
Transaction Costs and Choice of Best Credit Governance Structure of Commercial Banks in Tanzania.

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Abstract

The paper analysed transaction costs as determinants of the best credit governance structure (CGS) for scaling up of commercial banks credit operations in Tanzania. Primary data were collected from 37 registered and licensed commercial banks in January 2018. The main sources of secondary data were peer reviewed journal articles on transaction cost economics, governance structures (especially those of pioneers of New Institution Economics, Oliver Williamson and Ronald Coase) and Bank of Tanzania annual reports. Structured questionnaires for the survey on transaction costs (Information Search Costs, Credit Contracts Negotiation costs and Credit Contracts Enforcement Costs) associated with commercial banks credit transactions were administered to 204 respondents. Data were captured and analysed quantitatively through binary and multinomial regression models due to dichotomous nature of the dependent variables (Credit distribution channels). Transaction costs as predictors were used to establish a choice of preference between direct and indirect channels for credit distribution. Key findings identified direct channel for credit supply as the best for commercial banks credit supply to urban based customers since transaction costs can be well mitigated. Also commercial banks credit scaling up must involve distribution channels with intermediaries, given non-conducive credit business environment in rural areas. The current study recommends to the government of Tanzania to make tangible socio-economic

development in rural areas; such developments will greatly reduce the need for commercial banks to invest in infrastructures in rural areas. This will cut down transaction costs, allowing the scaling-up of commercial banks credit operations and facilitate accessibility of credit facility to the majority who are in need.

Keywords: *Transaction cost, Credit Governance Structure, Commercial Banks.*

1.0 Introduction

Transaction cost is an important determinant of choice of the best credit governance structure of commercial banks in Tanzania. As suggested by Williamson (2010), in his analysis of transaction cost economics theory, where transaction cost is too high, beyond acceptable levels, there may not be transaction at all. Such behaviour is portrayed by commercial banks in Tanzania, where most of them provide credit services to urban based customers and making the marginalized rural based customers victims of high transaction costs.

Tanzanians who live in the rural areas have no access to financial services of commercial banks. Information gap between commercial banks and rural based borrowers was a major setback on commercial banks behaviour of dealing directly with individual borrowers, resulting in high transaction costs. High transaction costs prevent commercial banks from providing credit services to rural based borrowers, and thereby negatively affecting both commercial banks and rural based population, (Financial sector deepening trust- FSDT, 2017).

Since liberalization of the banking industry in Tanzania in 1991, the commercial banks mostly preferred to directly deal with customers as far as credit provision services is concerned. This tendency resulted in limited credit supply from commercial banks to the most parts of the country, especially to rural areas due to inability to manage the associated credit transaction costs as reported by AgFiMS (2011). Major challenges in rural finance in Tanzania relate to information gaps which fall into three categories: (i) Knowledge of rural demand and market segmentation by financial institutions; (ii) Financial illiteracy of rural borrowers; (iii) Commercial banks knowledge of the best channels/methods for penetration to rural based market at low transaction costs (TCs), (FSDT 2017).

Information is a key input that goes into the credit decision of commercial banks. One of the challenges for commercial banks is to acquire information about the credit risk of the borrower, as borrowers have more information than the lender about the projects (Myers & Majluf, 1984). According to Transaction Cost Economic Theory, the banks are not interested in offering credit to micro, small and medium enterprises (MSMEs), farmers and poor households because of information asymmetry resulting to high screening costs, credit contracts negotiation costs, monitoring and enforcement costs.

Under asymmetric information conditions, commercial banks are uncertain about the future behaviours of the borrowers in terms of repayments. High transaction costs problems are more likely to occur when commercial banks deal with MSMEs, farmers and poor households especially in rural areas of developing countries due to higher opacity (Berger et al.2001; Beck et al.2004; Hyytinen & Pajarinen, 2008; Cole 2004). By opaqueness means, it is difficult to ascertain if borrowers have the capacity of paying (have viable project) and or willingness to pay (due to moral hazard) (Beck, 2010). Information asymmetry between borrowers and the commercial banks is reflected in the inability of the majority of rural based borrowers to provide up to date reliable financial information and realistic business plans, which increases credit transaction costs. This consequently, limits the ability of the banks to assess credit-worthiness of individual borrowers. And therefore the commercial banks believe to be better-off with some few known credit worth urban based customers, (Kessy and Temu, 2010).

