THE IMPLICATIONS OF HAWALA REMITTANCE SYSTEM TO THE SOMALI BUSINESSES: A CASE STUDY OF EASTLEIGH, NAIROBI.

BY

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UNITED STATES INTERNATIONAL UNIVERSITY

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THE IMPLICATIONS OF HAWALA REMITTANCE SYSTEM TO THE SOMALI BUSINESSES: A CASE STUDY OF EASTLIEGH.

BY

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A Project Report Submitted to Chandaria School of Business in Partial Fulfillment of the Requirement for the Degree of Masters in Business Administration (MBA)

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SUMMER 2014
DECLARATION

I, the undersigned, declare that this is my original work and has not been submitted to any other College, Institution or University other than the United States International University-Africa for Academic Credit.

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This Project has been presented for Examination with my Approval as the appointed Supervisor.

Signed: __________________________ Date: __________________________
Kepha, Oyaro

Signed: __________________________ Date: __________________________
Dean, Chandaria School of Business
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DEDICATION

To my loving uncle Shuriye Mumin Afrah, parents, aunts, uncles, my sisters, brothers, cousins, supervisor; Dr. Kepha Oyaro, friends, mentors and most of all Allah, through your patience and faith I have endured and succeeded, through your love, I have accomplished and without all of you, I will not be the person I am today.
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ABSTRACT

The general objective of this study was to investigate the implications of the Hawala Remittance Systems to the Somali Businesses. The study was guided by the following research objectives: To determine the role of the Hawala system in Somali businesses in Eastleigh, to identify the factors that motivate the Somali businesses in eastleigh to use Hawala system and to assess the challenges faced by Hawala system as a financial transaction system.

The study used descriptive research design that focused on the Somali business people, employees, individuals and hawala dealers based in Eastleigh. The subjects and participants of this study were homogeneous and constituted of only business people of the Somali origin living and working in Eastleigh, Nairobi, Kenya. The population comprised of 270 respondents. Simple random sampling was used to obtain a sample size of 30, comprising of business owners, employees, hawaladars and individual hawala users. Questionnaires were designed and used to collect data and analysed using descriptive statistics by use of Statistical Package for Social Sciences (SPSS) software and Microsoft Excel.

The study assessed operation, development, growth of the business and banking system as the major roles of the Hawala System. The study revealed that hawala had the role of being used as a banking system, for instance it was found out that 96.7% of the respondents agreed that hawala systems were also used as banking system, where these respondents deposited huge amounts of money in dollars in these systems after making profits from their businesses in eastleigh, before they transferred to a normal bank account safely. However the study showed that Hawala system had no major role in development, growth and operation of Somali Businesses in eastleigh, and infact Islamic banks like First Community Bank and also Gulf Bank were major financers of eastleigh businesses

The study showed speed of service delivery, cheap transaction, cultural convenience and versatility issues as the major factors motivating Somali Businesses to use Hawala systems. The study revealed that hawala remittance system was very fast in terms of financial transactions in businesses and also the cheapest mode of money transfer as compared to banks, reason being that the system’s limited overheads and the virtual lack of regulation and taxation, hence lower overall operation cost.
The study further revealed that government issues were the major challenges facing Hawala system and on the other hand the study demonstrated that security was not viewed as a challenge facing Hawala system; since it was found out that Hawaladars have put strict security measures. For example, it was discovered that Dahabshiil has hired security guards, who screen customers before letting them into the building to conduct their businesses. Further more the study revealed that hawala was not used for illegal money laundering activities here in Kenya, which lead to crimes and law violations.

It was concluded that in order to solve the challenges facing Hawala systems, the government, through the Ministry of Trade, should introduce bills or laws that cover and legalizes the use of the Hawala systems without any inhibitions. It was also established in the study, that new innovations should be introduced by the Hawala owners; like the introduction of personal and business accounts that will encourage more people who are not Somalis to use the system. The government should also start introducing courses about Hawala System in schools and universities to make its citizens aware of its benefits and implications so that the citizens or even foreigners living in Kenya are aware of the business opportunities this system creates. The Media should also dedicate a section of the business news to educative topics on Hawala and its performance in order to make the citizens and foreigners in Kenya aware of alternative financial transactions.

The study recommends that the government should introduce policies that will give Hawala system a fair chance of operating in Kenya just like other financial transactions that are already in operation. This move will enable the government to create jobs for its active unemployed youth and also revenue which will accrue from the taxes collected from these Hawalas that generate a lot of money. The study further recommends that auditing of accounting books of the hawala remittance system should be conducted since, no financial statements had ever been printed and released, and this will help the government when making policies for development purposes.

The researcher recommends that the government should develop Hawala Remittance Act that will create more favourable conducive environment to smooth the operations of the Hawala Systems, and implement it.
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CHAPTER ONE

1.0 INTRODUCTION

1.1 Background of the Problem

Although this report is focused on the hawala system, it should be noted that other informal money transfer systems are mentioned, as well. We have wire transfer, which is an international method of electronic funds transfer from one person or institution like a bank to another. Individuals can transfer money from any country to another using the western union. There is also Giro that is also called direct deposit, which is a payment transfer from one bank account to another bank account and instigated by the payer, not the payee (US Federal Reserve, 2008).

Giros are primarily a European phenomenon; although electronic payment systems such as the Automated Clearing House exist in the United States and Canada, it is not possible to perform third party transfers with them. In the United Kingdom and other countries the term giro may refer to a specific system once operated by the post office (US Federal Reserve, 2008). Money order, which is a payment order for a pre-specified amount of money.

We also have Paypal, which is an international e-commerce that enables users to make their payments through the internet using their emails. This eliminates the traditional paper methods. It is subject to the US economic sanction list, and subject to other rules and interventions required by US laws or government (Paypal, 2011).

Further more we have another money transfer called the suftaja procedure, which is the other main instrument of credit, usually cited along with hawala in Islamic legal texts. It is also referred to money transfer without money movement (Jost and Sandhu, 2000).

Hawala Remittance system(also known as hundi), is defined as an informal system primarily used to send money to and from the Middle East, North Africa, the Horn of Africa, and South Asia. Hawala has its origins in classical Islamic law and is mentioned in texts of Islamic jurisprudence as early as the 8th century. Islamic law and the later common law "had no difficulty in accepting agency as one of its institutions in the field of contracts and of obligations in general (Passas, 1999)
It should be noted, that Informal financial networks, similar to hawala, exist in parallel throughout Asia, for example the Tamil communities of Sri Lanka use the undival, India call it hundi, China fei ch’ien, the Philippines, it is known as the padala, Hong Kong’s hui kuan, and Thailand’s phei kwan, all operate as informal money transfer systems (Viles, 2008).

According to Elqorchi (2002), Hawala remittance system refers to the transfer of money or funds from one place to another through hawaladars. Money transactions through hawala remittance system are mostly initiated by people from the Somali, Sudanese or even Ethiopian communities, who have immigrated to developed countries like Canada, Germany and many others. The hawala system has also been used to send funds from a developing country, even though the purpose of the funds transfer is usually different, since people have different needs to satisfy, in different ways and at different times.

Although Informal Money Transfer Systems have operated in various communities over time, the largest ones operating today evolved from two original types, namely the hawala (hundi in Pakistan), which developed in South Asia (Bangladesh, India, and Pakistan) and the fei ch’ien, which started in China. Some researchers say that the hawala/hundi system was developed more than a century ago within the immigrant Indian population in Africa and South East Asia as a means of settling accounts. Other scholars place its origin many centuries ago when traders sought a secure system to transfer money and people looked for a way to travel without having to carry large sums, thereby making them less vulnerable to robbery by highwaymen (Passas, 1999).

One of the main issues faced by Somali Businesses is about financial transaction issues, specifically fastest ways of transferring money to their businesses located in abroad like in China, Dubai or even Uganda without any registration problems which they encounter in the banks when trying to open an account. Throughout the years, the Somali business women or men have considered different alternative ways to solve these kinds of financial transaction issues using the normal banking systems, which is very common in different countries all over the world, but because of the long procedures involved in these normal banks, they came up with the alternative of using the Hawala system (Elqorchi, 2006).

The operation of hawala essentially involves a hawaladar famously known as a broker delivering money from his cash reserve or account at the request of a counterpart.
hawaladar in another country who is serving a client (Nihar, 2002). It is believed that Hawala networks were first used by Asian countries to provide safe money transfers for traders which travel along the Silk route. It is based largely on trust and extensive use of connections, such as family members and other known affiliations. Some of the examples of Hawalas based in Eastleigh are: Dahabshiil and Mustaqbal. The contemporary development of this approach is connected to the partition between Pakistan and India in 1947, when exchange controls made it illegal to transfer money between nations and this approach filled the gap for this issue (Miller, 1999).

