

**THE IMPACT OF MICROFINANCE CREDIT ON THE PERFORMANCE OF
SMES IN TANZANIA:**

A CASE STUDY OF NATIONAL MICROFINANCE BANK-MOROGORO

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SMES IN TANZANIA:**

A CASE STUDY OF NATIONAL MICROFINANCE BANK- MOROGORO

By

Hamisi Madole

A Dissertation Submitted in Partial Fulfillment of the Requirements for the degree of
Master of Business Management (MBA) of Mzumbe University

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CERTIFICATION

I, the undersigned, do certify that I have read through this work and hereby recommend for presentation and defense, the dissertation report entitled: **An assessment of the impact of microfinance credit on the performance of Small and Medium Enterprises (SMEs) in Tanzania, using NMB Morogoro as a case study**, in partial fulfillment of the requirements for the Masters degree in Business Administration (MBA - CORPORATE MANAGEMENT) of Mzumbe University.

Signature

Major Supervisor

Signature

Internal Examiner

Accepted

Accepted for the Board of

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DEDICATION

I dedicate this work to my lovely mother Maimuna Mzee who gave me a lot of advice towards my career path and to my father, Selemani Hamisi Madole who actively encouraged, motivated and supported me throughout the research period.

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ABBREVIATION AND ACRONYMS

APEC	Asia-Pacific Economic Cooperation
GDP	Gross Domestic Product
LDC	Least Developed Countries
LF	Large Enterprises
MFI	Microfinance Institutions
MSE	Micro and Small Business Enterprises
NMB	National Microfinance Bank
OECD	Organization for Economic Cooperation Development
PRIDE	Small Enterprise Development Agency
SME	Small and Medium Enterprises
SPSS	Scientific Package for Social Sciences

ABSTRACT

This study was aimed to examine the impact of microfinance credit on the performance of SMEs in Tanzania specifically in Morogoro Municipal. The research design employed was a case study. Data were collected from 100 respondents. Simple random and purposive sampling techniques were used to arrive 80 customers as well as 20 Bank staff respectively. Moreover, data were collected using interviews, questionnaires, observation and documentary review. Data were analyzed using descriptive statistics (frequencies and percentages) using computer package called Statistical Package of Social Science (SPSS) 16 version. Results shows that credit obtained from NMB Bank in Morogoro, SMEs have been able to improve businesses in term of: increased business profit, increased employees, increased sales turnover, increased business diversification, increased business capital and assets as well as reduction of poverty among customers surveyed. Result also shows that collateral, age or experience of the SMEs owners, and, size of the firm influence the access of credit. The study concluded most of the small businesses depend on bank loan for business capital growth. Bank loan especially NMB loan plays a very crucial role to promote small business growth. Although some of the small businesses fail to repay bank loan due to various reasons such as grace period, moral hazard and high interest rate. In regard to the findings, however, it was recommended that MFIs should increase credit and enhances participation in SMEs financing, in order to sustain the growth and maximal contribution to economic growth and development of the nation. Government and MFIs should enhance the out-reach of microfinance through creating awareness of the activities and operations to SMEs especially those in rural and semi-urban areas that are yet to appreciate the benefits of the scheme.

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CHAPTER ONE

1.1 Introduction

This chapter consists eight sub-sections. The first sub-section is about introduction, the second sub-section introduces background of the study, while the third sub-section covers statement of the problem, objectives of the study, research questions, significance, scope of the study and definition of the key terms.

1.2 Background to the study

In recent years, both developed and developing countries support for SMEs development and growth has increased. This is because of the contribution of SMEs to the employment creation. Evidence shows that a dynamic and growing SMEs sector can contribute to the achievement of a wide range of development objectives, including: the attainment of income distribution and poverty reduction (DFID, 2000); creation of employment (Daniels and Ngwira, 1993); savings mobilization (Beck *et al.*, 2005); and production of goods and services that meet the basic needs of the poor (Cook and Nixon, 2000).

Small and Micro enterprises are the backbone of many economies in Sub-Saharan Africa (SSA) and hold the key to possible revival of economic growth and the elimination of poverty on a sustainable basis. Despite the substantial role of the SMEs in SSA's economies, they are denied official support, particularly credit, from institutionalized financial service organizations that provide funds to businesses (Kailembo, 2011). According to Wangwe and Semboja (1997), these enterprises account more than one – half of the economic activities of the countries within the sub- region, by contributing about 12% and 34% of rural and urban employment activities in Tanzania. Numerous evidences have pointed to the fact that the number of these enterprises in Tanzania is declining at an alarming rate (Satta, 2002) and little has been achieved in Tanzania, despite of the many efforts done to fight for poverty reduction

Lack of access to finance has been identified as one of the major constraints to small business growth (Lawson, 2007). The reason is that provision of financial services is an important means for mobilizing resources for more productive use (Watson and Everett, 1999). Performance of SMEs depends a lot on microfinance institutions support; therefore governments have introduced policies that enable SMEs to access credit from the microfinance institutions.

The importance of financial services to SMEs cannot be overemphasized. SMEs particularly those in developing countries like Tanzania need a range of enabling and sustainable financial services in order to enable them effectively exploit abundant resources in their areas and fulfill their productive potential (Nwanna, 2000).

The introduction of MFI's in Tanzania is seen as the best alternative source of financial services for low income earners and their SMEs as a means to raise their income, hence reducing their poverty level and contributing in country economy (Kessy and Urio, 2006). the service of microfinance institution to majority of Tanzanians who are low income earners have created opportunity to them including managing scarce household and enterprises resources more efficiently, protection against financial risks by taking advantages of investment opportunities and gaining economic returns (Chijoriga, 2000). Micro finance enables clients to protect, diversify and increase their incomes, as well as to accumulate assets, reducing their vulnerability to income and consumption shocks (Robinson, 2002).

It has however, Hogan (2001), argues that the financial service sector focuses its success on the effective management of credit risk. Most micro – enterprises in Tanzania fall under the informal sector. Micro entrepreneurs are engaged in traditional activities which have a low turnover. Traditional economic activities include vending such as street food vendors. Other activities include tailoring, and retailing mostly consumable goods. Micro enterprises have been constrained by many factors especially limited

access to financial services from formal financial institution due to the small business size and circumstances their business operate in.

The other major problem facing SMEs in Tanzania is that they are risky in terms of lending because most of them depend on agriculture which is seasonal hence high default risk and high transaction costs. Further, most traders do not have marketable collateral for loans therefore the banking institutions charge high interest rates of 8% and above on loans which scares away traders from borrowing funds. Without finance, SMEs cannot acquire new technologies, compete in the global market or establish linkages with larger firms and insufficient domestic savings is often mentioned as contributing to the lack of financing for SMEs (UN, 2002).

Capital is one of the major barriers to socio economic development and success for micro enterprise initiatives (ILO, 1998; ILO, 2003). Due to the small sizes of the business, and lack of resources available especially capital to small enterprises, small entrepreneurs need micro-financial services in order to start, grow and service their business. However, due to insufficient mechanisms and inadequate information in Tanzania on credit markets, banks are discouraged and unwilling to lend to micro enterprises (URT, 2002). It is against this background therefore, that the researcher is trying to find out the impact of microfinance credit on the performance of SMEs in Tanzania.

1.3 Statement of the problem

Despite of SMEs large contribution in countries development and economic growth in various aspects such as increased profit, increase of business outlast/ premises which in turn create employment, leads into increase of business assets, business diversification and sales return, however, their growth and development in developing countries are mainly inhibited by access of finance, poor managerial skills, and lack of training opportunities and high cost of inputs (Cook and Nixon, 2000). The SMEs face limited

access to financial services from formal financial institutions to meet their working and investment needs (Kessy and Temu, 2009).

According to Mosley (2001), MFI argued that to be a cheaper source of finance to SMEs. Despite of MFI service been cheaper way of source of finance to SMEs, but, very little is known on the actual cost for microfinance clients to access these services, except interest rates. The interest rate is not the only cost of credit incurred by SMEs, there are also other costs related to the process of obtaining information about the services and the whole process of applying for the loan, cost of getting transportation to make loan payments, time spent obtaining loan and tracking the debt all these are referred as transaction costs.

SMEs have continued to suffer on business capital improvement in Tanzania, although there are several microfinance institutions which provide loans. In Tanzania, most of the SMEs have low return on capital employed, low net profit margin and kept a small capital size (AMFIU 2010). Also, some of SME fail to run their daily operations because of financial incapacity Chowdhury (2002). Therefore, the relationship between the MFIs and SME continue deteriorating due to failure to fulfill their loan obligations (O'brien, 2007). Although the measures been put in place by microfinance operations to overcome the challenges of SMEs in Tanzania, still SMEs owners lack collateral securities which micro finances need in order to give out loans and this in turn raises the interest rates charged on loans which scares away traders and vendors from borrowing. This study is therefore examined the impacts of microfinance credit on the performance of SMEs in Tanzania using NMB as a case study.

1.4 Objectives of the study

1.4.1 General objective

The study aimed to assess the impact of microfinance credit on the performance of SMEs in Tanzania.

1.4.2 Specific objectives

- i. To examine the impact of MFI on small and medium enterprises growth and sustainability.
- ii. To determine the influence of credit terms and liquidity levels on SMEs performance.
- iii. To determine whether MFIs provide favourable credit terms to SMEs in Tanzania or to determine microcredit access challenges faced SME owners in Tanzania

1.5 Research questions

Basing on the objective of this study, the following questions were answered by this study:

- i. How does microfinance contribute on small and medium enterprises particularly on SMEs growth and sustainability?
- ii. What is the influence of credit terms and liquidity levels on the performance of SMEs in Tanzania?
- iii. Do microfinance institutions provide favourable credit terms to SMEs in Tanzania?

1.6 Significance of the study

This study contributes to the body of knowledge on the impact of microfinance credit on the performance of SMEs in Tanzania.

This study was intended to shed light on the relationship between microfinance credits and the performance of small and medium enterprise. This can help them to come out with substantive possible alternative policy interventions which might help to address problems and challenges which small and medium enterprises face. This study can offer empirical evidence on the impact of microfinance credit on the performance of small and medium enterprises for use in short term and long term interventions especially in the fight against poverty. A study of this nature is equally very important because it is going to enlighten the government and the public on the role of MFI in the SMEs sector.

1.7 Scope of the study

To cover all the regions in the entire country was impossible because of the limited time frame and financial constraints. For this reason, the research covered Morogoro region only using National Microfinance Bank (NMB) as a case study. The impact of microfinance credit to the performance of SMEs in this area was analyzed, looking at its contributions, and in what form, and of course the response of SMEs to the contributions of this institution to their enterprise.

1.8 Limitation of the study

This study was carried out under time and financial constraints. These constraints came to have a negative effect on both during the overall undertaking of the study and on the final findings. This is because the researcher was highly in need to extend the study area but he failed due to limited resources (time and funds), that is why this particular study was done in Morogoro Municipal, Tanzania.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter reviews the literature from various studies that are related to this study in hand. It explores through different written sources so as to get an understanding and experience from other places through the works of other scholars.

2.2 SME Development in Tanzania

SMEs all over in the world are known to play a major role in social economy development. This is apparently the case of Tanzania, where SMEs contribute significantly to employment creation, income generation and stimulation of growth in both urban and rural areas.

Different countries define SMEs own their own perspectives. Many advanced countries define SMEs as firms employing between 10 and 250 workers (or, in some countries, 500). SMEs are generally viewed as occupying the middle of the firm size distribution -- larger (and typically more formalized) than "micro-enterprises," which are usually informal units employing at most a handful of people (Jaques, 2000). In many small and less-developed countries, and in this regard, firms employing 250 or 500 people could well be among the larger firms in the country.

There are various SMEs across the World and these have been functioning differently because of different constraints such as management problems as well as financial constraints (Fowel, 1998). Several SMEs are operating at different stages. For example, a large proportion of SMEs are relatively stable in their technology, market, and scale. In light of this, many SMEs are in retail or service sectors. A significant number are at best static and a worst heading for failure.

Other SMEs are technically advanced specialists filling crucial product or service niches within complex modern economies. Examples come from the German *mittelstand* and technically savvy sub-contractors in Japan and northern Italy (Hoiley, 2000). SMEs are seen by those coming from developing countries as a means for alleviating and eradicating poverty and that have been indicated into the Tanzania poverty alleviation and reduction policy.