The argument of information asymmetry is supported by (Olomi 2009) and (Kibassa 2012) who emphasized that poorly compiled records and financial accounts coupled with inability of rural based borrowers to properly express their knowledge about business opportunities aggregates the lack of adequate information by the commercial banks and therefore , increasing credit transactions costs, when dealing with rural based borrowers in Tanzania. Satta (2006) amplifies this argument by pointing out lack of adequate and reliable collateral, lack of appropriate instrument to manage risk, not being familiar with complicated information about rural based borrowers and perceived risks make commercial banks in Tanzania become unwilling to provide the much-needed finance particularly to rural based borrowers.

With an appropriate choice of a credit governance structure (CGS) as determined by transaction costs, commercial banks will be able to penetrate the rural based market, and small and emerging commercial banks will be able to enter into credit supply business. This will increase competition, credit accessibility and in turn lower borrowing interest rates, (Mkenda and Campenhout, 2011), Unfortunately, the environment for commercial bank's credit operation is not conducive due to inadequate infrastructure for smooth banking operations, difficulties in identification and accessibility of information for potential borrowers and the nature of customers (who want many but small sized credits). Bureaucratic procedures and red tapes by village and district councils, lack of collateral or collateral of low market values are some of the barriers that make banking operations in URT very costly and inefficient, especially for small private commercial banks, (BOT, 2011).

The liberalization of the banking industry in 1991 aimed at allowing many private commercial banks to enter the industry thus increasing competition in the provision of banking services, namely, credit service, increases accessibility to the banking services by many, lowering banks credit interest rates and ultimately eliminating monopoly of three banks CRDB, NBC and NMB within the industry. Currently, the environment is still not conducive to allow efficient operations for most of the private commercial banks to provide credit services in most parts of the country especially rural areas due to high transaction costs as suggested in Tanzania banking sector performance report of 2010, (BOT, 2010).

Recent studies on efficiency of commercial banks in Tanzania focused on conventional approaches of measuring efficiency and performance through analysing the banks' profitability, repayment rates, accessibility to services, geographical coverage, transformational and or operational costs, interest rates, the number of borrowers, productivity and portfolio quality (Wangwe, 2004; Aikaeli, 2008; Ernst & Young, 2010; Serengeti, 2012). This study focused on transaction cost as the determinants of efficient CGSs of commercial banks in Tanzania, for credit operations scale-up purpose. Other previous studies on the application of transaction costs on Credit Governance structures (CGS) focused on the demand for credits and not on the supply side. For example, Ngaruko (2008) focused on how economic reforms of Tanzania influenced diversity characteristics

of farmers, their farm investment and ultimately their demand on agro-credits. The analysis of this study was made through the application of transaction costs theory. Mkenda and Campenhout (2011) conducted a research on the estimation of transaction costs in Tanzania supply chain focusing on commodity exchange of agricultural products. This study focused on how transaction costs determine the best CGS of commercial banks in Tanzania.

The current study was guided by Transaction Cost Economics Theory (TCE) which focuses on the organization of transactions that occur whenever a good or service is transferred from a provider to a user across a technologically separable interface. When transactions occur within an organization, the transaction costs can include managing and monitoring personnel and procuring inputs and capital equipment. The transaction costs of buying the same good or service from an external provider can include the costs of source selection, contract management, performance measurement, and dispute resolution. Thus, the organization of transactions, or “governance structure,” affects transaction costs as pointed out by Williamson (1989). Therefore, TCE represents another approach to studying institutional arrangements.

2.0 Methodology

The current study adopted the quantitative paradigm. The study utilized quantitative and statistical aspect of data organization, presentation and analysis through figures, numbers and tables. Both primary and secondary data were collected. Structured questionnaires for the survey of transaction costs associated with commercial banks credit transactions were administered to 204 commercial banks credit officers for primary data collection. For secondary data, the study used peer reviewed journal articles on transaction cost economics and governance structures, financial sector supervision and annual reports from the Bank of Tanzania (BOT).

