



# Rules of the Game and Efficacy of Public Microcredit Schemes: Evidence from Selected Borrowers in Malawi

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## Abstract

This paper contributes to the scholarly debates that question the efficacy of microcredit schemes in development programming. Dominant political economy debates posit that microcredit schemes have failed to achieve the envisaged financial inclusion and small-scale enterprise development outcomes because the nature of the intervention itself is an imposition by neoliberal promoters on global south economies. It is also argued that local political elites use microcredit programmes as a tool for advancing patronage. Motivated by this foregoing school of thought, we contend in this paper that informal credit management rules that dominate the administration of these schemes, at the expense of clearly spelt-out formal rules made known in the public domain, also contribute to this mission drift. Thus, our aim was to assess how prevailing microcredit-lending rules contribute to non-achievement of development outcomes. Guided by Douglas North's conceptualisation of rules of the game as our analytical framework, we employed Q methodology to generate key themes that emerged from primary qualitative data collected through in-depth interviews with purposively recruited microcredit clients of the National Economic Empowerment Fund, a public microcredit scheme in Malawi. Findings revealed that microcredit schemes were dominated by informal rules regarding turnaround time, credit appraisal processes, political interference, and misplaced borrower perceptions about the objectives of microcredit schemes. These rules were misaligned to what was promised to potential microcredit borrowers as reflected in the public microcredit's credit management procedures. We concluded that unless the apparent pervasion of these substitutive informal rules that distort outcomes is curtailed, public microcredit schemes risk becoming an irrelevant strategy for driving small-scale enterprise development agenda in countries like Malawi.

## Introduction

This paper explores how the developmental promise of subsidised microcredit, premised on the poverty-lending model, is challenged by informal rules of lending that crowd out an otherwise plausible development intervention. We showed this through a study that was conducted in Malawi, a country located in the southern part of Africa. The popularity of the microcredit concept in development discourse was propelled by favourable outcomes of a group-based lending microcredit action research project by Prof. Muhammad Yusuf in Bangladesh in the 1970s (Hearth, 2018). Since



then, the provision of microcredit services to poor and often financially excluded members of society in the global south has been projected as a potent tool for eradicating poverty (Bateman, 2012; Hearth, 2018). The theory of change behind microcredit was that a combination of self-help initiatives and the entrepreneurial mentality that the intervention claimed to promote and inculcate in its beneficiaries held the keys to the positive transformation of the socioeconomic fortunes of the poor (Robinson, 2001).

From the 1980s, microcredit programmes expanded substantially across sub-Saharan Africa, including Malawi, and became a key instrument for fostering financial inclusion (Chikalipah, 2017). Over time, researchers and practitioners have grown interest in studying the different impact dimensions of microcredit. The most common empirical focus areas in the existing literature include microcredit impact on the profitability of beneficiaries' enterprises, financial self-sustainability of microcredit institutions, geographical coverage of services and financial inclusion, as well as rising interest rates levels; precipitated by the need to achieve financial self-sufficiency of microcredit providers (Burrirt, 2006; Mtsitsi et al., 2026; Chikalipah, 2017).

Along the way, a different strand of literature emerged. This literature contends that the mission of microcredit has drifted from financial inclusion to being an instrument for promoting neo-colonialism and for propagating imperialism in the global south by the global north countries through financilising the poor (Ghimire, 2020; Bateman, 2022). Ghimire's (2020) argument specifically references the Canadian government's sustained funding of microcredit programmes in the global south through Global Affairs Canada (GAC) and Opportunity International Canada (OIC). Other prominent microcredit promoters included the World Bank and the United States Agency for International Development (USAID) (Bateman, 2012). Some scholars have further contended that microcredit has become a tool for rewarding political loyalists through giving out loans to 'voters' in the name of financial inclusion, only to write the loans off later after achieving political objectives (Burrirt, 2006; Schmidt, 2015; Hossein, 2016). This paper was motivated by this strand of literature on the political dimension of microcredit and aimed to expand the boundaries of knowledge by interrogating how informal rules of administering microcredit facilitate the achievement of these hidden objectives to the detriment of the known formal objective of promoting financial inclusion and enterprise development for the poor.