This remittance system approach aims on arranging for the transfer of money internationally for example from the UK, United States, Germany, and China or domestically for example within Kenya i.e. from Nairobi to Mandera. Even if there are talks about the black market and underground economy, hawala transactions are not deemed as illegal in most nations (Cottle, 2001).

Specifically, hawala transaction have some similarities with international money transfers done by normal financial organisations like the forex and those hawala brokers in Western regions or even in Some African Countries like Uganda, Somalia and even Tanzania do not operate underground but advertise openly to the local press about the ongoing transactions (Passas, 1999). There is little documentation and record keeping in the hawalas located in Eastleigh. There are many motivations for the Somali Business people in Eastleigh for using the Hawala system, they include: its speed, effectiveness, efficiency, reliability, lack of bureaucracy, and ability to evade taxes.

Just like Islamic banking, hawala constitutes a practical alternative approach to conventional finance (Tripp, 2006). However, it is necessary to address important governance issues and develop an effective legal framework for this specific type of systems in order to display their full potential (Mohieldin, 2012).

Many transactions associated with Hawala are done in the area of import and export businesses especially in the clothing and shoes stores in Eastleigh, whereby money used to purchase the goods for example from China or Dubai is paid through a Hawala located in the country of purchase and is paid by the buyer of the goods from the base country
where the business is located at, jewellery like the gold jewels imported from Saudi Arabia, Singapore and Dubai by the Somali business women and men located in Eastleigh who are in the gold jewellery business or silver jewellery business (interview, 2013).

Hawala is also involved in currency exchanges, whereby when a client takes money in dollars from the hawala and wants for example Kenyan Shillings, the hawala dealers will exchange the dollar for him or her with Kenyan Shillings at a rate higher than what the banks offer! Hawala often don't use negotiable instrument and as a result money transfers take place based on communications among members of the Hawala network (Passas, 1999).

This information about the hawala system is meant to make other business people who are not Somalis aware of alternative forms of financial transactions that exist in the world. One of the challenges with the Hawala system is that it paves the way for having a system that escapes the formal accounting procedures of the national government of the country it is operating in. Another challenge is that its registration has not been implemented by the Kenyan government (CBK, 2009).

Kenya is growing as the Islamic finance hub in East and Central Africa (Parker 2010). It has Islamic banking such as Gulf African Bank, which is the first Islamic bank that was launched in September 2007, followed by the First community Bank opened in 2008. Just like these Islamic banks, the Government should also become a hub for Hawala transaction systems hub, and authorize the Gulf or the First Community Banks to act as brokers, this will boost Government finances. These present an opportunity for the Government of Kenya to tap into this market (CBK, 2009).

Hawala has led to increased competition, for instance players in the banking sector, who are the formal transactors, have experienced an increased competition over the last few years resulting from new entrants into the Kenyan Market, thus many banks lose their market shares and some are even closed down (Muchene, 2003). The main goal of this research was to identify the importance of the Hawala system to the Somali Businesses especially in Eastleigh.
1.2 Statement of the Problem

The intention of this research is to assess the implications of the hawala system to the Somali businesses in Eastleigh, particularly whether and how they are becoming useful to empower both the upcoming and the growing businesses in Eastleigh. By providing a cheap, reliable and a fast remittance system to these Somali businesses especially the small upcoming businesses in Eastleigh, you not only provide fast financial transactions, but better service, high and better exchange rate compared to banks that give less Kenyan Shillings for the dollar.

Not many people in Kenya are aware of the benefits or the practice of the Hawala Remittance System as an alternative financial transaction, meaning there is knowledge gap. This study removes the knowledge and the practice gaps by providing adequate information on the Hawala System as an alternative financial transaction.

Hawala system is a new money transfer system which is unique to the Somali community. There isn’t enough documented literature on this money transfer system, compared to other money transfer systems like the western union or money gram and therefore, this is the knowledge gap that this study has attempted to fill.

1.3 General Objective

The general objective of this research study was to identify the implications of the Hawala remittance systems in Somali businesses in Eastleigh.

1.4 Specific Objectives

1.4.1 To determine the role of Hawala system in Somali Businesses in Eastleigh.
1.4.2 To identify the factors which motivate the Somali Businesses in Eastleigh to use Hawala system.
1.4.3 To assess the challenges faced by Hawala as a financial transaction system.

1.5 Significance of the Study

1.5.1 Government

It will enable the government to understand that hawalas are very significant sources of revenue through taxation if they start assessing it deeply from a neutral point of view and
implement the laws of allowing the hawaladars the right to register and to work freely here in Kenya just like the banks and the forex.

1.5.2 Business people and Organizations
This research paper is very significant to them as it will help them to have a clear understanding of the implications of the hawala remittance system and its role in the Somali businesses based in Eastleigh in their financial transactions. With the growing issues of improving financial transaction all over the world, most organisations and interested business people or parties like my work colleagues and my fellow graduate colleagues, are trying to find out the impact of the hawala system and its role in businesses especially in Eastleigh, hence analysing Hawala as an alternative remittance system that is very fast, convenient, and reliable is very crucial.

1.5.3 Money Senders
This study will educate the money senders more on the effective and efficient use of Hawala System, its challenges and how to go about it.

1.5.4 Researchers and Academicians
This study is very important to researchers and academicians because it may create an area for further studies, where broader research may show more advantages or benefits that would accrue from Hawala Remittance Systems. It will also be a source of reference for academicians, when teaching a course about this topic.

1.6 Scope of the Study
This study only covered the implications and the role of Hawala Remittance System to the Somali businesses in Eastleigh. As there were numerous issues surrounding the financial market and remittance systems, this research primarily examined the role of the said system, its implications to the growth of Somali businesses.

The outcome of this study was limited only to one specific community or business people who were the Somalis, the data gathered from, journals, books, news, and in depth interviews with Somali business women and men, hawala dealers and hawala customers. Other factors about the hawala system were not covered because of limited information and because of relatively short period of time available for the completion of the research.
This had an impact on the outcome of the study. The data was collected from second 2\textsuperscript{nd} September 2013 to 2\textsuperscript{nd} October 2013.

1.7 Definition of Terms

1.7.1 Hawala System
Hawala remittance system is an informal fund transfer system that runs in similar to – and usually independently from – the formal banking system (Tharoor, 1997).

1.7.2 Money Transfer
It generally refers to cashless modes of payment or payment systems. This may occur electronically or physically. The informal money transfers are used because the official currency exchange market cannot fully service the demand for foreign currency of the economy (Passas, 1999).

1.7.3 Money Senders
These are the users of the Hawala system who use it to send money as an alternative financial transaction system (the researcher).

1.7.4 Somali Businesses
These refer to businesses owned by the Somali business men or women, some of these businesses in Eastleigh are like the jewellery, clothing or the shoes businesses (the researcher).

1.8 Chapter Summary
This chapter presented the Hawala System, its implications and role in Somali Businesses; a case study in Eastleigh. Basically, this study attempted to identify and analyse the implications of the hawala system as a financial transaction system, its role in the Somali businesses and challenges it faces as a financial transaction system.

The chapter began with a historical background of the Hawala System to enable the readers to understand how the hawala system came to exist in this world of today. It started with the introduction of the study, background of the study, statement of the problem, general objective, research objectives of the study, significance of the study, scope of the study, definition of terms and finally the chapter summary.
Chapter two covers the Literature Review based on the research objectives. Chapter three presents the research methodology used, while the fourth chapter presents a summary of the results and findings of the study. Chapter five presents summary, conclusions, findings and recommendations for improvement and for further studies.
CHAPTER TWO

2.0 LITERATURE REVIEW

2.1 Introduction

This Chapter shows further understandings of the implications of the hawala remittance system to the Somali businesses. It reviews the literature which examines recent research studies, books, and hawala business data. Section 2.2, will give detailed information on the role of the hawala system in Somali businesses giving some of the important roles like; development and growth, versatility. Section 2.3, will identify the factors that motivate the Somali businesses especially in Eastleigh to use the hawala system as a financial transaction system as opposed to using the normal banks like Barclays, Equity or even the National banks. Section 2.4, will assess the challenges faced by the hawala system as a financial transaction system. Finally section 2.5 which is the chapter summary will give a brief recapture of the literature review highlighting the various research objectives.

2.2 The Role of the Hawala System in Somali Businesses

2.2.1 Operation of Business

According to Banks, formal banking institutions do recognize that a business entity or institution should not engage in business that is very risky or absorb risk that can be efficiently transferred to other participants, but rather accept only risks that uniquely a part of the bank’s services (Banks, 2005). Unlike Hawala systems, that deals with services outside its areas.

