FACTORS AFFECTING THE GROWTH OF SMALL MEDIUM ENTERPRISES (SMEs)

FACTORS AFFECTING THE GROWTH OF SMALL MEDIUM ENTERPRISES (SMEs)
A CASE OF MUFINDI DISTRICT

By

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A Research to be Submitted in Partial Fulfillment of the Requirement for the Award of the Masters of Business Administration (MBA_CM) in Corporate Management of Mzumbe University

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CERTIFICATION

We,the undersigned ,certify that we have read and hereby recommend for the acceptance by Mzumbe University Mbeya Campus college a research report entitled, ‘***Factors affecting the growth of small medium enterprises (SMES) a case of Mufindi district ’*** in partial fulfilliment of the requirements for award of the bachelor degree of Accounting and Finance in business sectors of Mzumbe University (MBA_CM).

Signature

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Internal Examiner

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I, **David Yosia Simbeye**, declare that this research report is the result of my own work and that it has not been presented and will not/ be presented to any othe university for a similar .

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ACKNOWLEDGEMENT

This work is the end product of the contribution of several individuals. The dissertation could not have been completed without support of many people.

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Finally, I would like to state that, any errors or shortcomings that may be found in this work, am entirely fully responsible.

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DEDICATION

This dissertation report is dedicated firstly to my lovely wife Mariam Daniel Kasomo and my children Fabian David Simbeye, Bressing David Simbeye and Emmanuela David Simbeye.

LIST OF ABBREVIATIONS

AS	:	Asset Structure
EBIT	:	Earnings Before Interest and Tax
FS	:	Financial Statement
GDP	:	growth domestic product
LEV	:	Leverage
ASB	:	Accounting Standards Board
IFRS	:	International Financial Reporting Standards
MM	:	Modigliani and Miller
MNCs	:	Multinational Corporations
PERS	:	Private Entities Reporting Standards
NSDC	:	National SME Development Council
PERS	:	Private Entity Reporting Standards
POT	:	Pecking Order Theory
PROF	:	Profitability
QUAL	:	Quality of Information
RO	:	Return on Asset
ROE	:	Return on Equity
SME	:	small and medium sized enterprises
SMIDEC	:	Small and Medium Development Corporation
TOT	:	Trade of Theory

ABSTRACT

This paper aims to investigate the factors affecting the growth of small medium enterprises (SMEs) from manufacturing sector in Tanzania. Specifically, this study wants to examine the effect of asset structure, profitability, and quality of information, size and age on leverage. Descriptive analysis and frequency were used to investigate the most significant factors that affect the capital structure choice of Tanzania SMEs during the year 2013. In the first model, both results find a negative and significant relationship for profitability and size with leverage while asset structure, quality of information and age show negative but not significant relationship with leverage. However, using a second model, asset structure shows a significant positive relationship with leverage, while quality of information shows significant negative relationship with leverage. The analysis indicates that firstly; the results are consistent with some capital structure theories such as trade-off theory and pecking order theory. Secondly, quality of information, asset structure, profitability and size are important factors that growth of Tanzania SMEs.

Keywords: **Leverage, SMEs, pecking order theory, trade-off theory, SMEs Growth**

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CHAPTER ONE
GENERAL INTRODUCTION

1.0 Introduction

This chapter aims to present an overview of the importance of SMEs Growth and to briefly discuss the background of SMEs in Tanzania. This chapter also provides discussions on the background of the study, problem statement, research question, research objective, scope and limitations of the study, and lastly, the organization of the study.

1.1 Background of the Study

Financing decision is one of the most significant decisions that a firm need to consider as this decision can influence the firm value and determine whether a firm can expand its business or face bankruptcy. A wrong decision made by the manager may lead to financial distress and ultimately affect the business activity. In this light, a blend of securities and financing sources by an organization to finance its investment activities is known as capital structure (Zabri, 2012), and managers play a significant role in selecting the best financing source that matches the business organization.

The financing sources available either through equity or debt. The equity is given by the proprietor and shareholders, while, debt is acquired or obtained from banks and monetary establishments. In other words, capital structure is known as the blending of financing source which is derived from equity or debt (Saarani,A.N.,& Shahadan,F., 2013)**.** In this study, capital structure is a paramount importance as it represents fortifying sources needed by SMEs to operate and expand their business. Several researchers have found that there are many factors that impact the capital structure of Tanzanians companies, namely profitability, firm size, growth opportunity, asset tangibility, liquidity, firm age, non-debt tax shield, investment, earning volatility and asset structure (Benkraiem,R.,& Gurau,C. , 2013); (Haron R. , 2014); (Hussain ,S.S.,Hamza,S.,& Miras,H., 2015); Similar factors have also influenced the capital structure of firms in other countries such as Iran, Ghana, India, Nigeria, Pakistan and so on.

This study wants to examine the influence of capital structure on Tanzanian SMEs. Herewith the study briefly explains the timetable of SME definition which is previously its name was micro, small and medium enterprises (MSMEs) before changed to SMEs. A review of the SME definition has been conducted in 2013. The new definition was approved in the 14th National SME Development Council (NSDC) Meeting in July 2013. The definition covers all sectors, including services, manufacturing, agriculture, construction and mining, and quarrying. There are two criteria to identify the definition of SME that is sales turnover and the number of full-time employees.