The targeted population was all registered and licensed commercial banks in Tanzania by January 2018 where the targeted sampling unit was commercial bank’s credit officers. Due to inability to determine the sampling frame since the

population (all employees from commercial banks with knowledge and experience in administration and control of credit distribution) was not reliably known, a non-probabilistic sampling method and a purposive sampling technique were used. Only the respondents with credit administration knowledge and working under credit department of commercial banks were included in the sample of 204 respondents. G power software was used in calculating the sample size since the population was not known with reliability. Input parameter in G power were, α err prob= 0.05, power (1- β err prob) = 0.8, odd ratio = 0.6, two tail test, normal distribution and the output result for the sample size is 204

The study was carried out in Dar es Salaam and Zanzibar only because all commercial banks had their headquarters in Dar es salaam and Zanzibar. A sample of 204 credit officers from 37 registered and licensed commercial banks that provided credit services to micro, small and medium enterprises and farmers were involved in the study. As a requirement of Bank of Tanzania, all information related to credit operations of commercial bank branches must as well be consolidated to their head offices for submission to credit reference bureau (CRB). Therefore, this study was not extended to other regions since the amount and quality of data captured in these banks' headquarters (Dar es Salaam and Zanzibar) was satisfactory. At the time of the study, January 2018, all commercial banks in Tanzania had their headquarters in Dar es salaam with exception of the People's Bank of Zanzibar and they amounted to 37 registered and licensed commercial banks.

This study used both binary and multinomial logistic regression. Binary logistic regression was used to assess the likelihood of commercial banks of choosing a particular Credit Governance structure (CGS) and not any other given the Transaction Costs. Every CGS (1-4) was equated as a function of transaction costs. Multinomial logistic regression was also used to predict the choice of an efficient CGS. Where the dependent variable has four different options (CGS1-CGS4) matched against categories of transaction costs, at each time, one option of dependent variable was set as a reference category. Given a sample of (X, Y) pairs in logistic regression, the X's can be numerical or categorical, but Y's are generally coded as 0 (for those which do not have the event) or 1 (for those which have the event). According to Bryman and Cramer (1990), the logistic model is

based on a linear relationship between the natural logarithm (ln) of the odds of an event and a numerical independent variable. The form of this relationship is as follows:

$$L = \ln (P/1-P) = \beta_0 + \beta_1 x + \epsilon_i$$

Where Y is binary and represent the event of interest (response), coded as 0/1 for failure/success,

P is the proportion of successes,

O is the odds of the event,

L is the ln (odds of event),

X is the independent variable,

0 and 1 are the Y-intercept and the slope, respectively, and ϵ_i is the random error. Computations of the estimates of β_0 and β_1 in logistic regression are far more complicated, P is the probability of the event, and then the odds of the event are:

$$\text{Odds} = O = P / 1-P$$

We defined $L = \ln (\text{odds of event } Y)$, sometimes called the “log odds” or logit of Y.

We can write L in terms of P, Probability ($Y=1$), as follows:

$$L = \ln (O) = \ln (P/1-P)$$

The logistic regression model may be written in terms of P, the risk of event Y, assuming that L is a linear function of X as follows:

$$P = e^{\beta_0 + \beta_1 x + \epsilon} / 1 + e^{\beta_0 + \beta_1 x + \epsilon}$$

Current study used logistic regression method for analysis, where transaction costs were predictors while credit governance structures (CGSs) were dependent variables (dichotomous). This tool assessed the likelihood of commercial banks choosing a particular CGS and not any other given the Transaction Costs. Every CGS (1-4) was equated as a function of transaction costs (TC). This means each TC category (TSC, TNC and TEC) was tested against each CGS to determine the likelihood of choosing or not choosing a particular CGS. Thus, for each TC tested across four CGS (CGS1-4), the most cost efficient governance structure was

revealed and recommended for scaling up. The mathematical representation of the above is,