Despite this, SME picture in developing countries varies greatly. Some more dynamic emerging market economies, notably in East Asia, present thriving SME sectors, including significant numbers of skill-intensive subcontractors (Hoiley, *ibid*). Many more developing countries, though, suffer from a "missing middle". They typically have very large numbers of informal micro-enterprises. They may also have a handful of larger firms-possibly ventures created by foreign investment (in large-scale activities like mining, for example), or family-controlled conglomerates built up over generations (Georges, 1998).

2.3 Definition

The SMEs nomenclature is used to mean micro, small and medium enterprises. It is sometimes referred to as micro, small and medium enterprises (**MSMEs**). The SMEs cover non-farm economic activities mainly manufacturing, mining, commerce and services. There is no universally accepted definition of SME. Different countries use various measures of size depending on their level of development. The commonly used yardsticks are total number of employees, total investment and sales turnover. In the context of Tanzania, micro enterprises are those engaging up to 4 people, in most cases family members or employing capital amounting up to Tshs.5.0 million. The majority of micro enterprises fall under the informal sector. Small enterprises are mostly formalised undertakings engaging between 5 and 49 employees or with capital investment from Tshs.5 million to Tshs.200 million. Medium enterprises employ between 50 and 99

people or use capital investment from Tshs.200 million to Tshs.800 million (Small and Medium Enterprises policy in Tanzania, 2002)

Different scholars in different nations define SME's in different perspective. Small and medium-sized enterprises (SMEs), typically employing between 10 and 250 workers, form the backbone of modern economies and can be crucial engines of development through their role as seedbeds of innovation. Ainley (2005) argues that in much of the developing world, though, SMEs are under-represented, stifled by perverse regulatory climates and poor access to inputs. A critical missing ingredient is often capital.

According to Ainley (ibid), tinier firms-micro-enterprises-frequently get more attention, as donors seek to help the very poor: the recent Nobel Peace Prize awarded to Muhammad Yunus of the Grameen Bank visibly demonstrates the emphasis given to this approach. But the type of support inherent to microfinance lending is generally ill-adapted to serving their slightly larger, and arguably more dynamic, cousins, the SMEs (Voibly, 2004). New options are emerging for meeting SMEs' financial needs, including commercial banks moving "down-market," micro-credit institutions moving "up," and creative application of venture capital investing ideas.

There is argument that governments can help by removing artificial policy and regulatory obstacles to SME lending-importantly; policies that promote greater competition within the financial sector as a whole are generally likely to be especially good news for smaller borrowers like SMEs. External factors can help too-for example by promoting development of credit information systems and reform of collateral regulations. They can also usefully play a selective pump-priming role; for example, they can partially guarantee commercial lenders' moves into SME lending.

Private investors-sometimes with collaboration from and in partnership with the public sector-have a key role, too. For example, in the case of firms facing high-risk, high-return scenarios, home-grown "angel investors" can step in (World Bank, 2002).

In this regards, donor support for traditional microfinance models has helped provide basic financial services to millions of poor people. According to the International Monetary Fund (IMF), in order to help build dynamic competitive economies in developing countries, the time has come to pay greater attention to the potential of small and medium-sized commercial firms to promote economic growth (IMF, 2000).

2.4 Credit

According to the American Bankers' Association (2001), credit refers to borrowed money. Typical forms of credit include credit cards, personal loans, overdrafts and home loans. These terms also refer to the debt repayment of your agreement with a creditor, such as 60 months, 48 months in form of duration.

Organization for Economic Co-operation and Development (2006) indicates that MFIs are the main source of external finance for SMEs. Therefore, it is essential that the banking system be prepared to extend credit to the SME sector. However, there are number of rigidities of a macroeconomic, institutional and regulatory nature that may bias the entire banking system against lending to SMEs. Macroeconomic policies may lead to excess demand for available domestic savings, while government policy may favour industrialization and/or import substitution, which effectively gives large domestic firms privileged access to finance. On the contrary, these terms frustrate the SME sector firm accessing credit because all the efforts and policies favour large borrowers at the cost of the small operators.

In a study by Chowdhury (2002), it was argued that local market competition among MFIs in Bangladesh is driven by credit terms especially in terms of loan amounts, interest rates and repayment time and that some borrowers and MFIs opt for a package of low interest rates tied with low amount of loan disbursed and some other borrowers and MFIs settle for a package of high interest rates tied with high amount of loan disbursed.

However, when assessing comparatively small and straightforward business credit applications, MFIs may largely rely on standardized credit scoring techniques (quantifying such things as the characteristics, assets, and cash flows of businesses/owners). This coupled with the terms and conditions that are perceived to protect their loans at times appear as burdens to the borrowers and because they (SMEs) do not have adequate or no collateral as indicated by Katto (2008) their performance ends up being affected.

2.5 The Microfinance Market

What makes microfinance such an appealing idea is that it offers “hope to many poor people of improving their own situations through their own efforts,” (Stanley, Fischer 2008). *Microfinance* refers to small-scale financial services for both credits and deposits — that are provided to people who running certain business; operate small or micro-enterprises where goods are produced, recycled, repaired, or traded; provide services; work for wages or commissions; gain income from renting out small amounts of land, vehicles, or machinery and tools; and to other individuals and local groups in developing countries, in both rural and urban areas. Microfinance programs also offer skill-based training to augment productivity and organization support and consciousness-raising training to empower the poor

‘Microfinance is one of the most important economic phenomena in the world in the last 50 years’ (Vinod Khosla, co-founder of Sun Microsystems and partner, Keiner Perkins Caulfield & Byers, quoted in Rai, S. (2004).

Market size for this demographic is enormous. The Global Development Research Center estimates that 500 million people own small or micro businesses and only 10 million of these entrepreneurs and producers have access to credit and other financial services. Indeed estimates suggest fewer than 2 per cent of the poor have access to financial services.

2.6 The Role of Microcredit in SME development

Lack of access to credit has been identified as one of the major constraints hindering the development of small businesses, and therefore the supply of entrepreneurial activities not just in Tanzania, but in other developing. Commercial banks have traditionally concentrated their lending mainly to large formal enterprises which possess collateral and, therefore, contended to be less risky. According to a 1997 study on the supply and demand for financial services in Tanzania by K-Rep, less than 5% of households (not necessarily all entrepreneurs) in the urban and rural areas in Tanzania had access to credit from formal sources. Women's World Bank estimated that worldwide, less than 2% of low-income entrepreneurs have access to financial services.

Although the role of credit as a determinant for successful entrepreneurial activity may look obvious when using a partial analysis, the dynamics in the entrepreneurial processes makes this role less obvious. The analysis of an entrepreneurial activity shows that finance does not in itself create economic opportunities. Rather it is entrepreneurial people who see ways in which they can generate income from situations, skills or contact or other push factors. It is in this context that the role of credit should be seen.

Entrepreneurial success could be defined in a conventional sense in terms of a firm's profit generation and growth in terms of employment, output, and sales etc. over-time. Through growth a firm can graduate from one size to a higher one. In addition, firms that are also realizing results like increased employment of family members, and increased household welfare (increased access to education, health, better housing) and those businesses that are able to survive under intense competition are also included. In a competitive situation these successes cannot happen unless a firm is developing an edge that allows it to take advantage of opportunities. The issue then becomes that of how credit can assist in a process of exploiting such opportunities (Kuzilwa, 2003).

As it was cited by Kuzilwa 2003 linked McCormick with the determinants of supply of entrepreneurial activities. Utilizing the Scott and Twomey model explaining the supply

of entrepreneurship, McCormick distinguishes what are called *predisposing* and *triggering factors* and how these are created by economic reforms. Predisposing and triggering factors and how these are created by economic reforms. Predisposing factors include entrepreneurs' background (education, work experience, personal ties), perception and personality which are Important human capital that influences the ability of an entrepreneur in dealing with business environment. *Triggering* factors are those that actually trigger the entrepreneurial activity. This include, for example, increase in the domestic demand for a particular commodity to increased processing capacity and market opportunity, or an opportunity to export due to linkage to a particular chain. Triggering factors have been seen as opportunity for profitable activity. Triggering and disposing factors are seen jointly to be necessary conditions for supply of entrepreneurial activities. At the same time there are factors, named as *constraining factors*, which are said to be against entrepreneurial activities. These include lack of financial resources, lack of information, lack of appropriate education, and weak markets.

2.7 SME Performance

To ensure a reliable performance measure among SMEs, there is need to use the Key Performance Indicators because a new pattern of performance measure has been adopted by many SME's. This is based on identifying what the business does in terms of levels of processes and attaching Key Performance Indicators to those processes. The recording and analysis of the Key Performance Indicators should significantly contribute to the achievement of business goals. The main reason for using KPIs include; telling businesses how well they provide services, how long they take to process customer requests, their product delivery performance and how much time they spend fixing mistakes.

The KPIs are those critical measures which ultimately determine profitability and shareholder value. The traditional Statement of Financial Performance, Statement of Assets and Liabilities and Management Accounts are not enough to effectively manage businesses which are seeking to survive and add shareholder/owner value. Management

needs additional timely information, much of which is not traditional Financial Data, if they are going to effectively manage their businesses.

A Performance Indicator (PI) measures is a measure of the behaviour of a business process. In business, understanding the state of the financial health of a business is a very important issue relating to business survival. There is a strong similarity between physical fitness and the health of a business. The Cash Flow of a business can be likened to the blood circulating through a person. If there is blood loss in the flow, the consequences are swift and predictable.

According to Sudhir and Subrahmanya (2009) and Dalrymple (2004), growth over a period of time can be used for performance measurements of SMEs since this, rather than short term performance, will reflect the long-term strategy of the firm. The researchers (Sudhir and Subrahmanya) probed how far Indian SMEs carried out technological innovations as a result of technology and other related inputs acquired through subcontracting relationships and achieve growth using the case study approach covering two SMEs in Bangalore. It was established that customer requirements were the major causal factors while internal factors such as self-efforts and in-house technical capability along with external factors in the form of technical inputs, suggestions and initiative from Large Enterprises (LE) customers were the sources of innovations for these SMEs. Because of these innovations, SMEs achieved growth in terms of investment in plant and machinery, output and customer base, which are ideal indicators of SME performance.

2.8 Credit, MFI-SME relationship and performance

Organization for Economic Co-operation and Development (2006) reported that the SME sector does not have access to external funds due to stringent terms that the financiers tend to tie to their credit and investment, this leads to the possibility that capacity building are seriously impaired.

In the same report, it was noted that the difficulties that SMEs experience can stem from several sources of their financial needs. For example, the domestic financial market may contain an incomplete range of financial products and services, the lack of appropriate financing mechanisms

In this case, suppliers of finance (MFIs) may rationally choose to offer an array of financial services that leaves significant numbers of potential borrowers without access to credit. Such credit rationing is said to occur if among loan applicants who appear to be identical some receive credit while others do not; or there are identifiable groups in the population that are unable to obtain credit.

According to Asia-Pacific Economic Cooperation (2003), it is recognized that the roles of micro finance institutions are very important for development of SMEs. At least two main goals of giving access for SMEs through development of micro finance institutions, namely: increasing business activity of micro enterprises through working capital or investment fund, and promoting and developing spirit of entrepreneurship. This without a close relationship between MFIs and SMEs may not be achieved.

In a study about MFI-SME financing in Afghanistan by Mennonite Economic Development Associates (2009) it was established that financing interventions that focus exclusively on SMEs may in the end prove to be a high credit risk. While there is value in focus and specialization in financial service delivery, it can also become a weakness if the needs of SMEs are set at to limit its affordability and access.

2.9 Models guiding business financing

Challenges facing MFI in serving MSEs are the little amount and high interest rates offered by MFIs do not meet MSEs needs (Mnenwa and Maliti, 2008), the interest of MFIs is very high compare to that of commercial banks because micro credit is more expensive in analysis, investigation and follow up, at the same time the loan amount is very small compared to that offered by the commercial banks, this is because of lack of

enough fund by MFIs. (<http://www.microfinancegateway.org>); Nightmare of non repayment: In MFI the repayment must secure between 90%-95% being reasonable standard, this is why the MFIs providing loans to urban MSEs require such high collateral (Micro and Small Enterprises and Micro financing in Africa September 2005). Most of the theoretical work on small firm finance and the behavior of institutions that lend to small scale enterprises have been undertaken on the industrial countries. A large proportion of this work has tended to concentrate on firms that, in terms of size, lie towards the upper end of the spectrum, where the range of ownership and financing options becomes wider.