On May 2nd, 1996, the Small and Medium Development Corporation (SMIDEC) was established in Tanzania. It aims to upgrade the status of SMEs by giving several facilities to entrepreneurs, such as financial aids, consultancy services, infrastructure facilities, market penetration and other programs. Moreover, in 2004 until 2007, the strategies such as:

i. The annual SME Integrated Plan of Action such as strengthening the enabling infrastructure, building the capacity and capability of domestic SMEs and enhancing access to financing by SMEs;

ii. SMEDEC Incentive for SMEs including giving tax incentive to stimulate investment, grant assistance, loans, credit and equity participation, and infrastructure and supporting service;

iii. Government Funds and Schemes for SMEs such as the SME assistance fund, the SME assistance guarantee scheme, the small debt resolution scheme and so on; were formulated for SMEs development across all economic sectors by the National SME Development Council (NSDC). It is also to enhance the effectiveness of the implementation of SMEs improvement program in Tanzania.

SMEs play an important role in the Tanzanian economic development. Thus, the role of the SMEs in financial advancement is noteworthy in light of the fact that it can be viewed as the spine for the country’s economic growth. SMEs also provides opportunities for particularly in terms of employment opportunities, improve household income and encourage training skill for entrepreneurs before they move to invest in larger companies (Zain, Z.M.,Anas,Y.,Hassan,F.,Lear,H.,& Shamsuddin,S., 2012). The most significant contribution of SMEs in Tanzania is in providing job opportunities. Hence, the development of SME in Tanzania will help to reduce the unemployment problem by creating job opportunities, particularly in rural areas (Kandasamy, 2015); (Katua, 2014) ;(Kayadibi, 2013); (Madanchian,M.,Hussein,N.,Noordin,F.,& Taherdoost,H., 2015).

According to (Omar,S.S.,Arokiasamy,L.,Ismail,M., 2009) and (Jan Khan ,m.w.,& Khalique,M., 2014), SMEs bring positive effects on a country's economic growth, but this important idea of economic growth still remains uninvestigated. Undoubtedly, SMEs have a significant contribution to the economic growth in Tanzania Apart from providing job opportunities, the Government programs also facilitates SMEs to access in financing sources (Kandasamy, 2015). Many previous studies have reported that the small firms especially SMEs is facing financial difficulties such as loan accessing problem to commence their business (Khalique, 2011).

Normally, smaller firms experience higher financial obstacles compared to large firms, due to several issues such as financial institutions' analysis to obtain loans, the lack of financial aid program for new entrepreneurs, the lack of tangible assets for collateral purposes, and other strict requirements by banks. Thus, SMEs have to use their own funds to start their businesses (Haron H. I., 2013). Consequently, many programs were developed by the Government to overcome this issue. Furthermore, other government agencies also provide assistance for the SME development. For instance, the Development & Technopreneur Development program which was implemented by the Ministry of Science, Technology and Innovation (MOSTI) in 2011. The objective of the program is to assist SMEs by providing financial support; such as loans, machinery, furniture, and non-financial support; such as advice, guidance and moral supports by matching experienced international SMEs with new entrepreneur (Kandasamy, 2015)

The increment of various items produced by local SMEs is one of the successful signs of SMEs in Tanzania (Kayadibi, 2013). This encourages the public to purchase local products and indirectly support Tanzanian products compared of imported products.

Thus, this approach can also reduce reliance on imported products, and promoted Tanzanian products export. In this light, a statistic by The SME Corporation Tanzania and Department of Statistics Tanzania shows that SMEs are forecasted to contribute to

Gross Domestic Product (GDP), export and employment sector in Tanzania. Based on SMEs had further contributed to the economic improvement such as, assisting in household income distribution, introducing innovations, able to gain competitive advantage and also able to produce high quality of goods and services which are comparable with bigger companies (Kayadibi, 2013). Consequently, high export activities can also reduce the currency fluctuation, as the value of Tanzanian currency is dropping. Therefore, the establishment of SMEs in Tanzania it will help to enhance economic growth because they generate income and raise profit.

SMEs also play a significant supporting role for industries. For example, by providing manufactured goods that are needed by large manufacturers such as automotive, wood products, chemicals, machinery and equipment, engineering, electrical and electronics (Kayadibi, 2013). This indicates that both small and big firms are interdependent with each other. Consequently, upon realizing the importance of the supporting role provided by SMEs, the government has tried a few activities to cultivate a close relationship between SMEs and large firms.

The programs were implemented to integrate small and large firms and increase productivity efficiently. Inherently, cooperation between SMEs, MNCs and GLCs are fostered through outsourcing Program, the Franchise Development Program, the Vendor Development Program (VDP), the Industrial linkage program, and the Global Supplier Program. As a result, the number of vendors has increased and companies are actively participating in the VDP program (Kayadibi, 2013).

The role of financing source and behavior of SMEs should be given prior attention as this issue plays an important role in the development of Tanzanian economies. The SMEs have contributed significantly in the development of increasing the GDP, creating jobs and employment opportunities (Abdullah, 2011). The importance of financing behavior to SMEs have encouraged the Government to offer initiatives through the various schemes and programs such as credit guarantee facilities, debt resolution scheme and many more. Thus, these programs are to ensure that the financing requirements will not be a barrier for the development of the business.