Whereby; $TC = (TSC + TNC + TEC)$

And

$$CGS(1 - 4) = f(TSC, TNC, TEC)$$

TSC includes but not limited to transport, meetings, village authority fees, reputation, personal relationship and time spent in searching and screening the borrower. **TNC** includes but not limited to the cost of lawyers, allowances for meetings, paperwork, personal relationships, transport costs, levies, opportunity cost of the time spent in negotiation, reputation and **TEC** costs include but not limited to penalties, enforcement campaigns, police and court case costs, time for making follow ups, the costs of lawyers and reputation. Binomial logistic regression gave binary outcome. For example, 1 meaning success and 0 failure when predicting whether a CGS has been chosen or not based on TSC, TNC and TEC. The logistic regression model gives the likelihood that, given CGS's TSC, TNC, TEC, that they are chosen (in this example, the higher the probability, the greater the chance for the CGS to be chosen). Again, the number of coefficients were obtained, but this time were used to calculate a LOGIT.

$$\text{Logit of } CGS(1 - 4) = \text{intercept} + aTSC + bTNC + cTEC + \varepsilon$$

Usually, ε is equated to 0 since focus is on TSC (search costs), TNC (negotiation costs) and TEC (enforcement costs) as parameters used to predict the likelihood of choosing a particular CGS. Therefore;

$$\text{logit}(p) = \log\left(\frac{p}{1-p}\right)$$

Thus;

$$p = \frac{1}{1 + e^{-(\text{logit})}} \dots$$

Thus, the model was fitted, values for a, b, c and the intercept obtained and the logit value was calculated from the given data. Thus, the probability P was calculated and established the chances (likelihood) of choosing a particular CGS.

Multinomial logistic regression was also used to predict the choice of an efficient CGS. Where the dependent variable has four different options (CGS1-CGS4) matched against categories of transaction costs, at each time, one option of dependent variable was set as a reference category. As Agresti (1990) explained, the multinomial Logistic Regression is the linear regression analysis conducted when the dependent variable is nominal with more than two levels. Thus it is the extension of logistic regression, which analyses dichotomous (binary) dependents. Multinomial logistic regression analysis assumed that, all four credit governance structures (CGS1-CGS4) existed, but at each time the analysis was made, one CGS was used as a reference category and determined the CGS more likely to be selected given the transaction costs.

3.0 Results and discussion

3.1 Transaction Costs and Choice of credit governance structures

This section critically analysed the effects of transaction costs on the choice of the best credit governance structure model of credit supply by commercial banks. Each model of CGS used similar predictors (Total search costs (TSC), Total negotiation costs (TNC) and the Total enforcement costs (TEC)) in determining whether to select or not, while assuming other CGSs did not exist. This study, matched each credit governance structure against the total transaction costs (total information search costs, total credit contracts negotiation costs and the total credit contracts monitoring and enforcement costs), to determine the likelihood of such particular CGS to be selected given the transaction costs. The Binary logistic regression was used for analysis.

Table 3.1 Transaction Costs and Choice of credit governance structures

CGS1	Variables	B	S.E.	Wald	Df	Sig.
	TSC	1809400	.000	14.092	1	.000
	TNC	-2228200	.000	7.950	1	.005
	TEC	21225000	.000	9.261	1	.002
	Constant	-2.903	.943	9.475	1	.002
CGS2	Variables	B	S.E.	Wald	Df	Sig.
	TSC	-13474000	.000	.465	1	.495
	TNC	57080000	.000	3.382	1	.066
	TEC	- 5679000000	.000	.018	1	.894
	Constant	-.854	.535	2.546	1	.111
CGS3	Variables	B	S.E.	Wald	Df	Sig.
	TSC	-181150	.001	28950	1	.986
	TNC	-225130	.002	10742	1	.992
	TEC	-1841500	.000	24478	1	.988
	Constant	202.027	12150	27655	1	.987
CGS4	Variables	B	S.E.	Wald	Df	Sig.
	TSC	-30662000	.000	1.069	1	.301
	TNC	-21724000	.000	.398	1	.528
	TEC	-18273000	.000	5.800	1	.016
	Constant	3.235	.668	23.431	1	.000

From the results in Table 3.1, when the log-odds units of TSC and TEC were increasing the log-odds units of TNC was decreasing, influencing the likelihood of commercial banks to supply credits directly to borrowers only without using any other credit governance structure. All predictor's variables (TSC, TNC and TEC) were very significant at 5per cent. The likelihood of commercial banks to supply credits through profits intermediary banks without using any other channel of credit distribution was highly influenced by a decrease of both TSC and TEC and a

decrease of TNC. Thus, TNC was significant at 7 per cent, the remaining predictor's (TSC and TEC) were not statistically significant.

