWORK



5. RESEARCH METHODOLOGY

- **Research Design:** The study used descriptive survey design.
- **Target Population:** The researcher targeted 800 SMEs that are clients of UOB in Nyarugenge district.
- **Data Collection Instruments:** Primary data were collected using questionnaires while secondary data were collected using documented evidence.

6. RESEARCH FINDINGS

6.1 Digital credit services and the growth of Urwego Opportunity bank in Rwanda

The first objective of this study was to assess the specific innovative approaches available in microfinance institutions which are meant to reach out to more clients who do not have

Table1: Innovative products offered inMFI

	Frequency	Percent
Mobile banking	6	54.6
ATMs	2	18.2
Message alerts from the MFI	3	27.3
Total	11	100.0

It was observed that 54.6% of the employees stated that mobile banking is one of the innovative products offered by the MFI to facilitate financial inclusion, 18.2% stated that ATMs are some of the means used by MFI to improve financial inclusion and finally message alerts to customers was rated with 27.3% of the employees as some of the recent innovativeness used to facilitate financial innovation. In general it is observed that mobile phone applications are one of the main products used to reach out to more clients in MFI.

Table2: Urwego Opportunity Microfinance offers their products to the clients using the following methods

	Frequency	Percent
Mobile Banking	2	18.2
Point of Sale-POS	7	63.6
Others	2	18.2
Total	11	100.0

The study established that MFI deliver their products using innovative ways such as easy 24/7 rated at 18%, point of service rated at 63.6% and others such as ATMs, over the counter services rated at 18.2%. There are several more specific motivations for diversifying an MFI's channels beyond the branch: Customer acquisition and retention: penetrating new markets or servicing hard-to-reach areas. Product diversification Customer acquisition and retention: offering valuable products, such as micro-savings and remittances, profitably and efficiently. Operational efficiency: reducing branch congestion and maximizing efficiency of branch tellers and loan officers. Cash reduction: reducing cash in the financial system to save money, provide more transparency, be less vulnerable to fraud risk, and be safer for the client. With few established models even in the retail-banking industry, many of these alternative channels are new to microfinance, and thus a high degree of experimentation is currently underway. It remains to be seen which channels will have the transformational impact described above.

Table3: Highest amount of money which you can transfer using your mobile phone

	Frequency	Percent
Less than 50,000 FRW	54	69.2
100,000 to 200,000 FRW	21	26.9
200,000 to 300,000 FRW	3	3.8
Total	78	100.0

Majority of the clients who consisted of 69.2% stated that the highest amount of money which they can transfer using your mobile phone is any amount less than 50,000 FRW, 26.9% mentioned that they can transact between 100,000 to 200,000 FRW through their phones whereas 3.8% mentioned that they can be will to transfer between 200,000 to 300,000 FRW using their mobile phones. This means that although MFIs are putting up with innovative techniques to ensure that clients gets easy, save and faster products and services, most of the clients are still skeptical closer to significantly serving more of the poor.

6.2 Flexibility of lending services and the growth of Urwego Opportunity bank in Rwanda

Table 4: Measuring the innovativeness of microfinance

	Frequency	Percent
product innovation	4	36.4
process innovation	4	36.4
organizational innovation	1	9.1
marketing innovation	2	18.2
Total	11	100.0

The study indicates that product innovation in MFI is very important in ensuring that they reach out to as many as possible clients. This is evident by the response rated at 36.4% of the respondents who supported it arguing that MFI should be in a position to introduce a new good or service to the market. Another important aspect is process innovation whereby a new production process or methodology should be effective and efficient. This was supported by 36.4% of the respondents who stated that process development is equally important as the product development. A new organization of management was considered by 9.1% of the respondents that it serves a key role in ensuring that the MFI reaches as many clients as possible and this is viewed as an organization innovation. Market innovation is a situation whereby it facilitates a new way of selling your goods or services. This variable was considered as the key measurement needed by MFI in order to extend their outreach by 18.2% of the employee respondents.

Table5: Accessing financial services through innovative ways in MFI

	Frequency	Percent
Easy	9	81.8
Normal	2	18.2
Total	11	100.0

According to 81.8% of the employees of MFI, the condition of accessing finance from their institution is easy whereas 18.2% stated that the process is normal. Low access to formal credit among rural households and microenterprises, and the widening income gap between rural and urban households, MFIs are now taking several innovative measures to increase the supply of credit and access to finance to a large population.