The motivation of this study is to investigate SMEs financing behavior which is bringing a significant contribution to the country. However, the development and expansion of SMEs is depending on their sufficient financing and capital to run the business (Saarani,A.N.,& Shahadan,F., 2013). Hence, to understand how firms finance their operations, it is necessary to examine the determinants of capital structure (either the profitability, quality of information, firm age, firm size and asset structure) will affect the financial sources decisions.

Determinants of capital structure of prior studies demonstrates that very limited amount of researchers have been conducted in certain of sectors or industries in Tanzania such as firms from financial sector like banks, insurance and finance companies because of the different accounting categories and rules governing by these firms (Haron R. , 2014); and (Zabri, 2012). Therefore, this study extends the existing literature to give a deeper understanding about the financing behavior of Tanzanian SMEs.

1.2 Problem Statement

Various studies on the determinants of SMEs Growth have been undertaken in both developing and developed countries around the world including those focusing on manufacturing companies in different countries such as India, Turkey, Italy and Pakistan (Chadha ,s., & Shama,A.K., 2016);(Acaravci, 2015);(Muscettola, 2014); (Zhang, 2010).

SMEs firms often face difficult to obtain financial resources to undertake innovative projects and increase firm growth as they face a lot of difficulties in obtaining loans from financial institution (Cela,S.,Shkurti,R., & Hilaj,B., 2013). Due to such financial problem, SMEs face difficulties in expanding their businesses and consequently affect economic growth. Therefore, this study attempts to examine the factors that can affect the capital structure of SMEs in the Tanzanian context.

This paper also intends to investigate how the characteristic of capital structure especially the quality of information, in this case, the use of international Financial Reporting Standard (IFRS) can impact firms' choice on their capital structure decision. This is because the determinant of capital structure is still an issue in Tanzania due to the lack of past studies (e.g.(Haron R. , 2014); (Hussain ,S.S.,Hamza,S.,& Miras,H., 2015); (Zabri, 2012) on this topic. In this regard, the previous studies only focused on few sectors or industries and very little study has been done in manufacturing industries in Tanzanian SMEs (such as (Haron H. I., 2013). Therefore, to provide a better understanding of financial choice between equity and debt, this study contributes to the literature by examining the determinants of the capital structure of manufacturing firms in Tanzania.

This paper examines five characteristics of firms that can be used in determining the growth of Tanzanian SMEs, namely quality of information, firm size, firm age, asset structure and profitability. Few studies have been done on the quality of information in financial statements prepared by firms. In a Belgian setting, (Caneghem, 2012) describe two formats of financial statement used by Belgian firms, namely the complete format and abbreviated format. A complete format contains full and detailed information that records all business transactions, while the abbreviated format contains only the information that is considered relevant and less items in the financial statement. (Caneghem, 2012)Find that the quality of financial information is positively related to leverage. On the other hand, to the best knowledge of the researcher, no study has been undertaken in Tanzania on the relationship between quality of information in the financial statement and leverage.

Many studies have investigated about firm size as one of the capital structure characteristics. Some studies found that size does not affect firm leverage (Njeru, 2012). Other studies found a significant and positive relationship between size and leverage (Acaravci, 2015); (Boateng, 2004). However, several empirical studies have reported that firm size has negative and significantly related to leverage (Hussain ,S.S.,Hamza,S.,& Miras,H., 2015). The studies furthermore found a mixed relationship between firm size and leverage.

(Benkraiem,R.,& Gurau,C. , 2013) Thus, the researcher need to carry out this study due to conflicting findings of past studies on the association between firm size and leverage or overall debt. However, there are several studies that reported that firm age has a negative significant relationship with leverage. Some researchers also argued that older firms that have strong financial resources have a tendency to have less debt (Ogbulu, 2012). Furthermore, Sherif and Elsayed (2013) found that the relationship between firm age and total leverage is positive. However,(Abu Mouamer, 2011) stated that firm age has no significant relationship with leverage. Due to the inconsistent and mixed findings, this study will try to reexamine this issue in the Tanzanian context.

Asset structure comprises of tangible assets, fixed assets, current assets and any item that can be declared as valuable to the firm. The studies of (Acaravci, 2015),(Chadha ,s., & Shama,A.K., 2016)and (Zabri, 2012) found that the relationship between asset structure and capital structure is positive and significant.

Other findings indicated that the relationship between asset structure and leverage is positive and significant (Hussain ,S.S.,Hamza,S.,& Miras,H., 2015); (Muscettola, 2014). The studies also pointed out that the relationship between asset structure and leverage is positive (Kiong and Lean, 2011; Sherif and Elsayed, 2013). However, some studies revealed that the relationship between asset structure and debt is significant negative (Amidu, 2007; Bereźnicka, 2013; Psillaki and Daskalakis, 2009; Sheikh and Wang, 2011). Nevertheless, a few studies found that there are mixed results between asset structure and debt (Abu Mouamer, 2011); Alipour et al., 2015; Ibrahim and Masron, 2011). Due to the conflicting results, a study on the relationship between asset structure and leverage in the Tanzanian context is timely needed.