2.9.1 The trade – off Model

Different explanations provide the theoretical basis for the decision taken by firms in the respective areas on the justification for the choice of financing sources and the appropriate mix. The trade-off model postulates that the firm will aim at the optimal gearing levels that will balance the tax benefits of additional debt with the expected costs of financial distress as the level of indebtedness rises (Brierley, 2001; Bunn, Cunningham, and Drehmann, 2005). Considering non-tax benefits of debt such as information asymmetries between lenders and borrowers, managers may raise equity only when company's shares seem overvalued. Investors will consequently discount any new and existing shares when a new equity issue is announced.

Cassar and Holmes, (2001) found out that firms' trade-off several aspects, including the exposure of the firm to bankruptcy and agency costs against the tax benefits associated with debt use. Firms are faced with higher cost of capital because of the increased risk of liquidation and thus they tend to avoid debt. However, firms use debt in order to enjoy tax benefits as a trade-off with the costs associated with bankruptcy and agency, and this implies that there is an optimal debt-equity ratio for the firm, which changes as benefits and costs alter over time (Modigliani and Miller, 1963). This model provides elaborate explanation for the objectives previously outlined in 1.3 where there is a need to understand the justifications for a particular mix of sources of capital due to various

benefits and risks embedded in each of these. It is clearly evident that managers will opt for the mix of sources that minimizes the cost of capital but at the same time not exposing the entity to the factors that may adversely affect the going concern of the firm.

2.9.2 The Pecking order model

This model attempts to avoid the resulting risk that profitable investment projects will be foregone by seeking to finance them internally. If retained earnings are insufficient, they will opt for debt rather than equity finance, because debt providers, with a prior claim on the firm's assets and earnings, are less exposed than equity investors to errors in valuing the firm. Managers will only opt for equity finance as a last resort in this model. In these circumstances, corporate gearing will reflect a company's need for external funds and — unlike the trade-off approach — there will not necessarily be any target or optimal level of gearing. This model was initially proposed by Myers (1994) and suggests that firms tend to finance their needs in a hierarchical fashion, first using internally available funds, followed by debt, and finally external equity.

Central concern appears to be a concentration by small firms on “sources of finance that minimize intrusion into business” (Lopez-Gracia and Aybar-Arias, 2000). Consequently firms do not have an optimal debt-equity ratio but rather it varies, justified by the firm's need of external finance. The pecking-order model to a great extent tells the way certain characteristics of a firm may influence gearing decisions. As Myers suggested, some entities follow a certain hierarchy to determine which the next alternative source of finance is, and that fear of intrusion and dilution of power in an entity may cause a certain sources to be selected. Myers (1994) suggests that issuing debt secured by collateral may reduce the asymmetric information related costs in financing. The difference in information sets between the parties involved may lead to the moral hazard problem (hidden action) and/or adverse selection (hidden information). Hence, debt secured by collateral may mitigate asymmetric information related cost in financing.

2.10 Problems faced by Micro Entrepreneurs

2.10.1 The MSE's inability to offer marketable collateral for loans

Microfinance clients are either very small businesses or poor individual who usually have few assets, non – existent credit histories, and low income levels (Shima, 2004). This is a problem because it means these clients cannot offer any collateral to microfinance providers against loans. As a result, microfinance institutes (MFIs) may either raise their interest rates (which are already high for small loan transactions) or turn down/rejects hundreds of applications.

2.10.2 Poor Institutional viability of micro enterprises

Poorly constructed business ideas with a lack of consideration of demand and costs render the micro venture unsustainable, and microfinance may incorrectly get the blame for it. For instance, in the case of micro crop farming, farmers often fail to account for their personal consumption between the sowing and harvesting periods and realize they face shortage of money. As a result, they often end up using the loan for personal matters. The problem arises when its time to pay back the loan – the farmer is forced to take up a second loan to pay the original loan. This may lead to a vicious cycle where the farmer gets inundated with debt.

2.10.3 Lack of knowledge about microfinance services

Many micro entrepreneurs live in far off rural areas (Chijoriga, 2001), often remote villages, and have little formal education which leads to two issues: a lack of knowledge about the existence of financial services for the poor and little access to microfinance services offered by MFIs

2.11 Problems faced by Micro finance providers:

2.11.1 Inability to exploit growth opportunity

Lack of access to finance or funds means micro entrepreneurs cannot inject money into their businesses (say, to buy more resources or hire more people) to grow them after observing a surge in demand. Moreover, the remote locations of micro businesses means they have little information pertaining to their market, such as customer needs and competitor strength and weaknesses. As a result, many critics may find faults with the idea of microfinance, not realizing that this isn't really a problem, but just a challenge that can be overcome as the business grows and increases in capital base.

2.11.2 Few organizational resources and poor governance

Micro entrepreneurs have limited skills, qualifications and exposures to handling businesses. While they need to be trained through capacity building initiatives by the MFIs, many micro entrepreneurs may not grow as planned because of these problems. For instance, they may borrow more money than needed, or mis-allocate it in their business and end up bearing the burden of large interest payments instead of enjoying the fruits of their business.

2.11.3 Low bargaining power

In case micro entrepreneurs operate in competitive markets, their individual bargaining power is diminishing when dealing with customers because of their small size. However, at the other end of the spectrum, there still isn't any respite because micro entrepreneurs deal with MFIs on an individual basis, which also erodes their bargaining power.

2.11.4 Vulnerability to economic shocks

Micro entrepreneur are particularly susceptible to sudden changes in customer demand, or weather (even though microfinance can help with natural disasters) because their business cannot sustain losses owing to their small size (low capital). This may be a

problem for the social objectives of microfinance providers but MFIs ensure their economic performance is untarnished by charging high interest rates to compensate this risk. Most problems faced by micro entrepreneurs are caused by their small sizes, varied locations and improper skills. Naturally, once the venture secures a loan begins to grow and these problems will eventually subside.

2.12 MFIs' Loans and Performance, Growth and Development of Micro Enterprises

Micro enterprises have an important role to play in the country's social economic development, by contributing significantly to productive and efficient use of scarce resources, employment creation, improved income distribution, region dispersal of industry and development of dynamic private enterprises (Bendera, 1997). Thus MSEs play an important role in improving the contribution the country's indigenous private sector (Mkude, 2004). In regard to employment, there are over one million enterprises in the sector employing between 3 to 4 million people or 20-30% of the total labor force in Tanzania (APDF, 2002). MSEs Growth depends to a larger extent on the financial assistance they obtained internally and externally. Internal source include fund from him/her, since these funds are not enough, external fund such as debt from MFIs, debt from MFIs, Equity finance and from family and friends become important. Olomi (2001) states that in order to improve the contribution of the private sector in Tanzania development process, a larger proportion of informal and small enterprises need to grow. However, limited access to the required financial resources to start service and grow has been identified as an important deterrent to individual and small enterprises development and growth (Mkude, 2004).

From an international perspective, the contribution of Micro enterprises to GDP and employment has been shown to be significant in various countries. In Uganda, MEs put in 40% of GDP more than 50% to manufacturing and over 80% in wholesale and retail. In Nigeria, MEs denote more than 42% of GDP. Despite the structure of a developed economy, MEs in Japan contribute 38% of GDP. In Italy, Ireland, Israel, Portugal and

Spain, MEs contribute between 35- 50% of their GDP (ILO, 2001). In Tanzania perspective, the growth of MEs in Tanzania has been observed in various surveys (Mkude, 2004; APDF, 2002). Their potential could be explained from an assessment of their contribution to employment and GDP. MSEs Contribution to GDP in Tanzania is estimated to be over 35% (APDF, 2002).

The 1991 national informal sector survey revealed that Micro enterprises employed about 20% of the total labor force of 2.4 million people recorded to be involved in MEs, 60% were engaged in these activities in rural areas while 40% were in urban areas. Furthermore, the 1991 survey established that about 50% of the Micro Enterprises workforce is engaged in trade related activities and 22% in manufacturing activities. Urban, agriculture and fishing absorb only 10% (Mashauri, 2004). The question remains what roles MFIs can play or play to enhance such achievement?

2.12 Review of Past Studies

Amin *et al*, (2003) used a unique panel dataset from northern Bangladesh with monthly consumption and income data for 229 households before they received loans. They find that while microcredit is successful in reaching the poor, it is less successful in reaching the vulnerable, especially the group most prone to destitution (the vulnerable poor). Coleman (1999) also finds little evidence of an impact on the program participants. The results, Coleman further explains, are consistent with Adams and von Pischke's assertion that "debt is not an effective tool for helping most poor people enhance their economic condition" and that the poor are poor because of reasons other than lack of access to credit.

According to Mosley (1999), microfinance makes a considerable contribution to the reduction of poverty through its impact on income and also has a positive impact on asset level. But the mechanism through which poverty reduction works varies between institutions. Generally, institutions that give, on average, smaller loans reduce poverty

much more by lifting borrowers above the poverty line, whilst institutions giving larger loans reduce it much more by expanding the demand for labour amongst poor people.

Mosley and Hulme (1998) shows that programmes that targeted higher-income households (those near the poverty level) had a greater impact on household income. Those below the poverty line were not helped much and the very poorest were somewhat negatively affected. The poorest tended to be more reluctant to risk-taking. They also used their loans for working capital or to maintain consumption levels rather than for fixed capital or improved technology. Since, microcredit programmes typically require loan repayment on a weekly basis; some critics argue that repayment comes from selling assets rather than from profits of micro-enterprises.

Fatchamps (1997) argues that with insufficient funds, farmers and fishers cannot invest in new equipment and machinery, and it becomes difficult to reach out to new markets and products. He further contends that without financial assistance, small farmers and artisanal fishermen cannot cope with temporary cash flow problems, and are thus slowed down in their desire to innovate and expand. The general perception is that access to external finance is critical for poor entrepreneurs, who may never have funds proportional to their ambitions.

Pitt and Khandker (1998) reasoned that given the small loan size and the type of activities undertaken by micro-entrepreneurs, it is unlikely that capital intensity has increased. Given that the labour and the capital intensity of rural non-farm production are unchanged, increased microfinance implies that employment can be expected to rise. However, if increased income as a result of microfinance programs results in a decrease in labour supply (income effect), it can negatively affect labour supply of particular type, for example male labour supply. As a result employment may decline, given the demand for labour. Therefore, the net impact cannot be determined a priori. Microcredit programs seem to reduce wage-employment and income, but raise self-employment and corresponding income for programme- participating

households. One might expect that a reduction of employment in the wage market might increase wages, but this may not happen because the wage-employment gap may be filled by previously unemployed or underemployed wage workers.

Mosley (2001), assessed the impact of microfinance on poverty, through small sample surveys of four microfinance institutions. Two urban and two rural, using a range of poverty concepts such as income, assets holdings and diversity, and different measures of vulnerability. All the institutions studied had on average, positive impacts on income and asset levels, with income impacts correlating negatively with income on account of poor households choosing to invest in low-risk and low-return assets. The studies revealed also that in comparison with other anti-poverty measures, microfinance appears to be successfully and relatively cheap at reducing the poverty of those close to the poverty line. However, it was revealed to be ineffective, by comparison with labour-market and infrastructural measures, in reducing extreme poverty.

Nichols (2004) used a case study approach to investigate the impact of microfinance upon the lives of the poor in the rural China and found that the participation of poor in MFI program had led to positive impact in their life. Their income have increased, spending on educational and health have increased hence improved their standard of living and also women have benefited out of this program. There were visible sign of higher wealth level within the village.

In Tanzania, several studies have been done on microfinance institutions service, one of the researcher who have done research on MFI service is Kuzilwa and Mushi (1997) examined the role of credit in generating entrepreneurial activities. He used qualitative case studies with a sample survey of business that gained access to credit from a Tanzanian government financial source. The findings reveal that the output of enterprises increased following the access to the credit. It was further observed that those enterprises, whose owners received business training and advice, performed better than those who did not receive training. He recommended that an environment

should be created where informal and quasi-informal financial institutions can continue to be easily accessed by small and medium businesses.

Chijoriga (2000) evaluated the performance and financial sustainability of MFIs in Tanzania, in terms of the overall institutional and organizational strength, client outreach, and operational and financial performance.²⁸ MFIs and 194 SMEs were randomly selected and visited in Dar es Salaam, Arusha, Morogoro, Mbeya and Zanzibar regions. The findings of this revealed that, the overall performance of MFIs in Tanzania is poor and only few of them have clear objectives, or a strong organizational structure. It was further observed that MFIs in Tanzania lack participatory ownership and many are donor driven. Although client outreach is increasing, with branches opening in almost all regions of the Tanzanian mainland, still MFIs activities remain in and around urban areas. Their operational performance demonstrates low loan repayment rates. In conclusion, the author pointed to low population density, poor infrastructures and low household income levels as constraints to the MFIs' performance.