If the choice of a direct channel for credit supply was made and not any other channels, despite that TSC and TEC were rising, the commercial banks were able to absorb all the costs. This is because all the predictors significantly influenced the likelihood of credit supply through direct channel. The likelihood of selecting other indirect channels requires TSC and TEC to be decreasing for commercial banks to absorb. Credit operating environment in urban areas is conducive, thus minimizing credit transaction costs. Therefore, direct channel is the best for the credit supply by commercial banks in urban areas since TCs can be well mitigated. Commercial banks credit scale up must involve CGSs with intermediaries, given the unsuitability of credit business environment in the rural areas.

The study observation are consistent with the observation by Yunus (1998) that high transaction costs associated with credit provision to rural areas are a result of information asymmetry. This is why commercial banks do not want to provide credit services to rural areas of Tanzania. The study findings reveal further that, not only information asymmetric caused high transaction costs but also the unsuitable nature of rural environment of Tanzania which is characterized by poor infrastructure (remoteness). unclear political will and commitment towards rural development, high illiteracy rate, poor traditions and customs (cultural barriers).

New and emerging commercial banks are also concentrating on urban borrowers; they are not interested in scaling up their credit operations to rural areas. The fundamental theory that guides the current study is the 'Transaction Cost Economic Theory.' According to this theory, when transaction cost is too high, there will be no transaction at all. And therefore the parties to such a transaction that did not take place are considered inefficient in transaction costs terms. The current study findings are inconsistent with the prepositions given out by Oliver Williamson (2000, 2001 and 2010) through the transaction costs economic theory since most commercial banks in Tanzania that failed to transact credit with the rural based customers were considered inefficient in transaction costs terms.

3.2 Multiple credit governance structures (CGSs) with reference category

Multinomial logistic regression used all four CGSs. In the analysis, one credit governance structure at each time was a reference category. The likelihood is reflected by the log-odds units of predictor variables (TSC, TNC and TEC). Thus, the best CGS given transaction costs was determined from three remaining CGSs. When assuming commercial banks were not giving credits directly to borrowers (CGS1), when TSC increased, and when TNC and TEC decreased the influence, the likelihood of commercial banks supplying credits through profit intermediary banks (CGS2), profit intermediary microfinance institutions (CGS3) or through non-profit making intermediaries (CGS4) is influenced by an increase in TSC while TNC and TEC were all decreasing. Despite TCs having similar effect on the choice of CGSs, their significance levels differ. TCs significantly influenced the likelihood of credit supply from commercial banks through profit intermediary banks (CGS2) whereas TSC and TEC were all significant at 5 per cent.

The likelihood of commercial banks distributing credits directly to borrowers (CGS1), through profit making microfinance institutions (CGS3) or through non-profit making intermediaries (CGS4) is similarly influenced by the same condition of a decrease in TSC and an increase in both TNC and TEC. This was when commercial banks channels for credit distribution through profit intermediary banks (CGS2) were assumed as non-existing. The significance level of TCs influence on the likelihood of choosing credit supply channel differs among CGSs.

TSC and TEC were 5 per cent significant when credits were directly distributed to borrowers. When credits were distributed through profit making microfinance institutions, TSC was significant at 6 per cent and TEC at 5 per cent. When credits were distributed through non-profit intermediaries, transaction costs had no significant influence. Thus, the transaction costs significantly influenced the likelihood of commercial banks distributing credits directly to borrowers and through profit making microfinance institutions than through credit distribution or through non-profit making intermediaries. Nonexistence of credit supply channel through profit making microfinance institutions (CGS3), a decrease of

TSC and an increase of TEC, influenced the likelihood of commercial banks credits to supply directly to borrowers. A decrease of TSC and a decrease of both TNC and TEC influenced the likelihood of credit supply through profit intermediary banks. Likelihood of choosing channel for credit supply through non-profit making intermediaries was also influenced by an increase in TSC and a decrease in both TNC and TEC. Among the above three choices of credit supply channels, transaction costs significantly influenced credit supply through profit intermediary banks compared to any other channels, where TSC was significant at 6 per cent and TEC at 5 per cent.