Studies by Chadha and Sharma (2015), Ibrahim and Masron (2011) and (Acaravci, 2015), (Zhang, 2010) and Sherif and Elsayed (2013) reported that profitability is positively related to leverage. Similarly, (Chadha ,s., & Shama,A.K., 2016) reported the relationship between profitability and leverage is positive and significant. However, several studies indicated that the relationship between profitability and leverage is negative (Fareed et al., 2014; Kiong and Lean, 2011; Psillaki and Daskalakis, 2009; Sheikh and Wang, 2011) and in some studies found this negative relationship is somewhat significant (Abeywardhana, 2015; (Hussain ,S.S.,Hamza,S.,& Miras,H., 2015); Shubita and Alsawalhah, 2012). In light of the conflicting results, it is worthwhile to reexamine this variable in the Tanzanian context.

1.3 Research Question

The following research question is developed to determine the factors that influence growth of Tanzanian SMEs:

i) What are the firm characteristics that affect the capital structure of Tanzanian SMEs?
ii) Does firm size is positive related to firm leverage?
iii) Does firm age is negatively related to firm leverage?
iv) Does assets structure is positively related to firm reverage?
v) Does profitability is negatively related to firm reverage?
vi) Does quality of information is positively related to firm leverage?

1.4 Research Objective

i) To find out the firm characteristics that affect the growth of Tanzanian SMEs.
ii) To examine the relationship between firm size and firm leverage.
iii) To examine the relatioship between firm age and firm leverage.
iv) To examine the relatioship between assets structure and firm leverage.
v) To examine the relationship between profitability and firm reverage.

vi) To examine the relationship between quality of information and leverage.

1.5 The Significance of the Study

The study will help the researcher to understand the impact of growth on performance of SMEs in Tanzania. Also the study will enable the researcher to acquire acknowledgement as a partial fulfillment of the Bachelor Degree of Accounting and Finance. The findings will be good input for the policy makers in formulating effective strategies and policies which will assist the financial manager of the SMEs to determine effective financing mix to improve the performance of SMEs in Tanzania. The study may save as the stimulant for further studies to be conducted on similar or related topic by other researchers.

1.6 Scope of the Study

The study investigates the determinants of growth of manufacturing industry in Tanzanian SMEs. The period covered by the study is only for the year and the sample is restricted to same SMEs firms from the manufacturing sectors. Furthermore, this study only relies on secondary data that is SMEs annual reports for the year. It is the only data available at the time of data gathering.

1.7 Limitations of the Study

They are the constraints on generalisability and utility of findings that are the result of the ways in which you choose to design the study and/or the method used (Thomson, 2007).

Poor cooperation from other respondents from the targeted SMEs owners/Operators because they were not willingly to provide the information relevant for the study because of confidentiality of such information; hence the researcher took up the responsibility of informing respondents on relevance of the study and assured confidentiality regarding their information. Also, the time allocated for the field work, data collection, data analysis and report writing was limited to enable carrying out a comprehensive field research with a large sample size. The researcher solved this problem by working even on weekends, asking the respondents to pardon him for the inconvenience if any caused. Meanwhile, financial difficulties also affected a researcher during data collection. This is due to the fact that the researcher is sponsoring himself, thus was depending on her only source of income (salary), hence it was difficult to meet all expenses while conducting the research. To solve this problem the researcher tried to conduct the study as cheap as he could to curb financial constrain.

1.8 Organization of the Study

The rest of the study is structured as follows: Chapter 2 provides a review of previous studies and theories of capital structure. Chapter 3 explains the research methodology which covers the research framework, hypothesis development, research design, variable definition, measurement of variables, sampling, data collection procedures and techniques of data analysis. Chapter 4 discusses the findings and the analysis of data. Lastly, Chapter 5 presents the conclusion and recommendation.

CHAPTER TWO
LITERATURE REVIEW

2.0 Introduction

This chapter reviews previous studies on the determinants of SMEs specifically those focusing on capital structure theories and provide empirical evidence on specific factors that influence capital structure.

2.1 An Overview of Capital Structure Theories

The study of capital structure attempts to explain the mix of securities and financing sources used by firms to finance their investment. Several determinants have been recognized as being influential in capital structure decision and represent different arguments relating capital structure theories (Haron R. , 2014). These include quality of information, firm age, firm size, asset structure and profitability. This section will explain the theories that may influence capital structure decision.

There are still doubts in identifying the accurate theory regarding capital structure choice. (Haron R. , 2014)

Argued that there is no theory that is able to, independently describe the complexity of capital structure practice. Similarly, Ahmeti and Prenaj (2015), claimed there are no proper theory of capital structure. Moreover, the current theories can just clarify certain aspects of the variety of financial structure choice despite many researchers who debated on the exact theories that are appropriate in explaining capital structure. This is due to the lack of comprehensive theory that explains firms’ capital structure (Al-Ajmi, Hussainand Al-Saleh, 2009; (Zabri, 2012). Therefore, prior studies have proposed several finance theories that can be applied in describing the capital structure, namely the Modigliani and Miller (MM) theory

2.1.1 Modigliani and Miller (MM) Theory

In 1958, Modigliani and Miller have published a new theory of capital structure that is known as MM theory, who suggested the theorem of irrelevance proposition. The MM proposition states that a firm’s financial decision does not affect its value. It states that there are no costs involved and the market can work efficiently. However, this theory was not relevant in the real market.

The original proposition and the fundamental idea of MM theory states that a fully efficient market is a market that has no taxes, transactions or bankruptcy cost, and there are plentiful of information available to all parties. However, in 1963, the effects of taxes were included in MM theory model so that the theory becomes nearer to the reality (Ahmeti and Prenaj, 2015). According to this new model, firm can lower their tax payment because interest payments are deductible from tax due to the increase in a firm's value and leverage. Thus, the balancing between the increasing in leverage and decreasing in cost of capital would bring to the optimal capital structure.