Hawala dealers, who own and invest in the hawala systems, do risk identification before agreeing to give Somali businesses in eastleigh loans to avoid bigger surprises, just like Robinson (2008) said the significance of risk identification is to avoid surprises. The importance is to identify risk as early as possible, thereby reducing risk (Brajovic et al, 2008).
In real estate, some Kenyan property dealers claim that real estate prices have tripled in areas where Somalis live, especially in Eastleigh, resulting in a real estate boom, led by the Somali business community in Eastleigh, using hawala systems (Recorded interview, October 2009). Hawala dealers do risky transactions for risky businesses, based on their character. Character is a measure of the reputation of the borrower, willingness to pay and repayment history (Banks, 2005). Businesses in Eastleigh prefer to use the Hawala for the operation of business since no collateral is involved due to repayment constraints. According to Robinson (2008), there may be periods when the borrower’s capacity to repay the debt is constrained.

The Amal Shopping Plaza was constructed in 2003 and hawala system played a major role in its development. Since then a number of additional shopping malls have been built and more are in planning phase or undergoing construction. Shopping malls have identified architecture as a medium of identification and a means to achieve a notion of uniqueness with their customers. They competed with the most expressive facades, shapes of windows, systems of stairs and ramps, as well as with their size, in order to attract more customers (Interview, 2013).

2.2.2 Development and Growth of Somali Businesses

According to Fight (2008), formal institutions, for example, the commercial banks put heavy reliance on the customers’ financial statements, when granting them loans to develop and grow their businesses. This is not the case in Hawala systems, where the informal lenders rely mostly on personal, social as well as business relationships in their collection of important information regarding potential borrowers (Steel et al., 2007).

Edmond (2007) holds that relying on financial statements can be suspect for the counter parties involved, due to time used to produce them and also poor attention to details. Hawala institutions don’t require such long financial statements, but rely on the basis of trust. The hawala remittance systems especially in Eastleigh have led to the development and growth of many Somali businesses, for example shopping malls like The Amal Shopping Plaza that currently represents the most developed and sophisticated shopping malls in Eastleigh. Located next Bangkok Shopping Mall, it is the highlight of retail environments in this urban refugee settlement (Passas, 2006a).
2.2.3 Banking System

In general terms, banking refers to the business activity of accepting and safeguarding money owned by other individuals and entities, and then lending out this money in order to earn a profit. (Investopedia). According to Nihar (2002), Hawala is used as a banking system, where Somalis who have no Accounts in the formal financial like banks, use it to keep their money for some time before they access it and use it to conduct their businesses.

The Somali Business Community based in Eastleigh used it to transact businesses all over the world, just like a bank, for example; a Somali Business person will go to a Hawala of his or her choice, deposit a specific amount of money in the country of residence, especially when purchasing goods in bulk from another country like Dubai, instruct the hawaladar who is based in Dubai to pay the supplier of the goods in Dubai before the shipment procedure starts. Also the hawaldars lend the money made within the Hawala system to other hawaladars or business clients in order to earn more profits and benefit a lot.

Hawaladars also offer foreign currency exchange services, where money can be changed from Kenyan, Somali or even Ugandan Shillings to American Dollars, just like banks such as Equity bank do. These hawadars offer the forex service at a very low and cheap exchange rate compared to banks. The profits accrue when for example the dollar currency depreciates, meaning $ 1 is exchanged for Ksh. 75, due to inflation and other factors, the $1 dollars is exchanged for Ksh. 90, then the exporters of goods or hawaladars of a Hawala Remittance System will benefit from the transactions.

Hawala system also engages in receiving and sending money from one location to another, a service that is also offered by banks such as Equity bank. The hawaladars ensure that the procedures of sending or receiving money is smooth, effective and efficient, so as to avoid costly errors made during the processes. The clients are asked to identify themselves by producing their identity to the hawaladar at the counter when receiving or collecting money from any hawala remittance system, since lack of an identification document is very risky (interview, 2013).

The receiver is also asked for the details of the sender, like the name of the sender, country of residence and the amount of money that was being sent, since failure to do so...
will lead to the resending of the money to the original person.

2.3 Factors Motivating the Somali Businesses to use Hawala System

2.3.1 Speed of the Hawala System

Hawala transfers are extremely fast, often completed within a single day, thanks to the lack of regulatory work required and the extensive range of the networks. Speed is of particular value when funds are being moved into or out of remote areas where, in some cases, it would not only slow but impossible to send or receive cash. In comparison to formal transfer methods, which can have fees of up to 20%, charges associated with hawala transactions are a mere 2-4% (Sharma, 2006).

Hawala transactions are usually completed within 24 hours. Remittances between the main international cities take an average of 6 to 12 hours (ElQorchi et al., 2003; Maimbo, 2003, 2005), although payments due in remote rural areas usually require more time, and they may take up to 48 hours (Passas, 2004). Sometimes hawaladars are able to deliver funds within very few hours.

Generally, telecommunication and information technological advancements have greatly benefited the development of this informal system. Payment orders can be sent by facsimile, telephone, or e-mail which very fast compared to when using the banks. It must be noted, however, that because the system is based on trust, modern telecommunication is not a prerequisite.

2.3.2 Cheap Money Transfer System

Hawala Systems are very inexpensive to use compared to banks and because of this factor, the client base does extend beyond nationality to include others from northeastern African (Maimbo, 2006). For example, it is not weird or unheard of for fellow Kenyans, Ethiopians, Eritreans or Sudanese clients to make use of Somali Hawala remittance companies like Dahabshiil, Amaana, Mustaqbal or even Express Hawala systems (The researcher 2013).
Hawala costs are always much lower than the fees charged in the formal banking System like the banks such as Barclays or even Standard chattered. El Qorchi et al. (2003) state that the cost of a hawala transaction averages around 2 to 5 percent of the total amount of the funds involved, although Maimbo (2005) report that these fees averaged 1 to 2 percent in Afghanistan. Passas (1999) offers several examples where hawaladars offer free services to their compatriots, in the corridor Australia-Africa, like Kenya. The cost of transferring money through the hawala remittance system is less than that of a wire or bank transfer. While a formal money transfer (like Western Union) or bank might charge 12% for transfer services, informal business like the hawala remittance systems charge 3-5%. Often a hawala transaction remains less expensive than payments made through the formal banking sector. The reason is related to the system’s limited overheads and the virtual lack of regulation and taxation. The infrastructure needed by a hawaladar to conduct business is simple in comparison with that of banks involved in international payment transactions or even of money changers. Also hawala exchange rates are more competitive and appealing than official rates (Passas, 2005).

Hawaladars often need little more than a table, phone, facsimile machine, or—for the most sophisticated an internet connection, Unlike banks, little, if any, consideration is given to the commercial and tax aspects of accounting obligations or for the principles of formal accounting procedures. It is the cheapest and also the most reliable financial transfer system which has been used by not only the Somali businesses in Eastleigh but also overseas workers sending remittances for their families in Kenya, Somalia, Uganda and many other countries (Passas, 2006).

2.3.3 Versatility Issues

Hawala transactions, which is an informal sector is better suited and highly adaptable to conditions of wars, civil unrest, conflicts, economic crisis, weak or nonexistent banking systems, areas that have fragmented markets, where it is not easy to get information on smaller clients, that are considered to be risky by formal financial sectors, making it easier for them to find willing lenders like the hawala lenders (Fowowe, 2008).
The Hawala systems are totally based on strong communal ties and family values, where there is a lot of trust and good values and it is through these shared values that self-regulation becomes possible and, in fact, it is very effective (Schaeffer, 2008).

Hawaladars have always maintained their operations under extreme circumstances even when sometimes the formal banking system has not been able to adapt and ceased to operate. For instance, in Somalia after the Siad Barre government was deposed in 1991, commercial banks collapsed and hawala was the only financial system in the country (Houssein, 2005; Lindley, 2009).

Similarly during the Taliban period in Kabul, the country’s formal banking system was not operational and hawaladars were the only active financial operators (Maimbo, 2005). These extreme circumstances show how in the context of institutional collapse, informal structures such as hawala may constitute a source of regulatory order.

Hawala money transfer systems have also been used in the past by humanitarian organizations such as the United Nations agencies and nongovernmental organizations (NGOs) to get urgent humanitarian funds into countries that don’t have a reliable banking infrastructure due to war or even ethnic or tribal troubles. This has been documented by (Dahabshiil, 2012).