Table6: Accounts opening per day averagely

	Frequency	Percent
Less than 5 Accounts	2	18.2
5 - 10Accounts	2	18.2
Above 10 Accounts	7	63.6
Total	11	100.0

The study indicates that 63.6% of the employees stated that MFI records more than 10 accounts opening each day. This is an impressive sign which shows that in average these instructions are expanding tremendously. The number of people gaining access to financial services climbed steadily, while microfinance became increasingly commercialized and transformed into a more and more financially efficient industry. Sustainability of market growth was rarely questioned during that time.

Table7: Number of transactions per day

	Frequency	Percent
Less than 10	1	9.1
10 – 20	6	54.5
Above 20	4	36.4
Total	11	100.0

The study reveals that more than 90% of the employees stated that in average, the transaction they make cannot come below 20. Microfinance has long been considered a powerful tool for sustainable development. The idea of granting loans at fair conditions to alleviate financial constraints of the poor has gained widespread acceptance among academics, investors and the public sector alike. The market for microcredit has expanded over many years, with microfinance institutions (MFIs) extending loans to many clients in Rwanda.

Table8: Level of financial outreach in rural areas

	Frequency	Percent
Very high	2	18.2
High	7	63.6
Low	2	18.2
Total	11	100.0

The study shows that 18.2% of the employees stated that the level of financial outreach in rural areas is very high, 63.6% stated that it is high and 18.2% mentioned that it is low. In average, financial outreach in rural areas is considered to be high.

Table9: Level of financial outreach in urban areas

	Frequency	Percent
High	1	9.1
Moderate	7	63.6
Low	3	27.3
Total	11	100.0

The study indicates that 9.1% of the employees believe that MFI outreach in urban areas is high, 63.6% stated that it is moderate and 27.3% mentioned that it is lower as compared to the rural areas.

Table10: Model of reaching out to customers in MFI

	Frequency	Percent
Individual business customers	2	18.2
Women	2	18.2
Youth	7	63.6
Total	11	100.0

It was observed that 18.2% of the respondents stated that majority of the customers of MFI are individual businessmen, 18.2% stated that they are women and 63.6% stated that they are youth. This is because Urwego Opportunity has several products such as SME business loan product. The product targets individual SME customers to meet their working capital needs. Another type of product is salary loan product. This product targets people in gainful employment for personal development whose loan repayment is through check off by the employer. Standing order loan product targets people in gainful employment for personal development whose loan repayment is through monthly standing orders. Back to school loan product is designed to meet the education needs of our customers. Asset financing loan product is for the purpose of purchasing business and household assets. Business training service is provided to customers to bridge the existing skill gaps in business management.

6.3 Specific course lending methods and the growth of Urwego Opportunity bank in Rwanda.

Table11: Descriptive Statistics showing the quality of using agent banking in MFI

	Mean	Std. Deviation
Urwego Opportunity Innovative Microfinance services are effective and efficient	1.82	.874
It is easy to make withdrawal and deposit in Urwego Opportunity Microfinance due to its innovative products	1.55	.522
It is easy to check balance using Urwego Opportunity Microfinance	1.27	.467
Opening an account is very easy using Urwego Opportunity Microfinance	1.91	.944
Urwego Opportunity Microfinance services are very quick	1.36	.505
Innovative products in Urwego Opportunity Microfinance are error free records	1.45	.522
Urwego Opportunity Microfinance agency systems are online 24 hours a day	1.45	.522
Urwego Opportunity Microfinance innovative products are secured	1.45	.522
Urwego Opportunity innovative Microfinancing systems are time saving	1.45	.522
Valid N (listwise)		

The study used a Likert scale to rate the above five variables such that those who indicates that they strongly agree would be indicated by a mean of (0-1.5), agree (1.6-2.4) Neutral (2.5-3.5) disagree (3.6-4.4) and strongly disagree (4.5-5.0). The statistics indicates that in average majority of the respondents agreed that Urwego Opportunity Innovative Microfinance services are effective and efficient having rated with a mean of 1.82 and a heterogeneous standard deviation of .874. Similarly majority of them also agrees that it is easy to make withdrawal and deposit in Urwego Opportunity Microfinance due to its innovative products as indicated by a mean of 1.55 and a heterogeneous standard deviation of .522. Strongly agreed that it is easy to check balance in their accounts at Urwego Opportunity because the Microfinance as shown by a man of 1.27 and a heterogeneous standard deviation of .467. Majority of them agreed that opening an account is very easy using Urwego Opportunity Microfinance having rated with a mean of 1.91 and a heterogeneous standard deviation of .944. regarding the issues such as quick access to MFI services, error free records innovative services, 24hour online services, security of innovative products and time saving, majority of them agreed normally as

indicated with a mean ranging from 1.36 and 1.45 with heterogeneous standard deviation ranging from .505 and .522 respectively.