### ***Context of the problem***

At the global level, Malawi's development goals are aligned with Sustainable Development Goals (SDGs) through Malawi's Vision 2063 and, at the continental level, to the African Union Agenda 2063 (Government of Malawi, 2020). Poverty in Malawi remains pervasive, with 51.5% of people living below the poverty line (Government of Malawi, 2020). Efforts to alleviate poverty at per capita level are mostly frustrated by the low average annual gross domestic Product (GDP) growth rate of 4.1% recorded in the past ten years, which is below both the global and regional average and not significant enough to translate into improved socio-economic indicators (Government of Malawi, 2020). Arguably, the Malawi Government's intervention in the provision of microcredit opportunities, therefore, remains one of the viable policy strategies to deal with poverty (Government of Malawi, 2019). However, the poor performance record of public microcredit schemes in Malawi, punctuated by systemic and recurrent failures of the schemes to survive over time, begs questions as to whether an enabling institutional environment anchors the development model.

Some commissioned study findings consistently rank access to finance as a major binding constraint against efforts to grow small-scale enterprises in Malawi (World Bank, 2009; Finscope, 2019). In response, the Malawi Government has persistently acknowledged the challenge by showing its



resolve to design and implement policy response strategies to ameliorate this (Government of Malawi, 2019; 2020). However, the outcomes of successive Governments' interventions in the microcredit market involving direct service provision have been unsatisfactory. Public microcredit programmes in Malawi have, hitherto, been riddled with a myriad of challenges, chief among which are massive defaults on the loans by the borrowers (Sangala, 2016; Chilora, 2020).

Some key schemes Malawi has implemented include the Nyasaland Loans Board from 1958, which later transitioned to the Central Loans Board after the country gained political independence in 1964 (Chirwa, 2002). These efforts were followed up by the setting up, in succession, of the Smallholder Agriculture Credit Administration in the late 1980s (World Bank, 1997), Malawi Mudzi Fund, Malawi Rural Finance Company; and later in the 2000s, the Malawi Rural Development Fund, Malawi Enterprise Development Fund. However, the rest of the schemes have faced similar challenges. Currently, the government owns the National Economic Empowerment Fund (NEEF). However, underperformance issues that characterised predecessor schemes continue to manifest as NEEF reported operational losses of MK6 billion<sup>1</sup> and MK13.6 billion in 2021 and 2022, respectively (Chitsulo, 2023).

We noted the dearth of evidence that could explain how the nature of lending rules for these public microcredit programmes contributes to poor loan outcomes. These poor loan outcomes include lending to non-deserving clients, failing to use loan proceeds for the intended purpose, and failing to repay the loans. In this paper, we contend that the nature of the rules of the game inherent in administering public microcredit schemes in Malawi could explain the status quo. Our central argument is that, while in theory, formal rules of administering the loan schemes are designed rationally, they are, in practice, replaced by informal rules that end up blurring the success of these microcredit programmes. This, in turn, renders microcredit schemes irrelevant and impotent towards achieving their programmed objectives. We, thus, analysed how the rules of the game interact with players of the game to shape the nature of the outcome. The paper empirically addresses how the rules of the game shape the outcome of public microcredit programmes. The Mzuzu University Research Ethics Committee, under protocol No. MZUNIREC/DOR/22/98 granted ethical clearance to conduct the study. Further, each study participant also signed an informed consent before the commencement of each interview.