Table 3.2 Multinomial regression results for choice of CGSs

Variables		B	Std. Error	Df	Sig.	Exp(B)	
CGS2	TSC	1373600	.000	1	.026	1.000	CGS1 reference category
	TNC	-1001500	.000	1	.191	1.000	
	TEC	-28226000	.000	1	.016	1.000	
CGS3	TSC	17663000	.000	1	.539	1.000	
	TNC	-28755000	.000	1	.411	1.000	
	TEC	-288830000	.000	1	.638	1.000	
CGS4	TSC	69673000	.000	1	.261	1.000	
	TNC	-68023000	.000	1	.269	1.000	
	TEC	-21231000	.000	1	.122	1.000	

Variables		B	Std. Error	Df	Sig.	Exp(B)	
CGS1	TSC	-1373600	.000	1	.026	1.000	CGS2 reference category
	TNC	1001500	.000	1	.191	1.000	
	TEC	28226000	.000	1	.016	1.000	
CGS3	TSC	-1196900	.000	1	.056	1.000	
	TNC	71391000	.000	1	.360	1.000	
	TEC	25338000	.000	1	.036	1.000	
CGS4	TSC	-67684000	.000	1	.298	1.000	
	TNC	32123000	.000	1	.705	1.000	
	TEC	699480000	.000	1	.628	1.000	

Variables		B	Std. Error	Df	Sig.	Exp(B)	
CGS1	TSC	-17663000	.000	1	.539	1.000	CGS3 Reference Category
	TNC	28755000	.000	1	.411	1.000	
	TEC	288830000	.000	1	.638	1.000	
CGS2	TSC	1196900	.000	1	.056	1.000	
	TNC	-71391000	.000	1	.360	1.000	
	TEC	-25338000	.000	1	.036	1.000	
CGS4	TSC	52010000	.000	1	.411	1.000	
	TNC	-39268000	.000	1	.538	1.000	
	TEC	-18343000	.000	1	.191	1.000	

Variables		B	Std. Error	Df	Sig.	Exp(B)	
CGS1	TSC	-70004000	.000	1	.258	1.000	CGS4 reference category
	TNC	68298000	.000	1	.267	1.000	
	TEC	21187000	.000	1	.123	1.000	
CGS2	TSC	67711000	.000	1	.298	1.000	
	TNC	-32162000	.000	1	.705	1.000	
	TEC	-699710000	.000	1	.628	1.000	
CGS3	TSC	-51541000	.000	1	.415	1.000	
	TNC	38860000	.000	1	.542	1.000	
	TEC	18464000	.000	1	.188	1.000	

A decrease of TSC and an increase of TNC and TEC influence the likelihood of commercial banks distributing credits both directly to borrowers and through profit making microfinance institutions. An increase in TSC and a decrease in both TNC and TEC influence the likelihood of a credit supply through profit

intermediary banks. The effects of transaction costs (TSC, TNC and TEC) on these choices had no significant influence on the likelihood of choosing them.

According to these findings, for efficient credit operations of commercial banks and scaling up of credit operations to both rural and urban areas, multiple credits governance structures must be used. Credit supply through profit intermediary banks was efficient when direct channel for the credit supply was not used. Direct and indirect supply channels for credit distribution through profit making microfinance institutions were efficient when indirect channel for credit supply through profit intermediary banks was not used. Similarly, credit distribution through profit intermediary banks was efficient when, credit distribution channel through profit making microfinance institutions was not used.

Formal financial institutions, particularly commercial banks are very sensitive to risks and high costs. Majority of Tanzanians especially those in serious need of credits live in rural areas. Such areas are very underdeveloped in terms of infrastructure. Thus, lack of effective National identification system and poor planning of towns and cities also make it difficult to locate and identify credit customers and even too costly to acquire their information and hence impose huge risks to commercial banks giving credits to most people in need.