However, several studies (e.g. (Hussain ,S.S.,Hamza,S.,& Miras,H., 2015); (Saarani,A.N.,& Shahadan,F., 2013) have revealed that the MM theory is ineffective under a variety of situations. This is because other costs such as taxes, transaction costs, bankruptcy costs, agency conflicts, adverse selection, lack of isolation between financing and operations and other relevant costs are not taken into consideration. In this case, the MM theory fails to suit the need of capital structure theory which considers all those conditions in the real capital market. Therefore, alternative theories have emerged from the weakness of MM theory, namely trade-off theory and pecking order theory.

2.1.2 Trade-Off Theory

The trade-off theory (TOT) had gathered attention in lieu of the debate on the MM theory (Jahanzeb, Bajuri, Karami and Ahmadimousaabad, 2014). The inclusion of the irrelevance theorem to tax effect had created the benefit of debt which shield the income from taxes. Consequently, the TOT proposes a parallel correlation and for instance, it recommends the association between leverage and profitability is positive by stating that high profitable firms prefer high debt to shield the income from taxes.

According to TOT, the firms can achieve an optimal capital structure by trade off the benefit of debt finance with debt's disadvantage. Benefits of debt include tax shield, the reduction free cash flow, conflict between managers and shareholders. The disadvantages of debt includes financial distress, cost associated underinvestment and assets substitution problem (Hussain ,S.S.,Hamza,S.,& Miras,H., 2015). According to Stretcher and Johnson (2011), this theory has two features. First, by considering tax effect; since the interest expense is tax deductible, the more debt incurred by the firm, the more wealth acquired by the firm due to the low tax payment. The firm can use the advantage of the tax shield as leverage can increase firm's value if a firm uses more debt. The second feature is the risk of increasing debt to the capital structure. In other words, the firm can take advantage of tax shield by adding more debt, but too much reliance on a large proportion of debt will bring financial distress because the firm has to meet interest payment obligations.

Moreover, the TOT emphasizes that an optimal capital structure can be obtained through the trading off the costs of debt and equity against their benefits. The use of debt is one of the benefits of debt tax shield advantage. On the other hand, the costs of potential financial problems are the main disadvantage of debt, particularly when the firms are heavily relying on debt (Jahanzeb et al., 2014). Thus, to obtain an optimal capital structure, the cost of debts and benefits should be balanced consistently.

2.1.3 Pecking Order Theory

Myers (1984) proposed the pecking order theory (POT) which is slightly, in contradictions with the TOT. The POT is based on asymmetric information between insider (managers or shareholders) and outsider (investors). The asymmetric information occurs when the managers have more information than the outside parties. Moreover, the POT states that a firm will decide their financial structure based on financial hierarchy, firstly using internal fund (retained earnings), secondly using debt, and equity as a last option or/and does not consider an optimal capital structure like TOT. Thus, this theory proposes an inverse correlation where a negative correlation is proposed as high profitability firms has a tendency to reduce the amount of debt. This is because firms are capable to create their own fund before seeking for external funding and will only borrow when their retained earnings are not sufficient for profitable investment or to pay dividends (Rahman and Arifuzzaman, 2014).

In other words, the POT proposes those firms' preferences to use source of funding by using internal fund first before going to external financing for the purpose of financing their valuable project. This is consistence with Kumah (2013) in his study who suggests that firms will choose to use their generated fund before seeking for external sources. Due to asymmetrical and transparency problem, SMEs have limited access to external financing, thus the POT is more applicable to SMEs (Holmes and Kent, 1991).

2.1.4 The Agency Theory

The agency costs occurred because of the use of debt in a firm's capital structure.(Jensen M. , 1976)emphasized that agency cost arise because of internal factors such as a conflict of interest between shareholders and managers (i.e. agency cost of equity) and a conflict of interest between debt-holders and shareholders (i.e. agency costs of debt). Equity-holders captured on expected high-returned investment projects whereas debt-holders acting on behalf of principal in collecting the fixed amount of interest payment. According to (Myers S. , 2001), when there is a risk of default, the conflicts of interest between debt holders and shareholders will arise.

Hence, if there is no default risk, the income, value, or risk are not able to attract the interest of debt holders and vice versa in case of the probability in default, the managers tend to have an interest of shareholders to maximize the wealth of shareholders (Sheikh and Wang, 2011) and financial distress may increase if firm taking too much debt financing (Jensen M. , 1986). Debt-holders should correctly predict the equity-holders' intentions as to reduce loss, because debt-holders prefer less risky projects, while equity-holders prefer the otherwise.

Agency cost arises because of conflict of interest between managers and shareholders and also due to separation management of firm and ownership. The conflicts of interest emerged when the managers tend to maximize their own interest rather than maximizing the firm's value due to the increase of ownership separation and control (Dawar, 2014). In this light, managers are often attracted to invest in projects that can increase their own personal benefits rather than maximizing the firm’s value (Jensen M. , 1976). Consequently, the use of leverage in capital structure by issuing debt may reduce agency costs between shareholders and managers, but it can affect the future cash outflows, resulting in higher estimated cost of financial problems and insolvency (Dawar, 2014). When the leverage level is lower, increasing of debt may mitigate agency conflicts through positive incentive for managers, while at higher levels of leverage, the increase of loses in a firm’s project will result in a negative net present value which can cause financial distress and bankruptcy.