#### ***Defining rules of the game: An analytical framework***

Our analytical framework was guided by Douglas North's (1991) conceptualisation of rules of the game. Specifically, North (1991, p.97) defined rules as "humanely devised constraints that structure political, economic and social interaction. These rules consist of both informal constraints (sanctions, taboos, customs, traditions, and codes of conduct) and formal rules (constitutions, laws, property rights)". Formal rules are written, developed and communicated formally, whereas informal rules are unwritten, socially constructed and communicated outside the known formal channels (Australian Government, 2016; Ledeneva and Efendic, 2021). Whether formal or informal, these rules prescribe how social actors interact to solve social problems, such that they constitute rules of the game, while actors occupy the space of players of the game (Pejovich, 1999; Skoog, 2005). We adopted this conceptualisation as our analytical framework for analysing how the rules of the game in public microcredit schemes in Malawi and how players of the game (borrowers) behave, interact or react to shape the final programmatic outcome.

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<sup>1</sup> MK is short form for Malawi's currency. US\$1 is officially exchanged for MK1,751



**Method and data**

The empirical process was designed to extract in-depth qualitative discourses about the research question; hence, the study design was qualitative. To assist in objectively grouping the data into themes, we employed Q methodology to cluster like-minded perspectives and reduce the number of groups of viewpoints to enable effective analysis. This method (Q methodology) reduces qualitative data from respondents into fewer factors or themes (Lee, 2017).

Construction of the Q-sample commenced with mapping the service delivery promise, standards or rules developed by NEEF, known and formally communicated to potential borrowers. These rules codified how the entity manages its loans concerning beneficiary identification, loan qualification criteria, loan appraisal processes, and turnaround time. These formal rules were akin to a service charter, expected to be formally enforced by the microcredit provider. NEEF’s loan management style, practices and ownership structure typified all public microcredit schemes that existed before. Hence, we found it to be a credible case study. Table 1 provides formal conditions for accessing different microcredit products from NEEF.

*Table 1: Selected loan products and formal access conditions*

No	Loan product	Target and Conditions
1	Women Enterprise Loan	<ul style="list-style-type: none"> <li>• Groups of women or individuals aged 36 to 65 years who are in business</li> <li>• Voluntary groups with group constitution</li> <li>• Business plan for a start up</li> <li>• Loan amount of between K500,000 to K10,000,000 for individuals and K50,000 to K1,000,000 for individual members in a group</li> <li>• 6 to 12 months’ repayment period</li> <li>• Turnaround time for 21 years</li> </ul>
2	Youth Enterprise Loans	<ul style="list-style-type: none"> <li>• Groups of 10 youths or individuals aged 18 to 35 who are in business or want to venture into business</li> <li>• Group constitution and business profile for existing business</li> <li>• Business plan for a start-up</li> <li>• Physical collateral for individuals</li> <li>• 6 to 12 months’ repayment period</li> <li>• Turnaround time of 21 days</li> </ul>
3	Enterprise General Trading Loan	<ul style="list-style-type: none"> <li>• Individuals, partnerships or private limited companies with well-established and registered general trading business or have a business license where applicable</li> <li>• Identification letter from a local leader</li> <li>• Sketch map of the home or district</li> <li>• Repayment period of 6 to 24 months</li> <li>• Turnaround time of 21 days</li> </ul>
3	Agribusiness Loans	<ul style="list-style-type: none"> <li>• Small and medium agricultural enterprises in serious farming wanting to do mechanization, value addition, livestock farming, etc</li> <li>• Bank statements</li> <li>• Business records</li> <li>• Grace period depending on crop being produced</li> <li>• Thresholds of between K5,000,000 to K50,000,000</li> <li>• Turnaround time of 21 days</li> </ul>

Source: [www.neef.mw](http://www.neef.mw)



Based on some of the formal conditions outlined in Table 1 and the overall rationale for government intervention in the microcredit market, we constructed 29 statements presented in the Appendix. The development of these statements, technically known as Q-sample in Q methodology, was primarily informed by multiple literature sources, including published reports and theoretical constructions identified within the research question conceptualisation process. Specifically, common sentiments from NEEF borrowers that were topical in the local print and electronic media were also considered when constructing these statements. This process guided the drawing of study discussions on whether the microcredit facilities' management respected formal rules set to facilitate the achievement of intended ideals espoused by NEEF as a formal organisation.