2.3.4 Cultural Convenience

The Hawala system encouraged cultural ties especially in rural areas where, rare dialects and a general distrust of outsiders act as a barrier to entry (Bowers, 2009, p. 384). These informal banking systems called hawalas are able to thrive in areas where trust among community members and group solidarity builds a trust that leads to the development of these networks. These informal lenders rely mostly on personal, social as well as business relationships in their collection of important information regarding potential borrowers (Steel et al., 2007). These shows that there are limited possibilities of providing insurance at the community or society level as well as the monopoly power which brings about high inefficient spreads of loans (Ghate, 2012).
Language and educational barriers that Somalis face in new countries like here in Kenya may make someone uncomfortable dealing with banks and filling out forms to send money or even opening an account. Cultural considerations also apply to family members in the hawala recipient country and shape social rules and behaviors, including respect of confidentiality and privacy. It is through these shared values that self-regulation becomes possible and, in fact, it is very effective (Schaeffer, 2008).

The client base does extend beyond nationality to include others from northeastern African. For example, it is not weird or unheard of for fellow Kenyans, Ethiopians, Eritreans or Sudanese clients to make use of Somali Hawala remittance companies like Dahabshiil, Amaana, Mustaqbal or even Express Hawala systems (The researcher 2013).

2.4 The Challenges faced by Hawala Systems

2.4.1 Government Issues

The government can limit or even worst case scenario foreclose entry of the informal financial sectors like the Hawala systems into industries by use of tools like licensing requirements (Porter, 1998).

Influencing major government decisions is a well known strategic move as long it is done in a transparent way and with integrity, and so any corporate strategy that doesn’t take this into account as part of the history of the government, is totally ignoring a very important environment of politics (Lynch, 2000).

According to Thompson, Strickland and Gamble (2005), Government actions can force important changes in industry practices and strategic approaches, for example, the government through the Central Bank of Kenya (CBK) have introduced some new rules requiring the operators of cash remittance like the hawala remittance firms to register with Central Bank of Kenya and pay a Sh5 million licensing fee in addition to maintaining a minimum core capital of Sh20 million.

Financial sector experts even said that the rules are targeted at Hawala, a system of money remittance that involves transfer of cash without any records of parties involved in the transactions. The Central Bank of Kenya has outlawed money remittance businesses
that operate without license, in a raft of new regulations that could drive out of business hundreds of informal operators especially the hawala systems in eastleigh in which Somali businesses in that area rely on, in the sector.

According to John Wanyela, who is the chairman advisory of the financial reporting centre; the Kenyan Government has tried to tighten business regulation around outflow and inflows in the country due to unlicensed and unformalised Hawala systems, whose transaction cannot be traced back as Hawala operators do not keep any financial records (CBK, 2012).

2.4.2 Legal Issues

Government legislation can influence the environmental regulations with which informal financial industries must comply, this can either benefit or damage an industry (Dess, Lumpkin and Eisner, 2006).

The hawala systems are commonly used in order to commit crimes which violate tax and other laws because informal hawala transactions are unrecorded in national accounts and other statistics, the data available to policy-makers would not offer an accurate description of the economic and monetary situation of a country and would tend to limit the effectiveness of their policies (Global Policy Forum, 2009).

Furthermore, people have found ways to abuse the hawala system. While accounting for a relatively small amount of hawala usage overall, these illegal applications have dominated media coverage of the system. Tax evasion and fraud are among the ways that hawala can be exploited (Passas, 2006); however these infractions are relatively minor in comparison to other potential abuses of the system.

A hawala transaction is a balance of payment transaction, not because “money is sent” across borders or there is any recorded purchase or sale of foreign exchange, but because the transaction is intrinsically linked to changes in international assets and liabilities. However, while hawala and other IFT transactions are conceptually part of national BOP accounts, accurate compilation is almost impossible. According to Sundaresan (2009), heavy or tight regulations by the government can eliminate any innovation and this
stimulates financial intermediation outside the formal financial transaction, and hence leading to informal financial transactions.

Nevertheless, even though national authorities are unable to directly maintain records of informal financial transfers, the indirect effects of these transactions on monetary aggregates and operations, as well as on the balance of payments, should be taken into consideration. The hawala systems can face legal issues since it reduces the amount of statistical information available to policy-makers on the level of economic activity in the country because of unrecorded data, however, despite its potential for negative use, hawala’s informality should not be confused with illegality (Viles, 2008).

2.4.3 Security Issues

The hawala remittance systems face a lot of security issues like for example theft, where thieves can easily break into them since these hawala systems are not guided by trained security personnel with the right materials, who are able to deal with dangerous robbers that want to steal the money from the hawala dealers, as opposed to banks that have the suitable trained security personnel who know what to do in case of theft or break ins robberies.

2.4.4 Vulnerability to Money Laundering Activities

The secrecy and opacity that surrounds hawala transactions have triggered the fear and mistrust of the West. Financial authorities (FATF, 2005) claim that informal financial practices like hawala could be easily misused for transmitting ill-gotten money, generated by different kinds of criminal, illegal and unethical activities.

However, hawala is vulnerable to criminal abuse, just like all other financial institutions (Passas, 2005), and more serious crimes are being committed through formal channels, including trade and financial intermediaries. Moreover, terrorist operations are often cheap as “a great deal of serious harm can be accomplished with just a few hundred US dollars, which are extremely easy to hide from anyone complying strictly with all current rules” (Passas, 2006a).
However this is not an excuse to leave hawaladars operate without any sort of control or surveillance. As it was clearly stated in the Abu Dhabi Declaration on Hawala (U.A.E Central Bank, 2002), it is vital to ensure that the system is not abused by money launderers and terrorist financiers.

Both the formal banking sector and the IFT like the hawala systems are vulnerable to abuse. The number and variety of methods used to launder the proceeds of criminal and illegal activities and finance terrorist acts continue to become more complex with time. The methods are diverse and can employ both banking and non-banking channels including exchange bureaus, check cashing services, insurers, brokers, and non-financial traders (FATF, 2005). The methods through which IFTs and the formal banking sector can contribute to the placing and layering of funds in the money-laundering process are similar, although, as discussed below, the informal transfer systems like the hawala remittance systems have peculiarities, which make them particularly more vulnerable. Firstly, hawala remittance system necessarily involves the physical transfer of funds from one jurisdiction to another. Instead, they depend on a series of accounting debits and credits between the accounts of a network of individuals, companies, accountants, lawyers, and intermediaries. Secondly, the hawala systems minimize detection risk because of little or no documentation at all and in the case where hawala dealers maintain records, the records are generally not accessible to the law enforcement officers.

2.5 Chapter Summary

The chapter discussed the reviewed literature based on the research objectives, which were; the role of the hawala systems to Somali businesses like operation of business, growth and development, factors motivating Somali businesses to use the hawala system i.e. speed, convenience, versatility, and challenges faced by the hawala system like government issues, legal and security issues. The aim of the study was to find out whether Hawala Remittance Systems had implications on the Somali businesses in Eastleigh. The next chapter will present the research methodology used in this study.
CHAPTER THREE

3.0 RESEARCH METHODOLOGY

3.1 Introduction

This chapter determines the process that led to the research design selection in this research project and also gives an outline of the research methodology by giving a description about the source data, method of conducting the research, the population, the sample, technique of collecting the data and also the technique of analyzing the data.

3.2 Research Design

This research project adopted a descriptive research design defined by Burns and Bush (2010) as a set of methods and procedures that describe variables, while Churchill and Brown (2007) stated that descriptive research design was concerned with determining the frequency with which something occurs or relationships between variables. The descriptive design follows the post positivist paradigm of Lincoln and Guba (1985) which emphasized the importance of the phenomenological, inductive, and contextual approach to inquiry for research into human experience.

Descriptive research design was appropriate because it gave adequate results between two or more variables. In this study, the implication of the Hawala Remittance System was the dependent variable, whereas the role, factors and the challenges of the Hawala System were the independent variables. It was specific since it was a case study that was based in Eastleigh. Furthermore, the study also used an aspect of the quantitative method even though qualitative method remained central to the entire case study, simply because the data explains the outcome in an evaluative way.

3.3 Population and Sampling

3.3.1 Population

Population is defined as the whole set of objects or events under investigation about which we wish to make inferences (Saunders and Thornhill, 2003). Furthermore, according to Cooper and Schindler (2008), a population is the total collection of elements which we wish to make inferences. Mugenda and Mugenda (2003) define it as the entire
group of individuals, events or objects having in common observable characteristics. The population of this study consisted of the Somali business people, hawala owners, hawala dealers and users based in Eastleigh. The subjects and participants of this study were homogeneous and constituted of only business people of the Somali origin living and working in Eastleigh, Nairobi, Kenya. The size of the business population in Garissa lodge business area in Eastleigh as at 2013 was a total of 270 people.