The conflicts between shareholders and managers can be reduced by using debt (Jensen M. , 1986). The agency costs can be reduced by using debt since debt plays a significant role in monitoring managers while utilizing the available of free cash flow. Then, to discipline the managers, firms can increase the leverage. By increasing the leverage, managers are contractually obligated in paying the interest payments. The probability to adhere to the payment schedule will decrease if the managers fail to use the free cash flow efficiently. Furthermore, bankruptcy can occur in case if the managers fail to do so, and managers would lose their right in the firm (Kochhar, 1996). Therefore, it can be seen that debt plays an important role in decreasing the amount of free cash flow accessible to managers to encourage them to utilize the properties properly.

The agency theory of capital structure also emerged due to unequal information. Unequal information exists when the private information obtained by managers or insiders regarding the features of the firm's expected return investment in future either high or low return. In other words, the information asymmetry which is the part of capital structure is created to increase the effectiveness in the firm's investment decisions which was first discussed by (Myers ,S.C., & Majiluf ,N.S., 1984) and (Myers, S.C, 1984). Thus, the companies normally prefer internal financing over external financing while these researchers believe that the issue of equity would bring negative information to outside investors in the information asymmetrical world.

The problem of agency cost of debt might reduce the moral hazard and adverse selection problems if there is high transparency in SMEs especially in financial report disclosure (Ang, 1992). This is supported by Ang (1992) and (Jensen, 1976) who argued that the main of agency problem in SMEs is not the separation of ownership and management but rather between the internal and external contributors. This theory explains that the leverage of SMEs is covered by financing constraints, and this is not present in larger firms, especially in the first early years as the firm tries to survive in the industry (Burgstaller and Wagner, 2015).

2.1.5 Market Timing Theory

More recently, in 2002, Baker and Wurglerhas recommended a theory that is known as equity market timing. This theory has a robust consequence on firm's financial behavior. It used the market to book values of the firm to time the market and found that the changes in leverage are statistically positive and significantly related to their market timing measure. Consequently, the study concluded that this theory was the outcome of previous efforts of capital structure to time the equity market. On the other hand, this theory contends that firms will issue their equity when the stock prices increase and repurchase their own stock when the price is low.

Consequently, fluctuations in stock price will affect firms' capital structure. Equity market timing consists of two, which are; the first is the companies are allowed to issue equity directly after information is released in a rational economic decision making situation. This decreases the asymmetry problem between managers and stockholders. By decreasing the information asymmetry, it will increase the stock price which brings the opportunities for the firm to construct their own timing market. The second predicts that in the irrational economic decision situation, managers cannot successfully predict stock returns and timing the market perfectly. There is a time-varying mispricing of the stock due to irrational economic decision which managers issue equity at irrationally low price and repurchase equity at an irrationally high price. This assumption tries to say that the market timing theory is sometimes inefficient in the actual market because the managers often time the equity market by issuing either undervalued or overvalued stock as their consideration.

2.2 Determinants of Capital Structure

The capital structure is determined by several factors. The aim of this section is to examine the previous studies on the determinants of capital structure. Many researchers (e.g.(Abor J. &., 2009); (Benkraiem,R.,& Gurau,C. , 2013); (Chadha ,s., & Shama,A.K., 2016); Fareed et al., 2014; Kiong and Lean, 2011; Shubita and Alsawalhah, 2012; Uyar and Guzelyurt, 2015) have examined the relationship between firms' characteristics and leverage. The results, however, are mixed. Therefore, this study intents to discuss the following factors; quality of information, firm size, firm age, asset structure and profitability that are most likely to affect capital structure. This section reviews and discusses the prior studies on the above-mentioned variables.

2.2.1 Quality Information

Very few studies have investigated the relationship between quality of information and capital structure. A study conducted by (Caneghem, 2012) and Campenhout and Caneghem (2009) who investigated on quantity and quality of information on SME financial structure, found that high quantity and quality of information will increase the amount of leverage. However, the low information quality prevent firms from obtaining external funds, which is consistent with TOT who suggests a positive relationship between quality of information and capital structure(Caneghem, 2012). The firms with more information quality tend to depend more on debt, which is consistent with firms having a lower cost of obtaining external fund. Moreover, Kardan, Salehi and Abdollahi, (2016) conducted a study on the correlation between the external financing and the financial reporting quality. The study found that the quality of financial reporting is positively related with debt financing.

2.2.2 Firm Size

Firm size has become a control variable in financial market even though it is not uncommonly among the significant variables. Prior studies (e.g. (Boateng, 2004); Chadha and Sharma, 2016; Saarani and Shahadan,2013b) have used firm size in examining the determinants of capital structure. Researchers in Tanzania have found that firm size is among significant variable associated with leverage (Hussain et al., 2015; Ibrahim and Masron, 2011; Suhaila and Wan Mahmood, 2008). However, there are mixed findings on the relationship between firm size and leverage. For instance, Researchers who investigated the determinants of capital structure of Tanzanian SMEs found that firm size is insignificant and negatively related with total debt ratio and short term debt ratio, but positively related with long term debt ratio.