Each study respondent was requested to sort the statements presented in the Appendix on a quasi-normally distributed grid by rating them on a 9-point Likert-type scale, with 4 denoting the most agreement and -4 denoting the least. We finally conducted in-depth interviews with each respondent to understand varying sentiments and reasoning behind their sorting. The study recruited 22 microcredit borrowers from NEEF, a public microcredit scheme used as a case study. Respondents were drawn from Lilongwe, an administrative district that hosts the capital of Malawi's political administration. This sample size was adequate because key proponents and practitioners of Q methodology, including Watts and Stenner (2005), Stone (2015), Damio (2016) and Lee (2017) recommend ten as a minimum sample adequate for Q methodology. We further confirmed sample adequacy through a favourable Kaiser-Meyer-Olkin test outcome, as reported in the succeeding section.

## **Results and discussion**

### ***Data suitability for factor analysis and extraction***

Before clustering data into main themes and conducting further factor analysis, the Kaiser-Meyer-Olkin (KMO) measure of sample adequacy and Bartlett's test of sphericity were conducted in IBM's SPSS Version 16. We found a KMO of 0.592 (KMO>0.5), and Bartlett's test reported  $p = 0.020$  ( $p < 0.05$ ), suggesting that our data passed the suitability test for factor analysis, according to Shrestha (2021). We then determined the number of themes (factors) to extract to represent respondents' views. According to Shrestha (2021), only factors with an eigenvalue of more than 1 ( $EV > 1$ ) should be retained. Table 2 shows that eight factors were extracted. Thus, the eight extracted factors explained almost 76% of all items, significantly above the recommended 50% minimum threshold. For our purposes, the results in Table 2 mean that the views of all 22 participants were collapsed into eight categories. Specifically, factor analysis showed that nine respondents' views were reduced to Theme 1, 3 respondents to 2, 1 respondent to Theme 3, 3 respondents to 4, 2 respondents to 5 and 6, and one respondent each to Themes 7 and 8.



**Table 2: Factor extraction**

Respondent Number	Initial Eigenvalues			Extraction Sums of Squared Loadings		
	Total	% of Variance	Cumulative %	Total	% of Variance	Cumulative %
1	4.813	21.875	21.875	4.813	21.875	21.875
2	2.710	12.318	34.193	2.710	12.318	34.193
3	2.176	9.893	44.086	2.176	9.893	44.086
4	1.912	8.690	52.776	1.912	8.690	52.776
5	1.487	6.761	59.536	1.487	6.761	59.536
6	1.324	6.019	65.555	1.324	6.019	65.555
7	1.233	5.603	71.158	1.233	5.603	71.158
8	1.005	4.567	75.725	1.005	4.567	75.725

Source: Authors

**Key findings and discussion**

Since as many as nine respondents’ views clustered into theme 1, our interpretation of results focused on four common key issues from this category. In-depth post-sorting interviews supplemented the interpretation to clarify the representation of these perspectives.

*Loans not synchronised with the seasonal nature of borrowers’ investments*

Generally, there was agreement amongst respondents that the availability of loan products was not synchronised with seasonality. The most referred-to product was agribusiness loans. This loan product's objective was formally marketed to benefit small and medium agricultural enterprises involved in commercial farming, mechanisation of farming, value addition, livestock farming, etc. (see Table 1). However, study findings revealed that financing for this product was often not available for disbursement by NEEF at the right time of the season when borrowers would expect the loans to be readily available during times for procurement of farm inputs and meeting labour costs associated with farming.