3.3.2 Sampling Design

3.3.2.1 Sampling Frame
Sampling frame refers to a complete list of all the cases in the population from which the sample will be drawn. (Saunders et al, 2003). According to Churchill and Brown (2007), a sampling frame could be a list of geographical areas, institutions, and individuals. The sampling frame of this study was selected from a list of various Somali business people that were involved in different businesses like the clothing, shoes, bags and the jewellery business and also from hawala dealers from different hawala remittance systems in Eastleigh. The source of the Sampling frame was a list that was worked on by the researcher when the study was conducted.

3.3.2.2 Sampling Technique
This study utilized the simple random sampling method which gave the researcher a fair view of the entire population. In addition, this technique enabled the researcher to have an in depth study and insight on the topic being studied (Merriam, 2003). A random sample is a subset of individuals that are randomly selected from a population where by each individual is chosen entirely by chance and each member of the population has a known but possibly non-equal chance of being included in the sample. Random sampling frequently minimizes the sampling error in the population. This in turn increases the precision of any estimation methods used (Schindler, 2008). Pratt and Loizos (1992) argue random sampling technique is appropriate where the population is known and can be classified into homogeneous data.

3.3.2.3 Sample Size
Patten (2004), states that obtaining an unbiased sample is the main criterion when evaluating the adequacy of a sample. Patten also identifies an unbiased sample as one in
which every member of a population has an equal opportunity of being selected in the sample. Therefore, random sampling was used in this study to help ensure an unbiased sample population. Saunders et al, (2005) advocates a confidence level of 95% to be employed which means that if the sample is selected 100 times at least 95 of these samples should be certain to represent the characteristics of the population.

According to Cooper and Schindler, (2008) a sample of 30% was considered representative enough to allow for generalization of the data for the whole target population. Because random sampling may introduce sampling errors, efforts were made to reduce sampling errors, and thus increasing precision, by increasing the sample size. The total sample size of this research was 30 out of a population of 270 people.

3.4 Data Collection Methods

The study used questionnaires to collect data, which solicited primary personal and business data from respondents. It was a good method that made sure that all relevant and important areas of research objectives were addressed. Some Structured and Unstructured questions were used because they provide more information as the respondents express their thoughts freely and spontaneously (Saunders et al, 2005).

The questionnaires contained open ended questions, where the respondents were allowed to answer the required questions. With the open ended questions, the respondent was able to provide answers to the questions. This allowed for collection of large amounts of data within a short time and also anonymity of the respondents. The use of questionnaires offered an effective way of collecting information from a large sample in a short span of time than other methods, that are time consuming and tiresome. Section one of the questionnaires gave the general information, section two, the Role of the Hawala System in Somali Businesses, section three, Factors motivating the Somali Businesses to use Hawala and finally, section four, Challenges faced by the Hawala System.

3.5 Research Procedure

A set or series of actions directed to some end or a natural series of changes; a procedure is a series of actions conducted in a certain manner, an established way of doing something.

The key problems and events were anticipated, key Somali business people and hawaladars were identified, letters of introduction were prepared, rules of confidentiality
were established before collecting the data in order to actively seek opportunities to revisit and revise the research design so as to address and add to the original set of research objectives.

The questionnaires that were designed based on the research questions were pre-tested during the pilot study, which aids the success and accuracy of the final study and offers the researcher the opportunity to fine-tune the document (Leedey, 2005).

Focused, short and repeated interviews were also conducted in order to gather additional data to cross check facts. To improve the response rate, a cover letter explaining the reason why the research is being conducted, why the research is very important, why the recipient was selected and a guarantee of the respondent confidentiality was provided. The questionnaire took an average of twenty minutes to complete.

3.6 Data Analysis Methods

The study used frequency distribution, which fits the study because of the use of descriptive design. Questionnaires were used to collect data, which was thoroughly edited, formatted and cleaned in order to detect mistakes like spelling mistakes and omissions that might interfere with the accuracy of the data, analyzed using percentages and presented in frequency tables. It was then transformed into quantitative form through coding which made analysis easy before it was entered into computer statistical software, (Statistical Package for Social Sciences) for analysis of the data. Finally the analyzed data was summarized and presented in form of tables and figures for ease of interpretation for the readers who would want to make use of these research data.

3.7 Chapter Summary

The chapter described the methodology of research that was used by the study. Descriptive research design was used; sample size of the study was 30, where simple random sampling was used. The data was collected using the questionnaires that were designed based on the three research objectives outlined in the study. The population consists of Somali business people that were involved in different businesses like the clothing, shoes, bags and the jewellery business and also from hawala dealers from different hawala remittance systems in eastleigh. The sample frame, size and techniques used were identified. Data was analyzed using SPSS and summarized for presentation in tables and figures. Chapter four will present the results and findings of the research study.
CHAPTER FOUR

4.0 RESULTS AND FINDINGS

4.1 Introduction

This Chapter discusses the results and findings on the implications of the hawala remittance system to the Somali businesses. Section 4.3 gives detailed information on the role of the hawala system in Somali businesses. Section 4.4, identifies the factors that motivate the Somali businesses especially in Eastleigh to use the hawala system as a financial transaction. Section 4.5, assesses the challenges faced by the hawala system as a financial transaction system. Finally section 4.6 gives the chapter summary which gives a brief recapture highlighting the various research objectives.

4.2 Demographic Characteristics / General information

In this section, data collected was analyzed using descriptive statistics to establish the demographic characteristics of the respondents.

4.2.1 Age of Respondents

As shown in table 4.1 below, the study showed that 40% of the respondents who had owned or worked for the business in eastleigh were between the ages of 31 and 35 years old, 33% were between the ages of 26 to 30 years old, 23% were at the age of 36 and over, while only 3% were between the ages of 20 – 25 years old. This shows that a total of 63% of the respondents were above 31 years and over, as showed in table 4.1 below.

Table 4.1: Age of Respondents

<table>
<thead>
<tr>
<th>Age group</th>
<th>Frequency</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>20 - 25 years</td>
<td>1</td>
<td>3.3</td>
</tr>
<tr>
<td>26 - 30 years</td>
<td>10</td>
<td>33.3</td>
</tr>
<tr>
<td>31 - 35 years</td>
<td>12</td>
<td>40</td>
</tr>
<tr>
<td>36 and over</td>
<td>7</td>
<td>23</td>
</tr>
<tr>
<td>Total</td>
<td>30</td>
<td>100</td>
</tr>
</tbody>
</table>
4.2.2 Gender of Respondents

Table 4.2 showed below presents a summary of the findings in regards to the gender of the respondents. The study showed that 66.7% of the respondents were males and 33.3% were females.

**Table 4.2: Gender of Respondents**

<table>
<thead>
<tr>
<th>Gender</th>
<th>Frequency</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Male</td>
<td>20</td>
<td>66.70%</td>
</tr>
<tr>
<td>Female</td>
<td>10</td>
<td>33.30%</td>
</tr>
<tr>
<td>Total</td>
<td>30</td>
<td>100%</td>
</tr>
</tbody>
</table>

4.2.3 Number of Years in Business

The study shows that 50% of the respondents who had owned or worked for the business in eastleigh have owned or worked between 6 and 8 years. 30% were under the bracket between 3 to 5 years, 13.3% of the respondents had owned or worked for the business between 0 and 2 years, as illustrated in table 4.3 below.

**Table 4.3: Number of Years of Ownership or Work in Business**

<table>
<thead>
<tr>
<th>Number of years in Business</th>
<th>Frequency</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>0 - 2 Years</td>
<td>4</td>
<td>13.3</td>
</tr>
<tr>
<td>3 - 5 Years</td>
<td>9</td>
<td>30</td>
</tr>
<tr>
<td>6 - 8 Years</td>
<td>15</td>
<td>50</td>
</tr>
<tr>
<td>9 Years and Over</td>
<td>2</td>
<td>6.7</td>
</tr>
<tr>
<td>Total</td>
<td>30</td>
<td>100%</td>
</tr>
</tbody>
</table>

4.2.4 Education Background

The findings in table 4.4 showed that 50% of the respondents who had owned or worked in businesses in eastleigh were holders of secondary certificates. During the interview, it was found out that after completion of secondary, most of the respondents went straight to starting their own business or get hired to work in the businesses in eastleigh, in order to
provide for their families or parents. Only 30% and 6% got a chance to pursue higher graduate and post graduate degrees respectively, compared to the 13 % who only managed to complete their primary education.