Table12: Descriptive Statistics showing the of MFI innovative products

	Mean	Std. Deviation
We are planning to introduce agency banking because customers are to transacting amount below frw 100,000at their nearest agent	1.36	.674
Customers are familiar with the agency banking systems	1.36	.505
Customers prefer agency banking more than other mode of financial services	1.36	.809
Most of customers approach agency when banks and SACCOs have closed	1.00	.000
Valid N (listwise)		

The study indicates that in average majority of the employees strongly agreed with the statements that We are planning to introduce agency banking because customers are to transacting amount below frw 100,000at their nearest agent, customers are familiar with the agency banking systems, customers prefer agency banking more than other mode of financial services and also Most of customers approach agency when banks and SACCOs have closed. This is indicated by a mean of 1 and 1.36 respectively and heterogeneous standard deviation of .674 and .000 respectively. This implies that agency banking is important aspect needed to consider in microfinance institutions for the purpose of financial inclusion.

Table 12: Descriptive Statistics showing the importance of mobile banking for financial inclusion in MFI

	Mean	Std. Deviation
Mobile banking is very safe way of handling money	1.36	.505
It take very little time to withdraw or deposit money	1.36	.505
One can deposit of withdraw money without necessarily going to the MFI	1.36	.505
In case there is a mistake in transferring money it can be reversed and the money is recovered	1.36	.505
Strategies to increase mobile banking in MFI	1.18	.405
Valid N (listwise)		

The study indicates that for MFI to actually make an impact in terms of customers outreach, one of the important thing to factor in is the used of mobile phones. This can allow a customer to access mobile banking services through his/her phone. Majority of the respondents strongly agreed that mobile banking is very safe way of handling money, It take very little time to withdraw or deposit money, One can deposit of withdraw money without necessarily going to the bank, In case there is a mistake in transferring money it can be reversed and the money is recovered and lastly strategies to increase mobile banking in MFI.

Table13: Correlations between financial inclusion and outreach in rural areas

		Level of financial outreach in rural areas	Model of reaching out to customers in MFI
Urwego Opportunity Innovative	Pearson Correlation	.657*	.629*
Microfinance services are effective and efficient	Sig. (2-tailed) N	.028 11	.038 11
It is easy to make withdrawal and deposit in your place due to its innovative products	Pearson Correlation nearSig. (2-tailed) N	.603* .050 11	.702* .016 11

The study shows that there is a positive correlation between the innovative MFI approaches and financial outreach in rural areas. The study shows that since Urwego Opportunity Innovative Microfinance services are effective and efficient, the institution is able to reach the rural clients as shown by the Pearson Correlation of .657* which is significant at a p-value of .028. This also contributes in enabling rural residents an easy process to make withdrawal and deposit in Urwego Opportunity Microfinance. This is indicated by a Pearson Correlation value of .603* which is significant as indicated with a p-value of .050. This means that majority of the people in rural areas are not supposed to travel for distance to access financial services by visiting the MFI offices to transact their businesses. Another aspect which shows a positive correlation is the model which MFI uses to reach to its customers. Innovation has increased the efficiency and effectiveness of offering services to youth and women in various parts of the country and have also facilitate proximal access to financial services to those who were locked out of financial services by the traditional banks.

7. CONCLUSIONS AND RECOMMENDATIONS OF THE STUDY

7.1 Conclusions

Rarely a day goes by without someone mentioning how financial inclusion can be boosted by new delivery channels, such as ATMs, banking agents, and mobile phones. Yet for all the talk about reaching the “unbanked” and other low-income groups, it is banks, mobile operators, and retailers that have been experimenting with new delivery systems to reach the poor. As the group that is closest to the niche segment, microfinance institutions (MFIs) seem conspicuously absent from the discussion. This study intended to unveil the importance of innovative products on financial inclusion by assessing it through the perspective of MFI.

Poor people need a variety of financial services, not just loans. In addition to credit, they want savings, insurance, and money transfer services. It is clear from this study that the poor benefit more from a wider range of options in financial services. MFIs have tried to diversify risks and develop new business lines where traditional banks used to refer to a risk group to invest into. The advances and refinements in lending technologies in microcredit as well as in mobile banking MFIs can be applied in other financial services for the poor.

One of the challenges is that other functions, such as risk management, branch operations, or marketing, alternative channels is a relatively new field, even in the banking sector. There are few reference points, especially in the microfinance sector, and even fewer success stories—and almost none are widely communicated across borders or regions. This means that senior executives at MFIs often have an incomplete understanding of alternative channels and how they might fit in their businesses and unclear ideas of what benefits they may bring.