Another study on microfinance in Tanzania were carried out by Rweyemanu et al (2003), he evaluated the performance and constraints facing semi-formal microfinance institutions in providing credit in Mbeya and Mwanza regions. The primary data were collected through a formal survey of 222 farmers participating in the Agriculture Development Programme in Mbozi and the Mwanza Women Development Association in Ukerewe. In the analysis of their study the interest rates were found to be a significant barrier to the borrowing decision. Also the borrowers cited other problems like lengthy credit procurement procedures and the amount disbursed being inadequate. On the side of institutions, Mbeya and Mwanza credit programme experienced poor repayment rates, especially in the early years of operation, with farmers citing poor crop yields, low producer prices and untimely acquisition of loans as reasons for non-repayment.

In a study conducted by Kessy and Urio (2006) on contribution of MFI on poverty reduction in Tanzania, the researchers covered four regions of Tanzania which are Dar es

Salaam, Zanzibar, Arusha and Mwanza. Both primary and secondary data were collected; primary data were collected from 352 SME's through questionnaires, interviews were also conducted. PRIDE (T) Ltd which is a microfinance institutions were used as a case study so as to get the insight of MFI operations. The study findings pointed out that to large extent MFI operations in Tanzania has brought positive changes in the standard of living of people who access their services, clients of MFI complained about high interest rate charged, the weekly meeting was pointed out as barrier as the time spent in weekly meeting could be used to other productive activities. The study recommended MFI to lower its interest rate, increase grace period and provide proper training to SMEs.

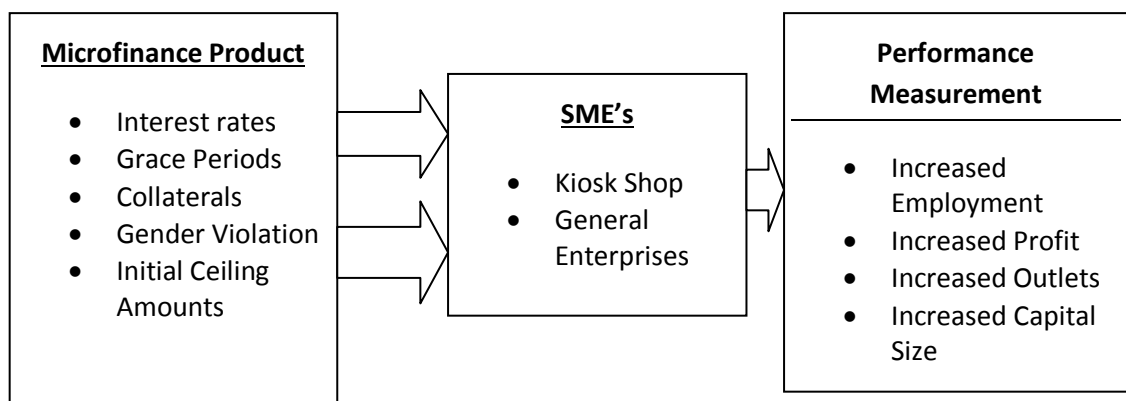
Research gaps: Therefore, the reviewed previous studies failed to show the effects of microfinance credit in improving the performance of SMEs in Tanzania. Previous studies failed to examine the effect of MFI on small and medium enterprises growth and sustainability. Not only that, also they failed to determine the influence of credit terms and liquidity levels on SMEs performance as well as to determine whether MFIs provide favourable credit terms to SMEs in Tanzania or to determine microcredit access challenges faced SME owners in Tanzania. Therefore, this study takes the mentioned weakness above as one of the research gaps found in this study that triggered the researcher to undertake this study.

2.13 Conceptual Framework

Conceptual framework shows interconnections relationships of the impact of microfinance credit on SMEs performance. The concept was converted into variables to assist easy measurement even though the degree of precision with which they can be measured varies from scale to scale. The conceptual frame work of this study is governed by microeconomic theory. Traditional microeconomic theory treats finance as a corporate factor of production. Irrespective of firm size and age, finance is normally required for three standard uses, that is for start-up capital in machinery and acquisition of buildings, financing working capital during start-up or while expanding and purchase of operating materials.

Implementation of a business activity can only take place when these factors are in place; otherwise the activity has to be aborted. Financing of factors of production can be undertaken from own savings, generated internal profits (for on-going businesses) or external funds (for start-ups and on-going businesses). Credit becomes important when internal sources of finance are inadequate for an envisaged entrepreneurial activity as figure 2 below indicates:

Figure 1: Conceptual Model



Source: Researcher (2013)

The conceptual model of the study expressed that the business needs to be connected to credit as well as macroeconomic factors. Credit is a major factor use to improve business to grow. Interest rate should be fairly. Then, both grace period and initial ceiling amount should be improved so as to improve impact of credit on SMEs. However, macroeconomic factors need to be improved by the government to improve economic benefits of the businesses. Macroeconomic factors is used to promote development of SMEs in the country especially when SMEs are adequately connected on business infrastructures and the government reduced tax rate as well as operates at economy transaction costs.

Despite of constraints faces small businesses to grow microcredit seems is a major driving factor for the business to succeed. Indicators for the business growth is increased employment, profits, sales, outlets and business survive.

Therefore, the model entails microcredit as well as macroeconomic factors if utilized and managed properly the country economy can grow and automatically industrial sector also can grow sustainably.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This sub-section one presents the research design, followed by sub-section two presents description of the study area, sub-section three was the study population, sub-section four was the sampling methods, while sub-section five was data collection methods, and sub-section six was data analysis techniques.

3.2 Research design

The study employed cross-sectional research design. It is not repetitive in nature as it is carried out once at a particular point in time. Moreover, it facilitates the study to examine a section of the population at a single-time period (Kothari, 2004).

3.3 Description of the study area

The study was conducted in Morogoro region involving small and medium entrepreneurs who have benefited from NMB credit schemes in the region. The study specifically dealt with those enterprises that are centered in Morogoro district or municipal which have small and medium enterprises beneficiaries of NMB credits.

3.4 Sampling method

3.4.1 Target population

Cohen (2000) shows that population is a group from which the study expects to get useful information and draw conclusions for the study. Target population for this study was entrepreneurs from small and medium enterprise who have been beneficiaries of NMB credit schemes or MSE's clients have accessed NMB Microfinance credits and

loan officer/employees of (NMB, Loan Department). The selection of the officers for interviewing was based on the knowledge of their presence during the period covered by the research.

3.4.2 Sample size

This study used a sample of 100 respondents whereby client of NMB PLC who involve in small and medium enterprises and having been beneficiaries of NMB credits and NMB officials mostly from credit/loan department were included in this study.

Table 1 Sample Size

Sample	Sample Size
MSE customers	80
NMB staff	20
Total	100

Source: Field Data (2013)

3.5 Sampling techniques

In the course of conducting this study, the researcher applied simple random sampling and purposive sampling method in data collection.

3.5.1 Simple random Sampling Technique

Simple random sampling was chosen as an ideal method for this study due to its nature that is representativeness, fairness and lack of biasness. Every person in the area of study had an equal chance to be selected as a respondent.

3.5.2 Purposive Sampling Technique

The study also employed purposive sampling technique based on the position hold respondents during the survey. Moreover, respondents were chosen based on the

researcher's judgment that they have desirable characteristics and can provide the required information. Furthermore, purposive sampling technique was used to select bank official who directly engaged in providing loans to SMEs. All senior officers such as managers were selected purposefully because of key positions, knowledge and experienced hold in their job position.

3.6 Data Collection Methods

Kothari (2004) advises that while deciding about the methods of data collection to be used for the study, the researcher should keep in mind two types of data; namely primary and secondary. The instruments for collecting data are therefore selected depending on the type of data the researcher would be collecting. In order to collect data needed in this study; the researcher used questionnaire, interview and observation methods for collecting primary data, and documentary method for collecting secondary data.

3.6.1 Primary Data Collection Methods

3.6.1.1 Questionnaires

Questionnaire was at first pre-tested to a small number of respondents to check if the instrument can measure what claimed to be measured. Thereafter, questionnaires were distributed by the study to the respondents for collection of raw data. They were filled in a self-administered manner. In this regard, they were formulated in English and translated into Swahili to make them understandable to respondents. 100 questionnaires were distributed to different entrepreneurs in the study area.

3.6.1. 2 Interviews

Interviews were arranged to allow respondents to freely provide their views related to the problem that is being investigated. The purpose of use this method was to supplement the questionnaire method of data collection so as to obtain the qualitative data that can be collected using questionnaires. In other words, it helped to get data that

serve as supportive in narrating the impact of microfinance credit to small and medium enterprises.

Interviews were semi-structured; i.e. some of the questions and topics were predetermined. Other questions arose during the interview sessions and thus the method appeared to be informal and conversational, but carefully controlled and structured. Interviews were used to collect data from respondents who had no time to fill in questionnaires but could express themselves verbally.

3.6.1.3 Observation

Observation is an eye sight inspection followed by writing or drawing, depending on what the researcher surveys (Adam and Kamuzora, 2008). During data collection, the researcher visited established enterprises to obtain first hand information to be related to information collected through interviews and questionnaires.

3.6.2 Secondary Data Collection

Secondary data are those data obtained from literature sources or data collected by other people for some other purposes (Adam and Kamuzora, 2008). The study collected secondary data using documentary review technique as presented below:

Documents Review Technique

The study reviewed various documents as part of secondary data collection technique. Data were collected from documented materials such as books, reports, and electronic archives in forms of websites. The purpose of used such method is to get archival information to support raw data to be collected from field in the course of this study.

3.7 Data processing and Analysis

The qualitative data collected was analyzed using statistical and qualitative approaches in order to make meaningful presentations and conclusions. Data collected from the 90 respondents was examined and arranged basing on the research objectives. The data collected were arranged into a more workable framework that enabled the researcher to classify and organize them. In order to make meaningful presentation of the data collected and to match it with the study objectives and research questions, the data was subjected to various steps including; editing in order to identify missing gaps, spelling mistakes, incomplete answers and to eliminate unwanted data; coding, classification of data with common characteristics. In the statistical method, analysis of clearing and forwarding data focused on various process and procedures involved by the port and other agents activities and this was done at three levels;

The researcher described the study population by background characteristics purposely relating to the impact of MFI on small and medium enterprises growth and sustainability, the influence of credit terms and liquidity levels on SMEs performance and as to whether MFIs provide favorable credit terms to SMEs in Tanzania or to determine microcredit access challenges faced SME owners in Tanzania.

3.8 Ethical considerations

Ethical considerations in conducting a research should not be overlooked. Nearly every research study has the potential of affecting subjects in some way, either psychologically or physically. Researcher dealing with human subjects must take great care to ensure that all precautions are taken to alleviate any potential harm to subjects. These include carefully planning a study as well as debriefing subjects upon completion of the project (Payne and Payne, 2004). Saunders (2007) defines research ethics as the appropriateness of researcher behaviour in relation to the right of those who become the subject of the study work. In this study ethical procedures were considered throughout the period of research study and the researcher ensured that names of respondents did not appear on

the questionnaire to ensure confidentiality of the respondents as it is a part of the ethical procedure to ensure that respondents are protected.

3.9 Validity and reliability

A pilot study was conducted to test-run the practicability of the study and to detect flaws in the data collection process. This helped to discover errors on the issues raised such as ambiguous instruction or wording, inadequate time limit and measurability of variables defined. Copies of the questionnaire were given to senior colleagues, colleagues, statisticians and loan officers before the pilot study. The views of the loan officers were considered very important because they work with the entrepreneurs and they understand their level of perception on the subject matter. Fifty copies of the questionnaire were used for the pilot study. Therefore the results obtained from this study are reliable and can be used as a source of further references.

CHAPTER FOUR

DATA ANALYSIS AND DISCUSSION

4.1 Introduction

The chapter based on the five sub-sections mainly. The first sub-section was introduction; the second sub-section was socio-economic characteristics of respondents. The third sub-section was about to examine the contribution of MFI on small and medium enterprises growth and sustainability, while the forth sub-section was to establish the relationship between credit terms, liquidity levels and SMEs performance, and the firth sub-section was to establish whether MFIs provide favorable credit terms to SMEs in Tanzania.

4.2 Socio-economic Characteristics of Respondents

The typical characteristics of respondents are crucial interpreting and discussing research findings in terms of education level, experience in microfinance institutions, credit management and SMEs financing and management. Such information would provide general image and meaningful information on the impact of microfinance credit towards the performance of Small and Medium Enterprises (SMEs) in Tanzania.