The TOT proposes a parallel correlation between firm size and leverage where large firms tends to increase their debt level in order to obtain an ideal capital structure. A recent study that investigated SMEs' capital structure across countries found that there is positive relationship between firm size and leverage (Psillaki and Daskalakis, 2009). Similarly, (Boateng, 2004) who examined the determinants of capital structure in Ghana found that the relationship between firm size and leverage is positive. These findings showed that larger companies tend to have more debt because they are more diversified as well as more stable in cash flow, which means that they are less disposed to bankruptcy.

Gomez, Rivas and Bolanos (2014) conducted a study on the capital structure determinants of in Peru. They found that there is significant and positive relationship between firm size and leverage. Similarly, (Nikolaos, 2014) investigated the capital structure and size of SMEs in Greece and found that firm size is positively related to debt ratio, which is in line with the results of other studies (Ogbulu and Emeni, 2012; Sheikh and Wang, 2011; Sherif and Elsayed, 2013; (Zhang, 2010).

Palacin-Sanchez and Ramirez-Herrera (2013) investigated the capital structure of SME across different regions in Spain. They found the relationship between firm size and debt ratio and long term debt ratio is positive. Similarly, Jo˜eveer (2013) examined the capital structure of small firms in Western European in 2000. The study involved small and large firms, as well as listed and unlisted firms. The study found that firm size is positively related to leverage for listed and unlisted firms.

However, several studies on determinants of capital structure found that the relationship between firm size and capital structure is negative (Alipour, 2015); (Kariuki, 2014); Masnoon and Saeed, 2014). Researchers who examined the capital structure and firm determinants in Tanzanian SMEs found that the relationship between firm size and long term debt is negative. Similarly, (Suhaila and Mahmood (2008) who studied capital structure in Tanzania SMEs found a similar result but firm size is significantly related to total debt.

This is in line with the POT which contended that finance source is based on preference ranking by using information asymmetry between managers and shareholders. The POT explains that large firms have more accessibility to the equity funding source rather than small firms, therefore large firms generate greater information asymmetry to attract less debt. In other words, a negative relationship indicates that large firm tends to use less debt because the large companies will reduce the undervaluation of new equity issue and inspires the firms to finance through its equity.

However, a recent study by Uyar and Guzelyurt (2015) reported mixed results. They indicated that the relationship between firm size and short term debt is negative, but positively related with long term debt. Other studies by (Benkraiem,R.,& Gurau,C. , 2013); and (Saarani,A.N.,& Shahadan,F., 2013) examined the relationship of firm size with three dependent variables, namely total debt, long term debt and short term debt. These studies found that the relationship of total debt and short term debt with firm size is negative, but positively related with size and long term debt.

Similarly, previous studies on capital structure of Tanzania SMEs showed mixed results. For example, a study done by (Ibrahim,H.,& Masron,T.A.,, 2011) found that the relationship between firm size and long term debt is significant. In contrast, (Zabri, 2012) found that the relationship between firm size and capital structure is not significant. Furthermore,(Saarani,A.N.,& Shahadan,F., 2013)also reported that size is not significantly related with all debt level but negatively related with total debt ratio and short term debt, and positively related with long term debt ratio. The mixed results showed that the association of size in measuring capital structure is still inconclusive.

Hence, this present study will reexamine this issue in the context of Tanzanian SMEs.

2.2.3 Firm age

(Ahmad, 2015)Investigated the relationship between firm age and capital structure. They found that age is negatively related to all debt ratio measurements. Similarly, (Caneghem, 2012) reported that the relationship between firm age and leverage is negative. Viviani (2008) who conducted a study on capital structure determinants indicated that the relationship between firm age and short term debt is negative.

Those results are in line with POT which postulates that managers normally have a financing decision hierarchy regarding the preference of financing sources. Normally they will use retained earnings before deciding to go for external financing. This implies that companies tend to use less debt since they have been in the industry for a long period of time, implying that the companies are able to accumulate their own fund. Thus, it will reduce the reliance on external debt. In addition, Ezeoha and Botha (2012) argued that the level of debt financing declines as a firm getting older. This is because the older firm may face the problem with asset depreciation, which may erode the company value, and finally affecting the company's growth.

Uyar and Guzelyurt (2015) examined the influence of firm characteristics on capital structure in Turkey and reported that the relationship between firm age and long term debt is negative and significant. They found that firm age is significant to all debt level measurement and the relationship between firm age and debt ratio and long term debt ratio is negative.

Forte et al., (2013) studied the determinants of capital structure of Brazilian SMEs and found that the relationship between firm age and leverage is negative. Thus, a positive relationship between firm age and leverage was proposed by TOT.

According to this theory, an optimal capital structure is achieved when older firm tends to increase levels of debt in order to increase the quality of firm value. Furthermore, older firms can obtain debt easier due to the good relationship they have with lenders as shown by (Chadha ,s., & Shama,A.K., 2016)who conducted an empirical study on capital structure in India. They found that the relationship between firm age and firm value is positive and significant.

The study analyzed the financial ratios of SMEs and the components of debt and found a negative relationship between firm age and leverage.

This finding was supported by Sanusi (2014) and Zare, Farzanfar and Boroumand (2013) who found similar findings. In contrast, several studies competed that firm age have no influence on capital structure. Previous studies by (Abu Mouamer, 2011), (Zabri, 2012) and Zhang (2010) on determinants of capital structure indicated that there is no significant impact of firm age on leverage.