In addition, majority of Tanzanians lack business and financial management knowledge, skills and commitment as a result, they usually divert the use of credits given, leading to high risks of defaults and non-repayments of credits. Normally commercial banks tend to avoid giving credits in such circumstances because they are not ready to incur high costs to provide financial and business management trainings to credit customers. These reasons make the costs of transacting credits too high and renders commercial banks inefficient in terms of credit transaction costs since they cannot absorb such costs, thus they chose not to provide credit services at all, especially to rural based customers.

Scholars (i.e., Hyytinen and Pajarinen, 2008; Temu, 2009; Olomi, 1998; Baker, 1984), all agreed that, the main source of high credit transaction costs is information asymmetry between lenders and borrowers. Under asymmetric information

conditions, commercial banks are uncertain about the future behaviour of the borrowers in terms of repayments. Information asymmetry between borrowers and the commercial banks is reflected in inability of the majority of rural based borrowers to provide up to date reliable financial information and realistic business plans, which increases credit transaction costs. Consequently, these limits the ability of the banks to assess the credit-worthiness of individual borrowers. The study findings revealed that the banks are not interested in offering credit to micro, small and medium enterprises, farmers and poor households because information asymmetry resulting to high screening costs, credit contracts negotiation costs, monitoring and enforcement costs and thus supports the arguments of previous authors and Transaction Cost Economic Theory as reported by Williamson (2000; 2001; 2010).

4.0 Conclusion and Recommendations

Whenever the choice of direct channel was involved, borrower's information search costs (TSC) must be decreasing. Non-conducive nature of credit business environment in rural areas cannot allow TSC to decrease due to underdevelopment of rural areas in terms of remoteness and poor infrastructure development, difficulties in identifying and screening borrowers due to difficulties in accessing borrower's information and cultural barriers (poor tradition and customs). Therefore, given the current credit business environment in rural areas in Tanzania, direct channel for credit supply is the best option for credit supply in the urban areas.

One among key objectives of Liberalization of banking industry in 1991 was to regulate credit operations so as to simply accessibility of such a facility by the majority of Tanzanians, especially those in rural areas at low and affordable costs. The study findings showed that, a few commercial banks that scaled up their credit operations to rural areas were no longer interested in providing such a service to rural customers and therefore shutting down their credit operations in rural areas. They concentrate in urban areas with some few credit customers they consider credit worth.

The credit operating environment in Tanzania rural areas is not conducive to support direct credit supply from the commercial banks. Commercial banks in Tanzania incur very high transaction costs in the provision of credit services, yet they reach a very few groups in need. Majority of Tanzanians especially those who live in rural areas cannot access credit facility from commercial banks (origin of financial services). Therefore, there is a serious need for commercial banks to use alternative modes of credit governance structures (CGSs) to assist them absorb high transaction costs to penetrate rural based credit markets.

Based on the findings it is recommended that, the government of Tanzania should put more emphasis on infrastructure development and makes most part of the country accessible. These will simplify the process of locating credit customers and enable commercial banks to expand their market share for credit supply at reduced transaction costs. The government should give priority on proper planning of urban and rural areas, town and cities as well as speeding up development of national identification system. Such developments will assist both the banks and non-banks financial institutions to easily and quickly search and screen potential credit customers and maintain data base of borrowers at low costs. The current established credit reference bureau is neither efficient nor effective since it lacks so many borrowers' information; it has information of some few known borrowers, especially those located in urban areas. The installation of the national identification system is so vital for commercial banks credit operations since it involves the maintenance of the national data base that is linked with the commercial banks, health insurance funds, pension funds, revenue authority and the like. Such developments may simply accessibility of borrowers' information and expected to extremely reduce the related costs.

According to transaction costs economics theory, where there is high socio-economic and technological underdevelopment, there is also very high transaction costs. This is what is happening in Tanzania rural areas. Because of this, despite the liberalization of the banking industry in Tanzania, most commercial banks are not willing to invest in rural areas because of high levels of transaction costs associated with credit business. Regardless of the market interest rates for credits, commercial banks should be allowed to charge different interest rates

in different areas of the country, depending on the level of development in those areas. This will enable commercial banks to compensate high transaction costs in most underdeveloped regions of the country. Thus, allowing commercial banks to scale up despite high transaction costs and simply accessibility of credit facility from commercial banks throughout the country.

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