Table 4.1: Social-Economic Characteristics of Respondents

General characteristics	Frequency	Percent
Age strribution		
20-30 Years	24	26.7
31-40 Years	36	40.0
41-50 Years	23	2.5
51 Years and above	7	7.8
Total	90	100
Gender distribution		
Male	47	52.2
Female	43	47.8
Total	90	100
Education level:		
Primary level	28	30.1
Secondary level	26	28.4
College	19	20.4
University	17	19.0
No formal education	0	0
Total	90	100
Experience of respondents		
Less than a year	19	21.1
1-2 Year	19	21.1
3-4 years	34	37.8
5 years and above	12	13.3
Total	90	100

Source: Field Data (2013)

The study sampled 100 respondents. However, only 90 (90%) respondents successfully filled and returned the questionnaires. Therefore, the study analysis was based on 90% response rate.

4.2.1 Age distribution of the respondents

The study employed respondents of different age groups from the field. Table 4.1 shows respondents with age group 31- 35 years were 23.3%, while, 36-40 years were 16.7%. While with 26 - 30 years was made to 15.6% of the respondents surveyed; also, 41- 45 years were 13.3%, 46 - 50 years accounted for 12.2% whereas 20 - 25 years and those of 51 years and above were 11.1% and 7.8% respectively.

This result implies that majority of the SMEs owners about 40% of respondents had 31- 40 age group. This group is active economic age group that needs to be supported financially for economic growth.

4.2.2 Gender distribution of respondents

NMB provides microfinance services to people of all gender. Thus, this study chose respondents from both genders. As Table 4.3 shows that 47% of respondents surveyed were male, while 43% were female in this study. The implication is that gender balance was considered as the number of respondents participated in this study is almost equal between males and females. In this study, as every member in the study population had equal chance of being selected.

Moreover, education level of respondents was also taken into account in order to find out levels of education of respondents surveyed in Morogoro region. Table 4.1 shows that most of the respondents (30.1%) had primary education level followed by 28.0% that had secondary education level. While 20.4% respondents had college and the remaining 19% respondents had university education level that represented most of the bank officials.

The implication is that majority of the respondents have attained their primary education which implies they can own and operate micro enterprises and the basic knowledge in business that can enhance them to access loan from financial institutions.

4.2.4 Experience with NMB credit scheme

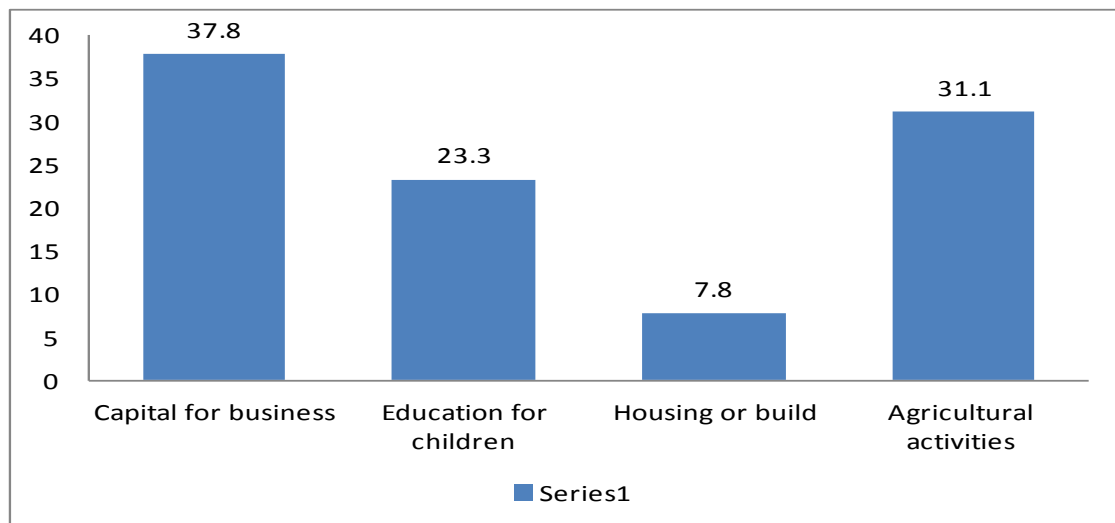
Table 4.1 shows majority of the respondents (65.6%) had an experience of between 1 to 4 years with micro-credit services provided by NMB. Moreover, only 13.3% had 5 or more years in using such services and 21.1% of the respondents had been members of NMB for less than a year. The implication of this result is that most of the SMEs owners had experienced microfinance services provided by NMB in the municipality.

4.3 Uses of Bank loans

4.3.1 Bank loan Allocation

The study aimed to assess how bank loan spend by customers in the study area. Figure 2 shows that the capital for business injection was scored higher (37.8%), thereafter followed by agricultural activities (31.1%), education consumption (23.3%), and the least was household consumption (7.8%) respectively.

Figure 2: Respondents views on the uses of Loans



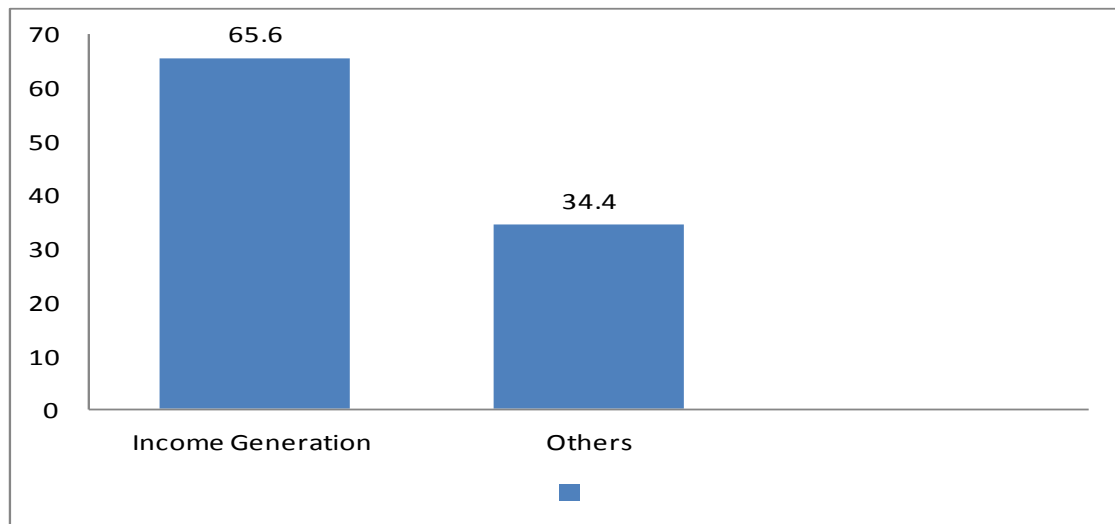
Source: Field Data (2013)

This implies that that NMB loan scheme is more effective in helping the beneficiaries raising their economic position through businesses and agricultural activities as well as investing in their children's education. Majority of SMEs are rooted in business and agricultural sector. Moreover, the consequences of loan obviously could be to pay education and other household consumptions.

4.3. 2 Income Generating Activities after Bank Loan Receipt

Microfinance aims at empowering the poor to come out of poverty. Figure 3 shows that 65.6% agreed that they had used a loan from NMB to start an income generating activity, such as agriculture or business activities while 34.4% used the loans in other ways such as to develop already started enterprises or using the loans for other activities such as education or housing. This implies that poverty refers to as when someone's "resources are so seriously below those commanded by the average individual or family that they are, in effect, excluded from ordinary living patterns, customs and activities (Peter,2000). Although it was not the aim of MFI to effect direct education and other economic activities out of business direct"

Figure 3: Establishment of income generating activities



Source: Field Data (2013)

4.4 Impact of MFI on Small and Medium Enterprises Growth and Sustainability

The study used change in sales turnover, profit growth, business capital and assets, business diversification, number of employees indicators to estimate the contribution of MFI on SMEs enterprise in the study area as follows:

4.4.1 Growth of Sales turnover

Table 4.2 shows that 43.8% of respondents remarked the growth of less than 10% of their sales growth after accessing loan from NMB, followed by 38.8% of respondents remarked sales growth of (10-25%) per year.

Table 4.2: Sales turnover estimates

Sales Turnover	Frequency	Percent
< 10%	30	30
10-25%	42	42
26-50%	13	13
More than 50%	15	15
Total	90	100

Source: Field data (2013)

Results (Table 4.2) are based on the responses given out by SMEs owners who have accessed loan from NMB bank. A large number of customers responded that their businesses had experienced sales turnover growth after accessing NMB Loan and 15.0% reported growth of 25 and 50% while 2.6% had growth of more than 50%. This means that for those who have accessed MSE loans from NMB, the sales turnover in their businesses had shown positive growth trend though in different growth rates.

4.4.2 Growth of Business Profit

Profit growth as an indicator for business performance was assessed for the purpose of estimating annual percent growth of an enterprise. Findings of the microfinance clients consulted revealed that, profit obtained in their business has been increased after accessing and utilizing SME loans from NMB.

Table 4.3: Growth of Business Profit

Profit growth	Frequency	Percent
< 10%	35	55
10-25%	31	34.4
26-50%	15	17.1
More than 50%	9	10
Total	90	100.0

Source: Field Data (2013)

Table 4.3 shows that 55% respondents indicated that microfinance loans from NMB had brought an increase to business profit growth trend by about less than 10% since they had started utilizing them. Other respondents, who represent 34.4%, revealed that their businesses have grown by 10-25%. While only few 17.10% reported to increase profit by 26-50% and 9% who reported more than 50% profit increase. Findings of the study suggests that loan provided to micro and small enterprises cause a slightly increase in profit growth of less than 25% per year.

4.4.3 Growth of Business Assets and Business Diversification

Among the key performance indicators that were examined during the administration of this study were: asset, increase in returns, increase in stock levels/Diversification and Increase in retained earnings. Table 4.4 shows the impacts of loan on assets, and diversification.

Table: 4.4: Contribution of loan to Firm Performance

Loan Help In Better Firm Performance	Frequency	Percent
Increase in Assets	36	35.5
Increase in returns	28	31
Increase in stock levels/Diversification	16	17.7
Increase in retained earnings	12	13.3
TOTAL	90	100%

Source: Field Data (2013)

Table 4.4 above indicates importance of loan to respondents' firm performance. The results indicates that loan help business overall firm performance in diverse ways. Respondents chose more than one important reasons of loan to their firms. Percentage wise, most respondents (28%) opted for increase in returns as their definition for importance of loan with respect to improvement in overall firm performance. increase in retained earnings (13.3%). This according to respondents is because of pressures to repay loan which limits expansion thus the business inability to retain excess funds. Increase in stock levels and product diversification or inventory (17.7%) also on the high side implied that loan taken are use to purchase materials for production, thus businesses are able to add up their stock to meet increasing demand. Definitely, with an increase in assets both physical and financial, the analyses of the data indicate that SMEs reaped significant benefits through loans accessed from NMB bank. Overall, the results showed appreciable improvements in financial and physical assets. They managed to diversify

and accumulate assets, which provide protection against risk and vulnerability to their business.

4.4.4 Growth of Working Capital

Results show that the loan obtained from the NMB by SMEs had assisted to expand their business; production had increased which in turn improves income and lead to development of dynamic private sector. Business expansion has a direct relationship working capital growth. The field study also went further into looking at what percentage of the micro entrepreneurs sampled had managed to increase their working capital as a result of microfinance loans.