Table 4.4: Education background

<table>
<thead>
<tr>
<th>Education Background</th>
<th>Frequency</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Primary</td>
<td>4</td>
<td>13.3</td>
</tr>
<tr>
<td>Secondary</td>
<td>15</td>
<td>50</td>
</tr>
<tr>
<td>Graduate</td>
<td>9</td>
<td>30</td>
</tr>
<tr>
<td>Post Graduate</td>
<td>2</td>
<td>6.7</td>
</tr>
<tr>
<td>Total</td>
<td>30</td>
<td>100</td>
</tr>
</tbody>
</table>

4.3 The Role of the Hawala System in Somali Businesses

The study sought to find out whether Hawala has any role in Somali Businesses in Eastliegh. It presents detailed information on the various roles mentioned in the literature review and considered relevant by the researcher.

4.3.1 Operation of Business

The study showed that 76.7% and 16.7% of the respondents disagree or strongly disagreed with this statement that says that hawala remittance systems play a role in the operations of businesses in eastliegh, while 6.7% strongly agreed with the statement.

Figure 4.1: Operations of Business
4.3.2 Development and growth

The findings for this study showed that a total of 93.3% did not agree with this statement that says that hawala systems lead to the development and growth of businesses in eastliegh, the respondents said that it only helps them in the execution of financial transactions that is very fast, but doesn’t help them in growing their businesses. In this case, it was found out that the respondents take loans from Islamic banks like gulf bank to grow and expand their business.

![Development and growth](image)

**Figure 4.2: Development and Growth**

4.3.3 Banking system

It was found out that 96.7% of the respondents agreed that hawala systems are also used as banking system, where these respondents deposit huge amounts of money in dollars in these systems after making profits from their businesses in eastliegh, before they transfer to a normal bank account safely. It is also used when transferring money from one country like Dubai to another country like China or Kenya, when making business deals and exchanges.

![Banking system](image)

**Figure 4.3: Banking System**
4.3 Role of Hawala System in Somali Businesses

The study sought to find out the Implications of Hawala system to Somali Businesses in Eastliegh. The data collected was transformed into quantitative form through coding which made analysis easy before it was entered into computer statistical software, (Statistical Package for Social Sciences) for analysis of the data. Finally the analyzed data was summarized and presented inform of tables shown. The findings of whether Hawala has a major role in Somali Businesses are represented below. The hypothesis is stated as follows:

Ho: Hawala system does not play a major role in the Somali Businesses in EastLiegh

H1: Hawala system does play a major role in the Somali Businesses in EastLiegh

The results showed that the significance level is 0.000 (P>0.05) which is within the acceptable level. We therefore, accept the alternative hypothesis and reject the Null hypothesis. This means that Hawala plays a major role in Somali Businesses as a Banking system.

Table 4.5: Role of Hawala System in Somali Businesses

One-Sample T-Test

<table>
<thead>
<tr>
<th>ROLE OF HAWALA SYSTEM</th>
<th>t</th>
<th>df</th>
<th>Sig. (2-tailed)</th>
<th>Mean Difference</th>
<th>95% Confidence Interval of the Difference</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>28.370</td>
<td>29</td>
<td>.000</td>
<td>2.75556</td>
<td>2.5569, 2.9542</td>
</tr>
</tbody>
</table>
4.4 Factors motivating the Somali Businesses to use Hawala System

4.4.1 Speed of Service Delivery

The research showed that a total of 96.6%; (73.3% agree and 23.3% strongly agree) of the respondents agreed that the hawala remittance system is very fast in terms of financial transactions in businesses. Furthermore, it was practically found out that it transacts financial activities for these businesses in a very fast and efficient way compared to the banks, it only takes 15 minutes or less to finish a transaction compared to the banks that take hours, days or even weeks to do the same transaction because of the long procedures involved in these banks, and as a result a business person can truly loose an opportunity because of these speed factor in the banks!

![Figure 4.4: Speed of Service Delivery](image)

4.4.2 Cheap Transactions

The study showed that; 40% and 56.7 agreed or strongly agreed that hawala remittance systems are cheaper in financial transaction activities compared to the banks, where you have to queue and wait for longer when transacting, while only 3.3% of the respondents disagree. I personally carried out hawala transaction and found out that the cost of transferring money through the hawala remittance system is less than that of a wire or bank transfer, for one to send 50 dollars via the hawala system, you are only charged 1 dollar, for sending 100 dollars, you are charged 2 dollars only!
The research carried out showed that 33.3% and 63.3% agreed or strongly agreed that the hawala transactions are highly adaptable to conditions of wars, civil unrest, conflicts, economic crisis, weak or nonexistent banking systems, as well as economic sanctions and blockades.

Figure 4.6: Versatility of the System
4.4 Factors Motivating the Somali Businesses to use Hawala System

Ho: Factors (speed, cheap, versatility) don’t motivate Somali Businesses to use Hawala System.

H1: Factors (speed, cheap, versatility) do motivate Somali Businesses to use Hawala System.

The results showed that the significance level is 0.000 (P>0.05) which is within the acceptable level. We therefore, accept the alternative hypothesis and reject the Null hypothesis. This means that factors (speed, cheap, versatility) do motivate Somali Businesses to use Hawala System.

Table 4.6 Factors Motivating the Somali Businesses to use Hawala System

<table>
<thead>
<tr>
<th></th>
<th>Test Value = 0</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>T</td>
</tr>
<tr>
<td>PARTIIIIFACTORS</td>
<td>37.676</td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
</tbody>
</table>

4.5 The Challenges faced by Hawala systems

4.5.1 Government Issues

From figure 4.7 below, it can be seen that 56.7% and 40% of the respondents agreed or strongly agreed that there are a lot of government restrictions on hawala remittance systems.
4.5.2 Legal Issues

The findings showed that 16.7% and 76.7% strongly disagreed, disagreed respectively, meaning a total of 93.4% of the respondents disagreed that hawala is used to commit crimes like violating taxes or enabling rich citizens and corporations to escape the national tax system. On the other hand only 6.6% of the respondents agreed that it faces legal issues from the government.
4.5.3 Security Issues

Figure 4.9 showed that 26.7% and 66.7% of the respondents disagreed that the hawala system faced a lot of security issues like for example theft, where thieves could easily break into them since these hawala systems were not guided by trained security personnel with the right materials, who were able to deal with dangerous robbers that would want to steal the money. These respondents included hawaladars that had put in place strict security measures to avoid losses due to theft.

![Security Issues](image)

**Figure 4.9: Security Issues**

4.5.4 Vulnerability to Money Laundering Activities

From the study conducted, the findings showed that 26.7% and 53.3% (a total of 90%) disagreed that the hawala remittance systems are used to launder money, which is an illegal transfer of money from one country to another. Only 10% of the respondents agree that some but not all of the hawaladars transact illegal money via the hawala systems, in order to make more money.

![Vulnerability to money laundering](image)

**Figure 4.10: Vulnerability to Money Laundering Activities**
4.5 The Challenges faced by Hawala System

Ho: Hawala system doesn’t encounter challenges such as government issues, legal, security and Money laundering issues.

H1: Hawala system does encounter challenges such as government issues, legal, security and Money laundering issues.

The results showed that the significance level is 0.000 (P>0.05) which is within the acceptable level. We therefore, accept the alternative hypothesis and reject the Null hypothesis. This means that Hawala system does encounter challenges such as government issues.

Table 4.7 The Challenges faced by Hawala System

<table>
<thead>
<tr>
<th>PARTIVCHALLENGES</th>
<th>t</th>
<th>df</th>
<th>Sig. (2-tailed)</th>
<th>Mean Difference</th>
<th>95% Confidence Interval of the Difference</th>
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<tr>
<td></td>
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<td>2.5167</td>
<td>2.3542 - 2.6792</td>
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4.6 Chapter Summary

This chapter presented the results and findings in relation to the three research objectives that were gathered from the questionnaires distributed to the respondents. The data gathered was entered into SPSS software for easy analysis of the data. Data was then presented in form of frequency tables and figures. The next chapter will present the discussions, conclusions and recommendations of the research study carried out.
CHAPTER FIVE

5.0 DISCUSSIONS, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

This chapter gives a summary of the findings of the study, draws interpretation and conclusions based on the research objectives. In the end the chapter concludes by providing recommendations for improvements and further studies.

5.2 Summary

The general objective of the study was to determine the implications of the Hawala Remittance System to Somali Businesses in Eastleigh. The specific objectives of the research study were to: determine the role of the hawala remittance system to Somali Businesses, identify the factors that motivate Somali Businesses and money senders to use Hawala remittance system as an alternative financial transaction and to assess the challenges faced by the Hawala as a remittance system.

The research design employed was the descriptive research design that focused on the Somali business people, money senders and hawala dealers based in Eastleigh. The population of the study comprised of 270 respondents and simple random sampling was used to obtain a sample size of 30 from the population of interest. Data was collected using questionnaires that were designed based on the research objectives and upon completion, analyzed using SPSS and Microsoft Excel. Findings were then presented in the form of tables of frequency distributions and figures for easier interpretation.