The second dimension of seasonality is related to enterprises that involve general trading. The findings revealed that retail trading, whether in agricultural produce or otherwise, constituted almost the whole portfolio of NEEF borrowers interviewed. This sample bias towards retail trading was not by design but was a reflection of the Malawi small-scale enterprise sub-sector, which remained dominated by retail trading (Finscope, 2019). For their businesses to be profitable, the study revealed that their investments, hence demand for credit, were timed based on seasonal fluctuations, aligning themselves with periods of the year when their customers had higher disposable incomes and scaling down when their clients had the least incomes. In this regard, the study revealed that while demand for respondents’ products peaked from April to July every year and slowed down afterwards, NEEF could not disburse loans during this need period. The explanation was that the entity usually had cash-flow problems during this period due to delayed subvention from the government, occasioned by the fact that the financial year commences on April 1 of each year and that the processes of replenishing the fund took a long time.



*Arbitrary turnaround periods and high collateral perfection costs*

Despite NEEF's formal rules promising a maximum turnaround period of 21 days across all loan products and reflecting this standard in its service charter, respondents lamented that it was generally too long, often unpredictable and frustrating. This was shown by agreement to statement 6 in our Q-sample that sought to assess adherence to this formal promise. During in-depth interviews, cases were recorded of loan applicants waiting for about six months and some, up to 2 years before disbursement of their approved loans, could be made. A representative experience was recorded of an individual borrower who recounted having applied for an MK10 million loan in 2020, out of which MK8 million was approved for disbursement. However, only MK2 million was disbursed two years later in 2022, translating into an informal effective turnaround period of 2 years.

In addition to the unpredictability of the turnaround time, individual borrowers revealed that increased collateral perfection costs and protracted processes also burdened them. For instance, one borrower provided the following account:

The collateral perfection process led me to incur unplanned expenses to the extent that the MK2 million that NEEF eventually disbursed, out of the MK8 million I applied for, was just enough to recoup the costs incurred in the loan perfection process. The loan perfection process involved working with lawyers on documentation for my properties. It also involved document certification processes with traditional leaders who normally demand to be given 'a goat' defined in monetary equivalent, in addition to costs for the valuation of properties pledged as collateral, as well as moving to and from NEEF offices to follow up on the status of the loan after dully submitting all the required documentation. These were among other hustles I had to negotiate past to get the loan (Key Informant Interview, January 12, 2023).

We found the whole notion of requiring the production of physical collateral as a pre-condition for lending in public microcredit rules as defeating the whole concept of microcredit, which was founded on group/social collateral as a way of averting stringent collateral requirements from the mainstream financial system (Kumari, 2020). In addition, the rules of lending required that in the case of a start-up enterprise, applicants should be able to provide a business plan to be used instead of business performance records required of existing business applicants. However, findings revealed that such rules were not followed as start-up enterprises could access the loans without proof of any business plan and without the same being subjected to appraisal as 'it all depends on your knowledge on how to push for things' (interview with a borrower, 12 January 2023). Faced with these often-familiar scenarios, there was increasing consensus amongst borrowers that applicants lose interest in the loans due to longer waiting periods. As a result, when the loans were finally disbursed, often in amounts less than what was approved, the funds were treated as windfall, hence not used for the originally intended purpose.

*Political interference with formal rules*

Findings further revealed entrenched bending of the game's formal rules in favour of politically exposed persons. This was exemplified by agreement to statement 3 (politicians influence the beneficiary identification process by imposing a list of people who should be given the loans) and statement 14 (I believe I successfully got the loan because I belong to a ruling political party). Formal rules of the loans, communicated through NEEF, indicated that access to loans was appraised based on ownership of a business enterprise and meeting other credit assessment criteria such as group constitution, providing bank statements and business plans, depending on a specific loan product.



However, respondents linked non-business-related reasons to being responsible for improved loan access in the study sites. They argued that after the regime change in 2020, they could now access NEEF loans, unlike before 2020. One respondent narrated the following indirect but telling statement that presented another face of political interference:

We used to hear that people from other parts of the country, especially the southern region, had opportunities to access government loans from MEDF. We were just wondering how that was possible because we, from this side (Lilongwe and surrounding districts), did not have that opportunity. Here we are (Key Informant Interview, December 15, 2022).