Table 4.5: Working capital growth after accessing loan

Working capital growth	Frequency	Percent
< 10%	15	16.6
10-25%	17	18.8
26-50%	44	48.8
More than 50%	13	14.4
Total	90	100.0

Source: Field Data (2013)

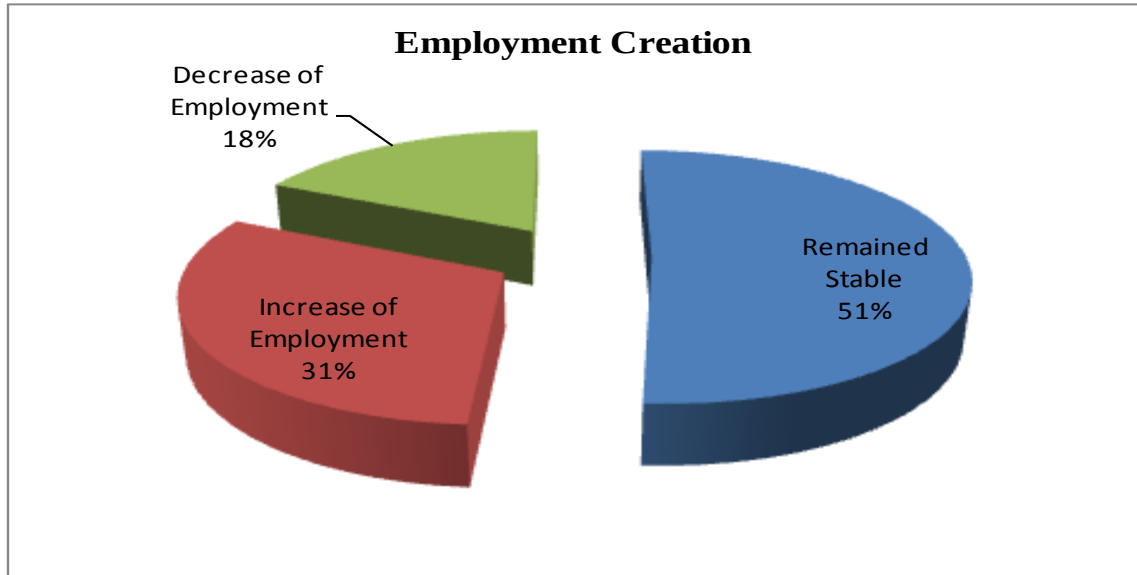
Table 4.5 shows that 48.8% respondents agreed that after access microfinance loans from NMB their working capital had increased for about 26-50%. This demonstrate that large number of respondents had reported working capital growth to the higher percentage compared to 18.8% respondents who reported working capital growth of about 10-25% which is in the lower side. Likewise, 16.6% of respondents indicated that they experienced working capital increase by 10% and lastly 14.4% indicated that the loan accessed from NMB bank enabled working capital growth for more than 50%.

4.4.5 Growth of number of employees in the business

Results shows that 18% of the respondents they decided to reduce a number of employees because they wanted to cut cost of operations especially after accessing and utilizing the loan facility, with the aim of profit maximization. While the 31% of the respondents reported increase in number of employees after accessing and utilizing the loan facility. During the administration of this study it was found out that self employment has increased as due to the increase of loans approval, to all business categories Micro, Small and Medium.

Moreover, the majority of the respondents (51%) were reported that a number of employees remain unchanged after loan utilization. This means loan access had assisted them to maintain their business operations as they could not expand and therefore they did not employ new workers. The study revealed that more employments were created in manufacturing sector, service; agriculture and construction sector due to the loan that was obtained from NMB, it was found that employment creation depended much on nature of business and individual skill and management of loan.

Figure 4: Creation of Employment



Source: Field data (2012)

Figure 4 shows that after loan access some of micro entrepreneur manage to increase employment and retain their workers and managed to create stable employments hence contribute toward the growth of micro enterprises. From the preceding discussion, it is apparent that SMEs constitute the most important national employment base.

4.5 The Influences of Credit Terms and Liquidity Levels on SMEs Performance

The study was aimed to examine the influence of credit terms and liquidity levels on SMEs performance in order to determine the rationally of the role of MFI in the study area as follow:

4.5.1 Liquidity levels and SMEs performance

Table 4.6: Shows Respondents Views on liquidity and SMEs performance

Responses	Frequency	Percent
Strongly Agreed	50	55.5
Agree	20	22.2
Neutral	11	12.2
Disagree	7	7.7
Strongly disagree	2	2.2
Total	90	100

Source: Field Data (2013)

Table 4.6 shows that 55% of the respondents strong agree that methods used in managing liquidation were effectively used by National Microfinance Bank (NMB). 22.2% agree, 12.2% were silent 7.7% disagree and 22% strongly disagree. This implies that effective methods were used by National Microfinance Bank (NMB). As for the National Microfinance Bank (NMB) at any time canceled the facility and requested borrowers to repay the facility including any interest accrued on it at any time of the contractual period.

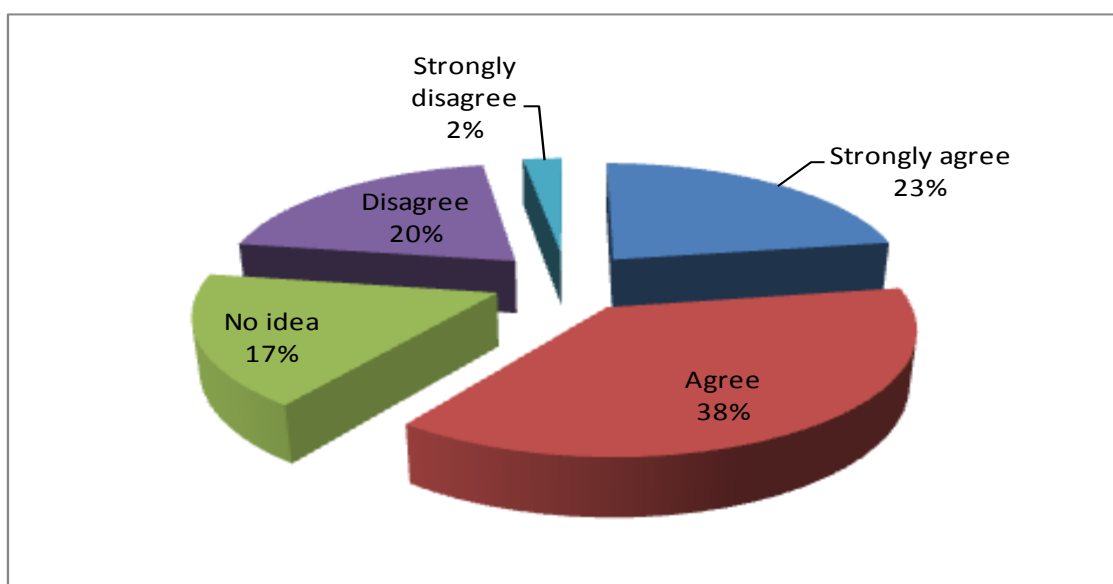
Results show that credit terms influence SME performance. This implies that the more favourable the MFI credit terms are, the higher will be the performance of SMEs. This is due to the fact that respondents were concerned about credit terms. Results also revealed that liquidity levels is an important aspects on SME performance which means that with more liquidity, SMEs are able to meet their obligations as and when they fall due. This therefore increases the performance in terms of market growth, increased product portfolio, timely loan payments as well as generating higher profits which increases their capital base.

Moreover, this result is supported by Chowdhury (2002) also emphasized that favourable credit terms such as adequate loan amounts, affordable interest rates and flexible repayment schedules help SMEs keep enough finances to run their working capital activities, it helps them to improve businesses performance because of the opportunity costs reinvested for further proceeds in order to generate more revenues something that increases on their return on capital employed Findings by Nyondi (2010) also stressed that the ultimate, beneficiary from all these reforms and innovations is the customer who has received a good and strong intimacy with the MFI especially with the demand tailored services. In return, their (SME) net profit margin can raise something that lifts the capital size (UNDP, 2003). Therefore, the MFIs can take advantage of the relationship they hold with SMEs to improve their performance.

4.4.2 Effective Management of requirements for SMEs to secure micro-financing

This sub-section stressed on estimates the effectiveness management for requirement for SMEs to secure micro-financing in the study area.

Figure 5: Effective Management of requirements for SMEs to secure micro-financing



Source: Field Data (2013)

Figure 5 shows that 23% and 38% of respondents respectively agreed that NMB Bank ensure effective management of requirements for SMEs to secure micro-financing especially at initial stage, 17% of respondents had no idea, while 20% disagreed and 2% of respondents strongly disagreed.

Moreover, NMB is providers is formal micro-finance providers, it was revealed that SMEs do not find it easy to acquire a loan. Though her requirements are not easy to be met, it is easier than the requirements needed by other commercial banks. It was found out that loans that are within savings are not a problem to get but when it goes beyond the savings it become a problem. Other members can stand as a security for a loan for

someone who does not have the needed security. The surety must be a trust worthy person and of course a faithful and high savings member. What it takes to get a loan is difficult to provide by the customers or members at a particular business level or of a particular business type. NMB only accept fixed immovable assets and preferably land and buildings since they can be owned in this context. More so, the borrower must be investigated and found that he/she has the capacity to repay. This is done by an expert counseling the member and providing skills needed to proceed. According to the field study, it is noticed that NMB has strict requirements for loans out of savings and this is because they do not target the very poor.

Also, when a business is in its early stage, it requires at least a certain sum of money in its account for the MFI to consider the application for a loan. When the enterprise cannot provide the required equity capital, they are bound to provide household belongings as collateral for the loan. These MFIs also employ some kind of financial and psychological measurements and when they find out that the prospective borrowers meet the needs, it is then that the loan can be granted. It is generally said that people care more on things that they have worked for or items that they own. This and other reasons explain why MFIs deem it necessary for borrowers to have minimal equity contribution before applying for a loan. The source of the minimal equity capital is known by the MFIs because the client may be at high risk of non respecting the terms of repayment had it been the funds were borrowed from somewhere (Ledgerwood,1999).

4.4.3 The importance of Firm size and Liquidity Level on SMEs Performance

Table4.7: Shows Firm size and Liquidity Level on SMEs Performance

Responses	Frequency	Percent
Strongly agreed	36	40
Agree	24	26.6
Neither agree nor disagree	8	8.8
Disagree	10	11.1
Strongly disagreed	14	15.5
Total	100	100

Source: Field Data (2013)

Results on Table 4.7 indicate that 40% of respondents strongly agreed and 26.6% agreed on the importance of firm size and liquidity level on SMEs performance. While 8% of out 90 respondents remained silent, 11.1% disagreed and 15.5 % out of 90 respondents strongly disagreed. The study revealed that firm size is one of the most important criteria used by NMB Bank to grant loans to SMEs in Morogoro, it implies that small and medium enterprises are financially more constrained than large firms. As this study is focused on small and medium sized firms, it seems logical to consider size as a determinant of access to finance. The result of this findings is in contrast with the study conducted by Weder (2001) sampled firms across a number of countries and found that there was a negative relationship between the size of a business and the risk it might pose for a lender.

During the field survey it was also, revealed that sometimes age influence access to credit. Being in the business for many years influence the financing decision, it can be argued that being an older firm means there is lower informational problems. The reason is information required by the lenders to evaluate and process applications is readily

available because these businesses have an established reputation or track record. On the other hand, the new firms are not likely to meet the collateral requirements of the banks since they have not accumulated sufficient assets. Combined with the absence of information on their financial records, this makes difficult to lenders to assess lending proposals submitted by new firms. Similarly klapper and Udell, (2001) argue that firm Size is significant in determining its liquidity levels. The traditional models to determine the optimal liquidity demonstrate that there are economies of scale associated with the cash levels required to confront the normal transactions of the firm, so that larger firms can keep lower cash holdings. It's therefore important to consider that firm size is related to another set of factors that may influence liquidity levels such as the level of fixed costs and these costs are proportionately greater for SMEs.

4.4.4 The use Group lending, networking and liquidity level on SMEs performance

Table 4.8: Show Views on Group lending, networking and liquidity level on SMEs performance

Responses	Frequency	Percent
Strongly agreed	19	21.1
Agree	38	39.1
Neither agree nor disagree	10	11.1
Disagree	9	10
Strongly disagreed	6	6.7
Total	90	100

Source: Field Data (2013)

Table 4.8 shows out of 90% of respondents interviewed, only 21.1% respondents agreed that the use Group lending, networking and liquidity levels were used by NMB Bank on financing decision of SMEs. 39.1% strongly agreed, while 11.1 neither agree nor disagree. Although it was found that a small proportional of SMEs interviewed used the

existing SMEs support programs provided by NMB, however, those who have attended seminars and training stated that workshops conducted on preparing project proposals for accessing credit were important for SMEs or business performance and managing finances in the business. In some occasions, one prominent and established member in an association may introduce another member to his or local bank managers and loan officers, and that referral may be used as a best screening method for the bank loan officers to get some idea of the character of the borrower.