7.2 Recommendations

1. To put much attention into the technological innovation, infrastructure building, institutional development, and human capital formation which directly increase the productivity and human resources.
2. To ensure an appropriate regulatory and prudential framework for the market of Microfinance including capital adequacy ratios, asset quality indicators and unsecured loan limits.
3. To provide a specialized credit bureau for Microfinance that can help financial institutions to have necessary information on clients in order to minimize risks.
4. To introduce agency microfinancing since this model is popularly used by commercial banks to reach out to their clients and also clients are familiar with it.

7.3 Suggested areas for further research

The study recommends that other researchers should concentrate in the following areas related to this study:

- To assess the contributions of alternative banking channels on the development of SME businesses especially those which have been given authorization to deal with agent banking
- To analyze the Relationship of microfinance services and products and the performance of commercial banks in the Rwandan market
- To assess the contributions of financial innovation in commercial banks on the growth of microfinance institutions in Rwanda

REFERENCES

- [1] Florida, R. (2012). *The rise of the creative class: and how it's transforming work, leisure, community, and everyday life*. Melbourne: Pluto Press Australia
- [2] Florida, R. (2014). *The flight of the creative class: the new global competition for talent*. New York: Harper Business.
- [3] Glaeser, E. L. (2013). The new economics of urban and regional growth, in G. Clark, M. Feldman, and M. Gertler, Eds. *The Oxford Handbook of Economic Geography*. Oxford: Oxford University Press, 83-98.
- [4] Glaeser, E. L. (2015). Review on Richard Florida's *The Rise of the Creative Class*.
- [5] Junarsin, J. E. (2015). *Learning experience in creativity: a reflective essay*. Assignment paper, the Australian National University, Australia.
- [6] Lang, R. E. (2015). Review Roundtable: Cities and the creative class/discussion/response. *Journal of the American Planning Association* 71 (2): 203-220.
- [7] Martins E.C and Terblanche F. (2000) "Building organizational culture that stimulates creativity and innovation". University of South Africa.
- [8] Rose, P. S., Marquis, M. H. (2009). *Money Market and Capital Market, Financial Institutions and Instruments in a Global Marketplace*. New York: McGraw Hill.
- [9] Sawicki, D. 2003. The rise of the creative class: and how it's transforming work, leisure, community, and everyday life. *Journal of the American Planning Association* 69 (1): 90
- [10] Teslurk, P.E., Faar, J.L And Klein, S.R. (1997). "Influence of Organizational Culture and Climate on Individual Creativity" *The Journal of Creativity Behavior* Vol. 31 No.1 pp. 21-41
- [11] Tushman and O'Reilly, C. (1989) "Corporation culture and commitment: motivation and social control in organizations". *California Management Review Summer*, pp. 9-15
- [12] Hannig, A., & S. Jansen. (2010). *Financial Inclusion and Financial Stability: Current Policy Issues*. ADBI Working Paper 259. Tokyo: Asian Development Bank Institute. Available: <http://www.adbi.org/working-paper/2010/12/21/4272.financial.inclusion.stability.policy.issues/>
- [13] Ledgerood J. (2009) *Microfinance Hand Book. An institutional and financial perspective. Sustainable banking with the poor*.
- [14] Surbhi S. (2015) Difference Between Microcredit and Microfinance <http://keydifferences.com/difference-between-microcredit-and-microfinance.html#ixzz4KsIDHGbZ>
- [15] Salahuddin M. and Rashmi, (2015) Rotating Savings and Credit Association: An Alternate of financing Among Low Income Households, Abhinav National Monthly Refereed *Journal of Research in Commerce & Management*, Vol. 4, Issue 3,
- [16] Rusdy Hartungi, (2007) "Understanding the success factors of micro-finance institution in a developing country", *International Journal of Social Economics*, Vol. 34 Iss: 6, pp.388 – 401
- [17] Boysen V. and Sahlberg R. (2010) Key success factors of Grameen Bank. A case study of Strategic cultural and structural aspects. *Lund University School of Economics and Management*
- [18] Lasagni A. & Lollo E. (2011) Participation in Rotating Savings and Credit Associations in Indonesia: *New Empirical Evidence on Social Capital*
- [19] Deelen L & Majurin E. (2008) Village banking in Lao PDR: handbook for village bank management committees and support organizations ILO Subregional Office for East Asia. – Bangkok: ILO, 74 p.
- [20] Westley G. (2004) *A Tale of Four Village Banking Programs: Best Practices in Latin America*.