In chapter four, which talked about the results and findings, the study carried out shows that hawala systems were used for banking purposes, for example It was found out that 96.7% of the respondents agreed that hawala systems were also used as banking system, where these respondents deposited huge amounts of money in dollars in these systems after making profits from their businesses in eastleigh, before they transferred to a normal bank account safely, on the other hand, The study shows that 76.7% and 16.7% of the respondents disagreed or strongly disagreed with the statement that said that hawala remittance systems played a role in the operations of businesses in eastleigh, while only 6.7% strongly agreed with the statement. The findings showed that some of the
challenges faced by hawala remittance systems don’t happen oftenly, for example the study on money laundering in relation to hawala systems showed that 26.7% and 53.3% (a total of 90%) disagreed that the hawala remittance systems are used to launder money, which is an illegal transfer of money from one country to another. Only 10% of the respondents agreed that some but not all of the hawaladars transact illegal money via the hawala systems, in order to make more money. The findings also showed that a total of 93.4% of the respondents disagreed that hawala was used to commit crimes like violating taxes or enabling rich citizens and corporations to escape the national tax system. On the other hand only 6.6% of the respondents agreed that it faced legal issues from the government.

Furthermore, the study was able to investigate on the factors that motivate the Somali business people or workers to use the hawala systems for financial transaction purposes, and it showed that it is faster and cheaper compared to banks, for instance; the research showed that a total of 96.6%; (73.3% agree and 23.3% strongly agree) of the respondents agreed that the hawala remittance system was very fast in terms of financial transactions in businesses, while 40% and 56.7 agreed or strongly agreed that hawala remittance systems were cheaper in financial transaction activities compared to the banks, where you have to queue and wait for longer when transacting, while only 3.3% of the respondents disagreed.

The researcher carried out hawala transaction by sending money from Nairobi to Mogadishu, and found out that the cost of transferring money through the hawala remittance system was less than that of a wire or bank transfer, for one to send 50 dollars via the hawala system, you are only charged 1 dollar, for sending 100 dollars, you are charged 2 dollars only!

5.3 Discussions

This section gives a discussion based on the specific research objectives. The research findings are also compared with the literature review.

5.3.1 The Role of the Hawala System in Somali Businesses

The study assessed the following as roles of hawala systems; operations of business, development, growth and banking system. In the literature review, it was discussed that businesses in Eastleigh operate on the hawala system of money transfer, since many
Somali business transactions associated with Hawala were done in the area of import and export businesses especially in the clothing and shoes stores in Eastleigh. The findings showed that Hawala remittance systems especially in eastleigh don’t lead to the development and growth of many Somali businesses; this refutes what has been brought forward by Passas (2006) who articulates that Hawala remittance systems led to the development of Somali Businesses.

However after conducting in depth interviews and data collection using questionnaires, the findings revealed that Hawala systems don’t play a major role in the operation of businesses in eastleigh, this findings was not in line with the sentiments brought forward by Robinson (2008), who argues that Businesses in Eastleigh prefer to use the Hawala for the operation of business since no collateral is involved due to repayment constraints, and further says that there may be periods when the borrower’s capacity to repay the debt is constrained.

After conducting in depth interview with Mr. Afrah Shuriye, who was in the real estate business in eastleigh, it was found out that, Islamic banks like first community bank and also gulf bank were major financers of eastleigh businesses as opposed to the hawala systems that only facilitated faster money transfers and transactions from one country to another but didn’t offer loans!

These findings were not in line with Fight (2008), who states that the commercial banks put heavy reliance on the customers’ financial statements, when granting them loans to develop and grow their businesses, as a result making it easier for Hawala dealers who don’t put any heavy reliance on the customer’s financial statements, to grant customers loans, to develop and grow their business.

The study conducted showed that hawala had infact the role of being used as a banking system, where these respondents deposited huge amounts of money in dollars in these systems after making profits from their businesses in eastleigh and later on access it easily without any long procedures involved. Furthermore it revealed that according to the Somali business people involved in different kinds of businesses like clothing, shoes, designer bags or the food sector in eastleigh themselves, who had filled the questionnaires, Hawala acted as a banking system for them. This is in line with Nihar
(2002), who argues that Hawala is used as a banking system, where Somalis who have no
Accounts in the formal financial like banks, use it to keep their money for sometime
before they access it and use it to conduct their businesses. When these businesses sold
their goods like the gold jewellery, clothes, bags or even shoes and get huge profits, they
deposited it to the hawala of their choice whether it is Dahabshiil or Mustaqbal, just like
the way business people who have accounts with any bank like Barclays or equity banks
in Kenya deposit their money for safe keeping.

5.3.2 Factors motivating the Somali businesses to use Hawala System

The literature review discussed factors such as speed of service delivery, cheap
transaction system and versatility issues. In the case of speed, the findings revealed that a
majority of the respondents agreed that the hawala remittance system was very fast in
terms of financial transactions in businesses.

It transacts financial activities for these businesses in a very fast and efficient way
compared to the banks, it only took 15 minutes or less to finish a transaction compared to
the banks that took hours, days or even weeks to do the same transaction because of the
long procedures involved in these banks, and as a result a business person can truly loose
an opportunity because of these speed factor in the banks! These findings are in line with
Elqorchi (2003), who argues that Hawala transactions are usually completed within 24
hours, compared to banks, that take up to two to three days.

The findings revealed that hawala remittance systems were cheaper in financial
transaction activities compared to the banks, where you have to queue and wait for longer
when transacting. The reason was related to the system’s limited overheads and the virtual
lack of regulation and taxation. The infrastructure needed by a hawaladar to conduct
business was simple in comparison with that of banks involved in international payment
transactions or even of money changers.
This is in line with Maimbo (2006) who argues that Hawala Systems are very inexpensive to use compared to banks and because of this factor, the client base does extend beyond nationality to include others from northeastern African. For example, it is not uncommon for Kenyans, Ethiopians, or Sudanese clients to make use of Somali Hawala remittance companies like Dahabshiil, Amaana, or Mustaqbal.

The study also revealed that, Hawala was the cheapest and also the most reliable financial transfer system which had been used by not only the Somali businesses in Eastleigh but also overseas workers sending remittances for their families in Kenya, Somalia, Uganda and many other countries. This is in line with Passas (1999) offers several examples where hawaladars offer free services to their compatriots, in the corridor Australia-Africa, like Kenya.

The findings revealed that the hawala transactions were highly adaptable to conditions of wars, civil unrest, conflicts, economic crisis, weak or nonexistent banking systems, as well as economic sanctions and blockades. This is in line with Pathak (2003) who argues that Hawala networks are based on strong regional, ethnic, or familial relationships. The finding is also in agreement with Schaeffer (2008) who argues that it is through these shared values that self-regulation becomes possible and, in fact, it is very effective.

According to the literature review the money from hawala funded an estimated 80% of start up capital for businesses in the country, where external financing through other means was not an option (Chalmers & Hassan, 2008).

The findings revealed that Hawala channels were used by other Organizations, and this is in line with Dahabshiil (2002) which revealed that Hawala channels were also used by United Nations agencies and non governmental organizations (NGOs) to get emergency and humanitarian funds into countries that lack reliable banking infrastructure.

5.3.3 The Challenges faced by Hawala Systems

Some of the challenges discussed in the literature review were: government issues, legal issues, security issues, and money laundering issues.

It was found out that the rules were targeted at Hawala, which is a system of money transfer that involved transfer of money from one location to another, for instance, transferring money from Kenya to Somalia or Tanzania.
The findings showed that there were a lot of government restrictions on hawala remittance systems. This is in line with Porter (1998), who argues that the government can limit or even worst case scenario foreclose entry of the informal financial sectors like the Hawala systems into industries by use of tools like licensing requirements (Porter, 1998).

The findings above is also in line with Thompson, Strickland 111 and Gamble, (2005), who argue that the Government actions can force important changes in industry practices and strategic approaches, in order to protect the local industries and discourage competition from other financial transactions like the Hawala system.

The findings revealed that Hawala system did not face legal issues; this is not in line with Dess, Lumpkin and Eisner, 2006) who argue that the Government legislation can influence the environmental regulations with which informal financial industries must comply, this can either benefit or damage an industry.

The literature review discussed that there are some people who have found ways to abuse the hawala system. In contrast, the findings revealed that Hawala system did not face any legal issues, This is not in line with Passas(2006), who argues that tax evasion and fraud are among the ways that hawala can be exploited. Further more it is not in line with Thompson (2006), who also argues that hawala can facilitate the funding of illegal activities or the laundering of those activities’ proceeds.