Furthermore, the study found that NMB encouraged SMEs borrowers to form groups as criteria to access loans; also, members of associations or groups were being given information on various credit schemes available in the bank. There could be instances where one members act as a guarantor for another member at the time of obtaining a loan from a bank. The finding of this study showed that solidarity of group lending is one of strategy that NMB Bank has adopted to reduce rate of defaulters. Taking an example of group loans, in order to access this service, borrowers must be in a group and must own a business, know each other, trust each other, love each other, willingly engaged in the group, ready to guarantee each other, have attended preliminary training, ready to attend weekly centers meetings, ready to save specific amount of money on weekly basis, likely in terms of income and are not blood relatives. Solidarity of group lending strategy has been attracting number of business owners because has enable most business owners to be reach with loan from formal financial institutions

These findings are in line with the research conducted by Levitt and March (1998) have acknowledged that networking sometimes called external relations, of firms among industry, trade associations and other forms of association create learning by facilitating the sharing of knowledge, providing a means for organisations to learn from the experience of others in the industry. Likewise, study by Cohen (1999) indicates that participation in microfinance programs contributes to reduced vulnerability to liquidity risks among SMEs. Microfinance services help the SMEs to diversify their income sources, building up physical, human and social assets, and focus on good money

management, rebuild the household's base of income and assets after economic shocks have occurred and to smooth consumption.

4.4.5 System for monitoring the condition of credits to SMEs

Table 4.9: Show respondents views on monitoring condition of credit risk to SMEs

Responses	Frequency	Percent
Strongly agreed	30	33.3
Agree	24	26.6
Neither agree nor disagree	17	18.8
Disagree	9	10
Strongly disagreed	8	8.8
Total	90	100

Source: Field Data (2013)

Table 4.9 indicates that 33.3% out of 100 respondents strongly agreed and 26.6% agreed that the NMB bank has system for monitoring condition of credit risk to SMEs. While 18.8 % out of out 100 respondents remained silent, 10% disagreed and 8.8% out of 100 respondents strongly disagreed that the NMB bank has system for monitoring condition of credit risk to SMEs. The study found that these procedures include defining criteria for identifying and reporting potential problem credits and other transactions to ensure that they are subject to more frequent monitoring as well as possible corrective action, classification and/or provisioning to ensure that the bank understands the current financial condition of the borrower SMEs, monitor compliance with existing covenants; assess, where applicable, collateral coverage relative to the obligor's current condition; identify contractual payment delinquencies and classify potential problem credits on a timely basis; and direct promptly problems for remedial management. It was found that there are specific individuals who are responsible for monitoring credit quality;

including ensuring that relevant information is passed to those responsible for assigning internal risk ratings to the credit.

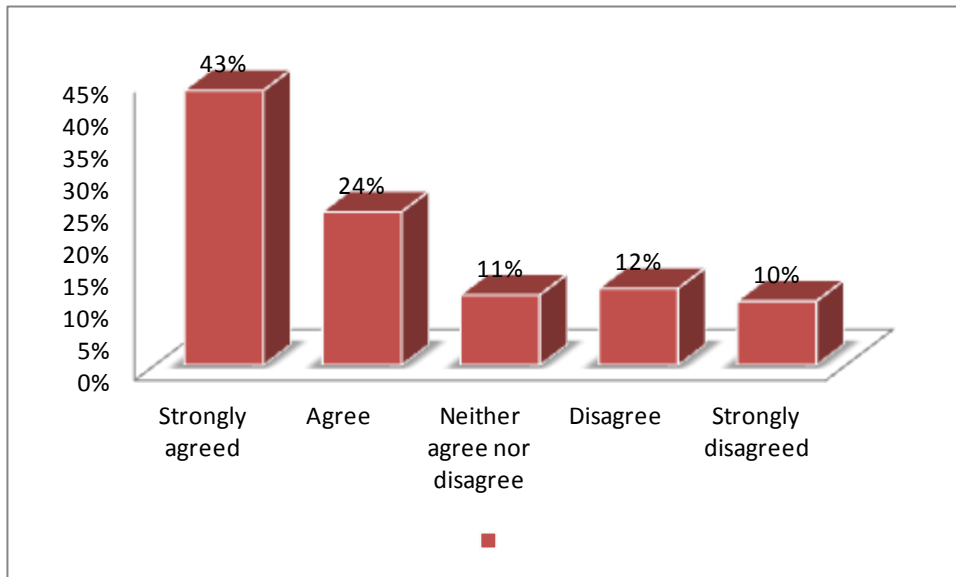
4.5 Credit Terms to be fulfilled by SMEs before Credit to be disbursed to Customers

This sub-section was aimed to assess whether MFIs provide favorable credit terms to SMEs in Tanzania or not. The following were the discussion of the findings.

4.5.1 Size, Nature and Business Type

Securing finance in the form of loans by SMEs is determined not only by the size of business operation but also of the type of business and the worth of it. Early stage businesses are not easily granted with loans. They represent a small percentage from the field data gotten. Most of them do not or find it difficult to meet the requirements for a loan. They cannot secure the necessary resources and has a possibility to die in this early stage. The granting of loans is much easier to large firms than small ones (Gary and Guy, 2003). MFIs consider client's ability to repay debt and assess the minimal sum they can contribute as equity before offering a loan. Existing firms are considered to have a history that can be judged by the MFIs before granting a loan. A bad history means loan denial and a good history means the loan will be granted. A start up business does not have this history and MFIs do not rely on them because of not facing the problem of information asymmetry. This is in confirmation with Ledgerwood (1999) that MFIs prefer to provide products and services to meet the needs of growing businesses since they are considered more reliable and less risky.

Figure 6: Respondents Views on the influence of Nature and Business Type financing decision of SMEs



Source: Field Data (2013)

Figure 6 shows the influence of business type in lending decisions of the SMEs; 43% of the respondents strongly agreed that the type of the business influence the financing decisions of the SMEs 24% of respondents also agreed, 11% of the respondents neither agree nor disagree, 12% of respondents disagree, while 10 strongly disagree that the type of business influence the financing decisions of the SMEs.

Based on the figure 6, it was found out that business type can be stated as a factor affecting access to finance. The lending banks may favour towards to industry sectors that are growing. For example, it was found that sector like manufacturing and constructions seems important for having credit access while at the same time results indicated that both metal-mechanic and wood-furniture sectors have lower credit access than the food processing sector. Their interpretation for this was MFI attach a lower risk premium to food processing sector, construction as well as manufacturing sectors compared to other two sectors.

4.5.2 The use of grace period strategy

It was revealed that this strategy enable more entrepreneurs to access to finance from financial institutions because entrepreneurs have the reasonable time starting repayment of loan given to them and mostly is considered to manufacturing activities since it takes a long time for these firms before making profit.

4.5.3 Tangible asset as financing decision

The study found that collateral is the general practice of NMB Bank in financing to the SMEs. However, it was found that NMB bank evaluate collateral differently as indicated below: Collateral accepted, however only land/building is Land/building and equipment are assigned little or no value accepted as collateral accepted as collateral. According to the NMB policies, the collateral is typically immovable property such as land or building. This pro active may reflect the country's current legal system that provides for the registration of a security interest in immovable property.

Table 4.10: Shows influence of Tangible Assets on financing decision

Responses	Frequency	Percent
Yes	83	92.2
No	7	8
Total	90	100

Source: Field data (2013)

Table 4.10 shows that (92.2%) of interviewed respondents argued that tangible assets was the key determinants of the lending decisions at NMB bank while (7. 8%) of respondents interviewed argued it was. The implication is that tangible assets were the major evaluation for SMEs to qualify for loans at NMB Bank. This indicates that bank financing depend upon whether the lending can be secured by collateral that other factors held constant, firms with more intangible assets need to borrow less, compared

with firms with more tangible assets, because of collateral factor. Generally it was found that many SMEs in Morogoro suffer a lot especially those that are at the infancy stage as they found it difficult to purchase some fixed asset such as land and buildings. SMEs have fewer collateral assets than large firms.

4.5.3 High interest rate

It is thought that with a successful financial reform the interest rate spread will be narrowed to reflect efficiency in the intermediation process, reduction of costs of transactions and improvement of market competitiveness this is not holding because, regardless of tremendous growth in the number of banks, microfinance and SACCOS still are charging higher interest rate.

Table 4.11: Interest rates offered and their effect on SMEs performance

Responses	Frequency	Percent
Strongly agree	39	43.3
Agree	15	16.6
No idea	17	18.8
Disagree	12	13.3
Strongly disagree	7	7.7
Total	90	100

Source: Field Data (2013)

Table 4.11 shows that NMB offers relatively low interest rates since 43.3% of respondents strongly agreed and 16.6% agreed. However, the interest rates need to be adjusted because 32.1% of respondents were no agreed with the statement. Thus is inclusive of 18.8% who are not sure. The findings also show that interest rates were charged at flat rate whereby NMB charge 18% a year which is also considered to be reducing rate.

Furthermore, from the study revealed NMB offered moderate rates since higher interest rates charged could have had economic effects such as increases the cost of borrowing on borrowers because the surplus income is spent on interest payment ultimately contributing to poor business performance.

4.5.5 Age/ Business Life as criteria to access credit

Table 4.12: whether the age of the firm influence Lending decision

Responses	Frequency	Percent
Strongly agreed	19	21.1
Agree	41	45.5
Neither agree nor disagree	8	8.8
Disagree	12	12.22
Strongly disagreed	10	11.1
Total	90	100

Source: Field Data (2013)

Table 4.12 shows that 21.1% agree that age of the firm matters a lot on lending decision, while only 45.5% of the respondent agreed. 8.8% remained silent, 12.2% of respondents disagreed, while 11.1% strongly disagreed. The results of the study show that life of business influence access to credit. Majority of respondents argued that being in the business for many years influence the lending decision; it can be argued that being an older firm means there is lower informational problems. The reason is information required by the lenders to evaluate and process applications is readily available because these businesses have an established reputation or track record.

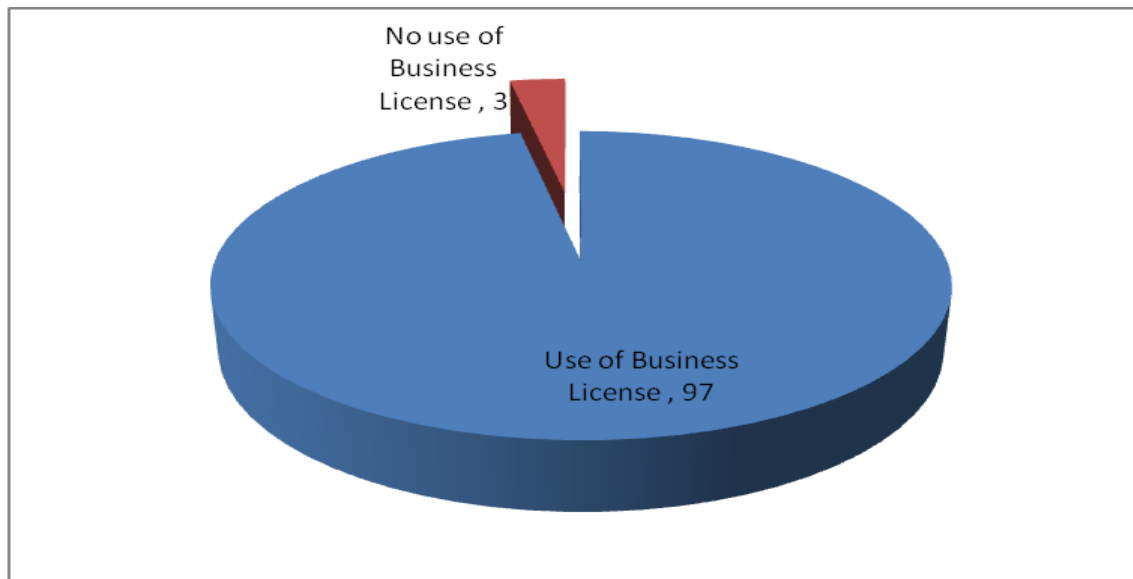
On the other hand, the new firms are not likely to meet the collateral requirements of the banks since they have not accumulated sufficient assets. Combined with the absence of information on their financial records, this makes difficult to lenders to assess lending proposals submitted by new firms. This study found that the financing constraints are

particularly severe in startup enterprises and relatively young firms. During this survey in Morogoro it was reported that most firms with more workers and more years in operation are able to access bank loans, compared to the case of smaller firms.

4.5.6 Business license/ Registration Status of Small and Medium Enterprises

The business license and registration is one of the major criteria used to determine the credit granting process to SMEs which implies that all unregistered companies cannot access credit and this was among the key problems that were identified during the administration of this study. Similar findings were reported by Rugumamu and Mutagwabwa (1999) argued that many small and medium enterprises do not register business due to bureaucracy. This study showed that 87% had accessed credit because they had business license which means they are registered and recognized by authority of Morogoro authority. While, only 13% did not agree that business licence is used as among the key criteria in accessing credit. Figure 7 shows more details.