The preceding quotation reflected an entrenched culture of politicisation because the previous political regime (led by the Democratic Progressive Party) running the government for the period referred to in the discussion had an established support base in the southern region. However, the ruling party at the time of the study, the Malawi Congress Party, had an established support base in the country's central region (European Union Election Observation Mission, 2019), where primary data collection took place. In this regard, the implication of the quote above was that potential borrowers from the central region had an improved chance of accessing the loans than they used before due to corresponding changes in political dynamics. This revelation agreed with findings from a study done in Jamaica by Hossein (2016) and by Schmidt (2015) in Uganda. In both cases, findings revealed that microcredit schemes were an instrument for political patronage.

While the government formally projected NEEF as a revolving loan fund and encouraged borrowers to repay so that more 'deserving' Malawians could benefit, most borrowers grew to believe they did not hold a moral obligation to repay. This was revealed by respondents' agreement to two key statements in the Q set that intended to assess the behaviour and expectations of the borrowers concerning how they understood their obligations. First, there was growing conviction that even if the borrowers did not repay their loans, the government had the responsibility to find financial resources from elsewhere to capitalise the fund for the benefit of others (statement 25 in Appendix). The respondents' position was that because most beneficiaries invested their loans in agricultural production, if their crop failed, it implied that they should not be required to repay the loans.

Generally, most borrowers did not take the repayment appeals or campaigns seriously because, informally, they believed that the silent rule of not repaying the loans was fully entrenched. They believed that public appeals to repay government-sponsored loans had existed from time immemorial. Still, nobody had been seriously penalised for not repaying the loans, as was normally done with private microfinance players. The following sentiments were representative of respondents' views on need and their expectations and obligations to repay the loans:

Since the time of MRFC, which started during the Kamuzu Banda era, who has been arrested for not repaying the loan? We should not talk about what happened during the MARDEF or MEDF period during the democratic era. Repayment messages are just a gimmick by the loan administrators to show that they are doing something about it, and NEEF people even know about this (Key Informant Interview, December 12, 2022).

#### *Lack of due diligence*

A further commonality in the sorting pattern amongst respondents revealed that prior to disbursement of the loans, NEEF loan officers did not conduct serious assessments or appraisals of the viability of the enterprises. The common agreement to statement 11, for instance, amongst





respondents 11, 12, 13, 14 and 17 revealed this entrenched practice. We argue that developmental lending, which promotes enterprise growth, should ordinarily be interested in the nature, type and viability of an enterprise for which a loan is being attached. Merely focusing on the ability to repay the loan defeats the developmental objective of a public microcredit scheme. Lack of due diligence was also manifested in the finding that borrowers could easily oscillate between investing in one business enterprise to the other when loans were disbursed out of season. The study revealed that this practice deprived borrowers of the benefits of experiential learning in their chosen line of business, an important ingredient in enabling enterprise stability and growth.

### **Conclusion**

Generally, formal rules indicated that government intervention in microcredit provision was driven by the Government's determination to economically empower ordinary and underserved Malawians (particularly women, youth and persons with disabilities). This economic empowerment was planned to be achieved by providing quality, affordable and sustainable microcredit services for improved livelihoods, as professed in the mission statement for NEEF. However, findings from this study revealed that the variance between what formal rules prescribed and lending rules that were followed in practice contributed to the obscurity of an otherwise technically sound developmental intervention. This paper has shown that informal rules in microcredit delivery appeared to have created competition with, and replaced formal rules in agreement with the conceptualisation of rules by the Australian Government (2016) and North (1991). In this case, the entrenchment of informal rules in public microcredit lending provides fertile ground for manipulation by political elites to achieve their ends. Based on this evidence, we concluded that unless the apparent pervasion of these substitutive informal rules that distort outcomes is curtailed, public microcredit schemes risk becoming an irrelevant strategy for driving small-scale enterprise development agenda in countries like Malawi.

### **Conflict of interest**

The authors reported no potential conflict of interest.

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