The findings revealed that Hawaladars face a lot of police harassment most of the time, who only wanted to extort money for their own selfish gains; they had no choice but to give them almost 20,000 to 30,000 to continue with their business and to shake these police men off their back.

The findings revealed that Hawala system did not face security issues like theft; it was found out that Hawaladars have put strict security measures. For example, it was discovered that Dahabshiil has hired security guards, who screen customers before letting them into the building to conduct their businesses. This is not in line with Passas (2006), who argues that Hawala systems face security issues.
Findings revealed that Hawala system is not vulnerable to money laundering, this shows that the findings is not in line with Passas (2005) who states that hawala is vulnerable to criminal abuse, just like all other financial institutions, and more serious crimes are being committed through formal channels, including trade and financial intermediaries. Moreover, terrorist operations are often cheap as “a great deal of serious harm can be accomplished with just a few hundred US dollars, which are extremely easy to hide from anyone complying strictly with all current rules.

5.4 Conclusions

5.4.1 The Role of the Hawala System in Somali Businesses

After data collection, the study showed that a majority of the respondents agreed that hawala didn’t play a major role in the operations of businesses in eastleigh compared to Islamic banks like gulf bank, that provided them with free interest loan, which these business people used it to operate and grow their businesses.

However, hawala had the role of acting as a banking system, where by, it was found out that the respondents agreed that hawala systems are also used as banking system, where these respondents deposited huge amounts of money in dollars in these systems after making profits from their businesses in eastleigh and later on accessed it easily without any long procedures involved.

5.4.2 Factors motivating the Somali Businesses to use Hawala System

The findings showed that a total of 96.6% of the respondents agreed that the hawala remittance system was very fast in terms of financial transactions in businesses. Furthermore, it was practically found out that it transacts financial activities for these businesses in a very fast and efficient way compared to the banks, The study also showed that; 40% and56.7 agreed or strongly agreed that hawala remittance systems were cheaper in financial transaction activities compared to the banks.

5.4.3 The Challenges faced by Hawala systems

Some of the challenges discussed in the literature review were; government issues, legal issues, security issues and finally money laundering issues. In the major results and
findings after the case study was conducted, it was found out that hawala systems faced problems such as high licensing fee from the government and a lot of police harassment from the Kenyan police. Furthermore, it was found out that hawala was not used for illegal money laundering activities here in Kenya, which lead to crimes and law violations.

5.5 Recommendations

5.5.1 Recommendations for Improvement

5.5.1.1 The Role of the Hawala System in Somali Businesses

Only three roles were discussed and analysed and as a result the findings after conducting the case study, collecting and analyzing the data, showed that only one community in one particular area; Eastleigh were large users of the Hawala Remittance System.

This showed that a larger part of the community that lived in Kenya were not aware and so the government through the Ministry of Trade should start putting in efforts to incorporate Hawala Remittance into the country’s Financial institutions.

The researcher suggests that the government should also start introducing courses about Hawala System in schools and universities to make its citizens aware of its benefits and implications so that the citizens or even foreigners living in Kenya are aware of the business opportunities this system creates.

5.5.1.2 Factors motivating the Somali businesses to use Hawala system

In this case, the factors that motivated the Somali businesses in eastleigh to use hawala were few and so other factors should be deeply investigated from all sides of communities or businesses using hawala remittance system, in order to find out what actually makes business people to use hawala as a financial transaction system.

The Hawala owners should also introduce usage of accounts which the hawala system lacked compared to banks that had accounts for each of their customers, like the current and the savings accounts. This will encourage other users living here in Kenya to use the hawala system by opening accounts with it just like the banks.
The hawala owners should partner with banks like the Kenya commercial banks, the Barclays or even equity bank to introduce the usage of Automatic Teller Machines, famously known as ATM, so that it becomes easier for the money senders to simple transact their transactions from any place in Kenya instead of going to a particular Hawala remittance system like Dahabshiil or Mustaqbal. Before taking the above actions, the hawala owners should carry out a thorough research to avoid heavy losses later on in the implementation process.

**5.5.1.3 The Challenges faced by Hawala Systems**

There were many challenges faced by hawala remittance as a financial transaction system. The government in corroboration with the Central Bank of Kenya should establish a legal framework that properly covers and encourages the Hawala Business.

The Ministry of education should also introduce subjects on Hawala Remittance system in schools to make people aware of the pros and cons of the Hawala as an alternative financial transaction to avoid negative image of the Hawala at a later stage.

Furthermore, the Hawala owners should introduce suggestion boxes, which they didn’t have at all the hawala places visited compared to their competitors like the banks, in order to find out the comments, complaints or suggestions of their clients, so as to make Hawala system a better, effective and efficient financial transaction.

The Media should also dedicate a section of the business news to educative topics on Hawala and its performance in order to make the citizens and foreigners in Kenya aware of alternative financial transactions.

**5.5.2 Recommendations for Further Studies**

The study was a unique case study to Hawala based in Eastleigh and as a result the findings therefore cannot be generalized and applied to other financial transactions like forex, money gram or western union and as a result it is recommended that additional research should be conducted on the implications of the Hawala remittance systems.

The researcher recommends that a study on the financial statements or accounting books of the hawala remittance system should be conducted since, no financial statements had
ever been printed and released on the internet, financial books or financial websites, the study will be a huge advantage to the government for positive economic growth and development, and benefit the business people by providing investment opportunities.

The researcher recommends that the government should develop Hawala Remittance Act that will create more favourable conducive environment to smooth the operations of the Hawala Systems, and implement it.
REFERENCES


In depth interviews with hawaladars in eastleigh, Nairobi, Kenya, 17 June 2013.


pp 909-937. doi:10.1017/S0026749X07003459.


Post Office Money Order: A. Scott of Bootle to Peter Hodgson Esq, Whitehaven, Regulation of Informal Value Transfers’, *Crime, Law, and Social Change* 45 (4), 315-


APPENDICES

APPENDIX I: COVER LETTER

DEEQO MOHAMED MUMIN
UNITED STATES INTERNATIONAL UNIVERSITY-AFRICA (USIU-A)
P.O. BOX 14634, 00800.
NAIROBI.

Dear Respondent,

I am carrying out a research case study on the Implications of Hawala Remittance System to the Somali Businesses.

This is in partial fulfillment of the requirement of the Masters of Business Administration (MBA) degree program at the United States International University.

The result of this study will provide insight to government for developing policies and also to other business people that are not Somalis.

This is an academic research and confidentiality is guaranteed. The information gathered herein shall only be used for the above mentioned reason and your name will not appear anywhere in the report.

Kindly spare some time to complete the questionnaire attached.

Thank you in advance,

Yours sincerely,

Deeqo Mohamed Mumin.
APPENDIX II: QUESTIONNAIRE

SECTION I: GENERAL INFORMATION

The following four questions are concerned with demographic data. Please, indicate your selection by checking the box which describes your demographic characteristics.

1. Age group?

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<tbody>
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<td>20 - 25</td>
<td>26-30</td>
<td>31- 35</td>
<td>36 and Over</td>
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2. Gender?

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<tbody>
<tr>
<td>Male</td>
<td>Female</td>
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3. How long have you owned or worked for this Business?

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<tr>
<th>YEARS OF BUSINESS</th>
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<tr>
<td>0 – 2Years</td>
<td>3 – 5 Years</td>
<td>6 - 8 Years</td>
<td>9 Years and Over</td>
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4. Education Background?

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<td>Primary</td>
<td>Secondary</td>
<td>Graduate</td>
<td>Post Graduate</td>
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WITH RESPECT TO PART II, III AND IV, PLEASE TICK THE APPROPRIATE BOX NEXT TO EACH STATEMENT:

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<thead>
<tr>
<th>LEVELS OF AGREEMENT</th>
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<tr>
<td>Strongly Agree</td>
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<td>Agree</td>
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<td>Neither agree</td>
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<td>Nor disagree</td>
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<td>Disagree</td>
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<tr>
<td>Strongly Disagree</td>
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PART II: THE ROLE OF THE HAWALA SYSTEM IN SOMALI BUSINESS.

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PART III: FACTORS MOTIVATING THE SOMALI BUSINESS TO USE HAWALA SYSTEM:

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PART IV: CHALLENGES FACED BY THE HAWALA SYTEM

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<tbody>
<tr>
<td>1 Hawala system encounter government restrictions like paying licensing fee and minimum core capital</td>
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<td>2 The hawala systems are commonly used in order to commit crimes which violate tax and other laws.</td>
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<td>3 Hawala systems are vulnerable to money laundering activities</td>
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<td>4 Hawala Remittance systems face security issues like robberies and theft from outsiders</td>
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Thank you for taking your time to complete the questionnaires