Figure 7: Business license/ Registration Status of Small and Medium Enterprises



Source: Field Data (2013)

On business registration status, it was observed from sampled SMEs that sampled firms operate as both registered firms and unregistered firms. Results from previous studies show that registered firms grow faster than unregistered firms. In large firms, registration enhances credibility, opens up access to rationed resources and reduces transaction costs when dealing with other firms, thus aiding growth and performance (Goedhuys, 2002). This is interpreted to imply that registered firms owners are more willing to invest in risky ventures that may foster firm growth than unregistered business since most of them are more likely to make use of internally generated funds. Mitullah (2003) argued that unregistered firms are unprotected and the environment in cities is not conducive for business for them. Unregistered businesses in cities are constantly disrupted by municipal authorities in conflict over licensing, taxation, site operation, sanitation, and working conditions.

CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Introduction

This chapter presents the summary of findings, conclusion and recommendations of the study.

5.2 Summary of Findings

The study examined the impact of microfinance credit on the performance of SMEs in Tanzania. The specific objectives included assessing the contribution of microfinance on small and medium enterprises growth and sustainability, examining the relationship between credit terms, liquidity levels and SMEs performance in Tanzania and examining whether microfinance institutions provide favourable credit terms to SMEs in Tanzania or not. The research design used was case study strategy whereby a single unit was selected data collection methods includes interviews, questionnaires, observation and documentary review. Data were analysed through Statistical Package of Social Science.

Findings revealed that due to credit obtained from NMB Bank in Morogoro, SMEs have been able to expand their business operations, profit growth, reduction of poverty among others. It was also revealed that collateral, age or experience of the SMEs owners and size of the firm influence the access of credit. Generally respondents indicated that microfinance loans from NMB had brought an increase to business profit growth trend. It was concluded that the nature of the structure of most SMEs in Tanzania makes debt financing one of the most convenient ways for start – up firms. They depend on banks for loans to boost their business, one of the advantage of taking a bank loan is that its less risky, some of the NMB SMEs customers explained indicated that in the event of default or not being able to repay loan on time, the bank next move is usually to restructure the loan repayment, be it date or monthly payments, to suit the current state of the business making it more flexible and also less risky since their collateral or

security that was given to the bank because of the loan application is not confiscated unlike other micro

Positive relationship has been established between MFIs loans and SMEs performance, growth and sustainability. The study confirms the positive contributions of MFIs loans towards promoting SMEs production, efficiencies and competitiveness. Although MFI sector in Tanzania faces insufficient funds problems which militate against their efforts to grant sufficient loans to SMEs, yet their tendencies to boost the financial needs of SMEs is considerably acknowledged. Furthermore, it has been unveiled that government policies and programs designed to develop SMEs in Tanzania are ineffective and thereby need to be re-conceptualized.

5.3 Conclusion

The intension of this study was to assess the impact of microfinance credit on the performance of SMEs in Tanzania, it can be concluded that most SMEs use loans as working capital mainly to source raw materials for production. The research findings confirmed that the role of financial institutions toward SMEs success is a vital important. Also, some beneficiaries benefited from loan once acquired for example according to the results in the field some of SMEs interviewed concluded that there are positive changes in terms of sales revenues, physical assets, financial assets among others.

Credit terms given by the MFIs are not favourable and if made favourable , the liquidity levels of the SMEs will be high because they would be able to afford borrowing at any given time without worrying about the barring terms. This helps (SMEs) to maintain or even improve their performance in terms of expanding their capital base as well as harvesting more profit arising from increased business activity. The researcher also concludes that when making decisions on credit, most SMEs considered flexibility, loan size and the collateral security as the most important aspects. It is therefore important for MFIs to appreciate that if the three aspects are favourable, they would be a necessary

infrastructure to facilitate good relations between the MFIs and SMEs. This helps to step up the SME performance

For instance with the increasing number of government contracts, most contractors apply for loans to enable them execute these government projects. The nature of the structure of most SMEs in Tanzania makes debt financing one of the most convenient ways for start – up firms. They fall on banks for loans to boost their business

It can also be concluded that one advantage of taking a bank loan is that its less risky, per face-to-face interview, some business customers explained that for some banks for example, in the event of default or not being able to repay loan on time, the bank next move is usually to restructure the loan repayment, be it date or monthly payments, to suit the current state of the business .making it more flexible and also less risky since their collateral or security that was given to the bank because of the loan application is not confiscated unlike other micro finance institutions.

Additionally, the researcher also found out that financial management advice is obtained from business relationship managers of NMB Bank in Morogoro in their day to day interactions with owner-managers of the SMEs and this helps in efficiently managing their businesses

Microfinance institutions are an asset to the developing countries. The services they provide are tailored to meet the needs and aspirations of the local inhabitants and their small up to medium enterprises. It is in fact the truth that products and services put forth to the beneficiaries are not by themselves a solution to the numerous problems affecting SMEs. These problems range from business skills, lack of financial intermediation services, and the lack of markets, technology etc. The financial intermediation services will only provide a platform for the attainment of considerable growth and sustainability of SMEs. It should be noted that microfinance does not serve or solve all the problems of the poor but it serves as a means of helping them to boost their economic activities or augmenting their status.

Microfinance is only a portion of what is needed to boost enterprise activities and developing new markets, increasing income, create and accumulating assets and promoting a culture of entrepreneurship.

In nutshell, a general conclusion can be made that there exists a significant relationship between MFI credits and terms and SMEs performance and growth. This relationship is enhanced by the close business intimacy between the MFIs and SMEs based on trust. It is also supported by the adequate liquidity levels which keep the SMEs running their working capital projects. Increased access to finance will foster efficient growth in the SME sector. Small firms are disproportionately handicapped by a lack of finance, but they receive a stronger boost in growth than large firms if financing is provided. Financing obstacles affect small firm's more than large firms. Small firms not only report higher financing obstacles, but they are also more adversely affected by these obstacles.

5.4 Recommendations

To ensure that MFIs enhance participation in SMEs, sustain the growth and maximal contribution to economic growth and development of the nation, the following recommendations are hereby proffered. Based on the available findings the following are the key policy recommendations:

- (i) Government and MFIs themselves should enhance the out-reach of microfinance through creating awareness of the activities and operations to SMEs especially those in rural and semi-urban areas that are yet to appreciate the benefits of the scheme. Regular campaigns at the local government and ward levels will help to achieve this effectively. More so, the expansion of MFIs through the establishment of rural branches is an imperative for increase access to MFIs services.

- (ii) In a management perspective, MFIs need to improve their credit terms because the findings indicate that they are not favorable but in my opinion, there is need to make the present terms more flexible and reduce on the terms against collateral especially when there is a delay by the SMEs to repay their loans. This requires an understanding of the nature of operations by SMEs such too much exposure to bad debtors.
- (iii) In order for SMEs to improve their performance, it is recommended that owners and managers should maintain adequate liquidity levels through designing strategies to meet their revenue targets. It also requires effective current asset management such as maintaining adequate stock levels which enables them to avoid stock outs whilst avoiding dead stock because it also creates losses. SME owners/ manager need to ensure that they maintain adequate cash levels in order to be able to meet their working capital obligations such as paying their staff on time so that the motivation of timely salaries enable them to continue being committed to delivery of results. These cash levels also help to pay the business suppliers on time because the survival of any business depends on how reliable its suppliers.
- (iv) Apart from provision of tax incentives, and financial supports, it is recommended that Government should try to provide sufficient infrastructural facilities such as electricity, good road network and training institutions.
- (v) Also, the government through responsible ministries should undertake periodic review of the activities of MFIs in line with the microfinance policy objectives/targets so that modifications and corrective action could be taken where necessary. Such an exercise is important if MFIs must effectively support the sustainable growth of SMEs in the country.

- (vi) Reduction of interest rate of SME loans, since SMEs are the engine of growth for developing economies like Tanzania. Bank loans are usually one of the fastest means of acquiring credit for SMEs. This credit is what helps them in boosting their business and in effect economy growing as a result. Thus the cost of such loans should be reviewed downwards to enable smooth repayment and increase in the demand for loans by SMEs to enable growth in their business which will in effect affect the economy as a whole positively.
- (vii) Provide technical assistance and capacity building that prepares SMEs in Tanzania; provide capacity building efforts that could lead to well-managed, sustainably financed SME support mechanisms (especially credit guarantees) at the national level. These mechanisms could be government led, but also could be independent guarantee funds. Technical assistance should help to strengthen controls for SMEs financing, but efforts are required as well to build the financial infrastructure and control framework for the SMEs operation in Tanzania. There should be support to change the strategic or operational capacity and behavior of financial institutions to monitor issues concerning their relationship with SMEs.
- (viii) Most of the Micro and Small Enterprises have low level of education, the government should design a way to enhance entrepreneurial skills in this segment through offering them education on business initiation skills and management. This can be done by incorporating entrepreneurial based curriculum in teaching subjects in schools at all levels so as to inculcate entrepreneurial spirit especially among the youth. Curriculum change in Tanzania is necessary as entrepreneurial studies are taught in colleges and universities and not in primary or secondary schools.

- (ix) The NMB in Morogoro should develop effective SME business training programme and offer proper consultation to their clients. Majority of SME clients are primary level leavers which has impact in their record keeping, preparing marketing strategy and overall decision making. Despite the fact the NMB plc train and advice their clients on adhering to the terms and conditions especially proper loan repayments, clients propose that business training should be emphasized which shall help them on how best to identify opportunities in the market, proper marketing strategies, business management and entrepreneurial skills that will help in business growth.

However, the theoretical contribution of this particular study is on the extended body of knowledge. The study contributes in the body of knowledge whereby academician and other scholars get knowledge about the effects of microfinance products in improving SMEs Tanzania.

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QUESTIONNAIRE FOR THE BENEFICIARIES OF NMB CREDITS

Dear Respondent,

This questionnaire aims to collect data for partial fulfillment of the requirements for the award of Master Degree of Business Administration (MBA) awarded by Mzumbe University. The researcher intends to assess the impact of microfinance credit on the performance of small and medium enterprises using Morogoro as a case study.

Therefore the researcher declares that, this research is for academic purpose only. You are kindly invited to complete this questionnaire as directed for a purpose of facilitating the study. Information from this document will be confidential and in no way will it be communicated to any person. Thank you in advance.

PLEASE NOTE: Your name should not appear anywhere in this document.

Part I: General Information

Circle the correct answer

Gender:

- a) Male
- b) Female

Age:

- a) 20 – 25 years
- b) 26 – 30 years
- c) 31 – 35 years
- d) 36 – 40 years
- e) 41 – 45 years
- f) 46 – 50 years
- g) Over 50 years

Part II: Information on credits from MFIs

1. Have you ever taken a loan from NMB?
 - a. Yes
 - b. No
2. What were the uses of a loan?
 - a. Capital for business
 - b. Education for children
 - c. Housing
 - d. Agricultural activities
 - e. Others (mention) _____
3. Have you used a loan from NMB to start an income generating activity?
 - a. Yes
 - b. No
4. What were the changes in your income after obtaining a loan from NMB?
 - i. _____
 - ii. _____
 - iii. _____
 - iv. _____
5. Are you presently engaged in any kind of income generating activity?
 - a. Yes
 - b. No
6. If the answer is YES in the above question, what kind of income generating activity are you involved in?
 - i. _____
 - ii. _____
 - iii. _____
7. Do you manage to repay the loans taken from NMB on time?
 - a. Yes
 - b. No

8. Do you see interest rates charged on NMB loans to be a burden?
 - a. Yes
 - b. No
9. Do you see any change in income and business after obtaining NMB credit?
 - a. Yes
 - b. No
10. What are the consequences of failing to repay your loans in time?
 - i. _____
 - ii. _____
 - iii. _____
 - iv. _____
 - v. _____
11. Do you see NMB loan scheme as favourable for the development of your enterprise?
 - a. Yes
 - b. No
12. In your own opinion, what should be done to make NMB credits an important tool for development of SMEs in your area?

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Rate the situation concerning NMB and their microfinance services in Morogoro

Instructions

Below are statements related to NMB credit scheme. Read each statement carefully and put tick (✓) in the appropriate box which you agree with according to the key.

Note: Each statement should have only one tick

		Strongly agree	Agree	Neutral	Disagree	Strongly disagree
16	NMB credit scheme is the best way of improving the performance of SMEs					
17	NMB credit has played an important role in elevating status of your enterprise					
18	NMB provides loan on time when needed by the clients					
19	NMB credits comes with affordable interest rates					
20	NMB credits satisfies the financial needs of the enterprises					
21	You are satisfied with the treatment clients get from NMB employees					

THANK YOU FOR YOUR COOPERATION