Another study by (Saarani,A.N.,& Shahadan,F., 2013) who investigated the comparison of capital structure between SMEs and large firms in Tanzania found that there is significant and negatively relationship between age and with long term debt ratio. However, (Abdullah, 2011) who investigated Tanzania SMEs' financing pattern, found that the relationship between age and capital structure is not significant. This finding was supported by (Zabri, 2012)who **also** found a similar result.

2.2.4 Assets Structure

Previous researchers have discovered mix findings on the impact of asset structure on leverage.(Abor J. &., 2009)Study on capital structure also found a mixed result. The study found a significant and positive relationship between asset structure and long term debt but negatively related with short term debt. The results were varied based on the type of debt undertaken for each study. However, another study by Ogbulu and Emeni (2012) on the determinants of corporate capital structure in Nigeria found that there is no impact of asset structure on leverage.

On the other hand, some studies found a positive and significantly influence of asset structure on leverage. (Chadha ,s., & Shama,A.K., 2016)Performed an empirical study on capital structure determinants in India. They found that the relationship between asset structure and leverage was positive and statistically significant. Their result also supported previous studies by Sanusi (2014) and (Zabri, 2012) who found similar results. Normally, firms with a lot of tangible assets can obtain financial aid easier as their tangible asset can be used as collateral. This argument is supported by several recent studies that found the relationship between asset tangibility and leverage is positive (Gomez et al., 2014; (Hussain ,S.S.,Hamza,S.,& Miras,H., 2015); (Kariuki, 2014); Memon, Rus andGhazali, 2015; (Muscettola, 2014); Qaderi et al., 2015; Ukaegbu and Oino, 2014).Similarly, other researchers also found similar results (e.g. (Abu Mouamer, 2011); Chiang, Cheng and Lam, 2010; Omran and Pointon, 2009; (Zhang, 2010). Palacin-Sanchez and Ramirez-Herrera (2013) investigated the capital structure ofSMEs and its determinants across regions in Spain. They found that the asset structure is significant to all debt level measurements, and assets structure is positively related with long term debt ratio and negatively related with short term debt ratio. The study is based on small and large firms, as well as listed and unlisted firms. The study found that assets structure has positive relationship with leverage for unlisted firms.

The study analyzed the financial ratios of SMEs and the characteristics of debt and found that assets tangibility has a negative relationship with young SMEs while positively related to old SMEs. The above studies showed that tangible asset plays a crucial role in firm accessibility to increase debt and it also can be used for collateral purposes.

However, the POT proposes that tangibility is negatively related with leverage. This theory states that a firm tends to use less debt if they have high tangible asset, as they prefer internal funding rather than external debt as their last resort. This theory is supported by several studies that found asset tangibility is negatively related with leverage (Bereźnicka, 2013; Masnoon and Saeed, 2014; Psillaki and Daskalakis, 2009; (Saarani,A.N.,& Shahadan,F., 2013).

Dong (2012) conducted an empirical study on capital structure decision in small economy in New Zealand and found that asset structure is negatively related with leverage. Other studies that investigated capital structure determinants also reported similar findings (Al-Ajmi et al., 2009; Amidu, 2007; (Ibrahim,H.,& Masron,T.A.,, 2011); Sheikh and Wang, 2011).

In the case of capital structure in Tanzanian SMEs, some researchers found positive and significant relationship between asset structure and leverage (such as (Zabri, 2012)). Furthermore, (Saarani,A.N.,& Shahadan,F., 2013) found that there is significantly positively relationship between asset structure and long term debt ratio but negatively related with short term debt ratio. However, (Abdullah, 2011) in their study on SMEs and financial patterns in Tanzania found that asset structure have no significant impact on capital structure.

2.2.5 Profitability

Numerous studies have investigated the correlation between leverage and profitability.

In order to explain the relationship between this variable, the use of POT is proposed. This theory recommends that profitability has negative relationship with leverage, where firms with a higher profitability less rely on external debt financing. The firm prefer on internal fund for the first ranking, followed by debt financing and new equity issuance as the last choice. Many recent studies have found profitability have a negative relationship with leverage (Abeywardhana, 2015; (Ahmad, 2015); Amidu, 2007; Gomez et al., 2014; (Hussain ,S.S.,Hamza,S.,& Miras,H., 2015); (Kariuki, 2014);Masnoon and Saeed, 2014; Psillaki and Daskalakis, 2009; Ramjee and Gwatidzo, 2012; Ukaegbu and Oino, 2014).

These studies investigated the capital structure determinants in different countries and reported that profitability is negatively related with capital structure. Furthermore, several studies that investigated the relationship between profitability and capital structure also found negative results (Fareed et al., 2014; Kiong and Lean, 2011; (Nikolaos, 2014); Sheikh and Wang, 2011; Shubita and Alsawalhah, 2012; Thomas, Kiptanui, Chenuos and Biwott, 2014; Velnampy and Niresh, 2012).

An empirical study of capital structure determinants in France SMEs done by (Benkraiem,R.,& Gurau,C. , 2013) showed that the relationship between profitability and short term debt is negative, as well as a study on capital structure that include the zakat environment in Saudi Arabia which showed a similar result (Al-Ajmi et al., 2009)

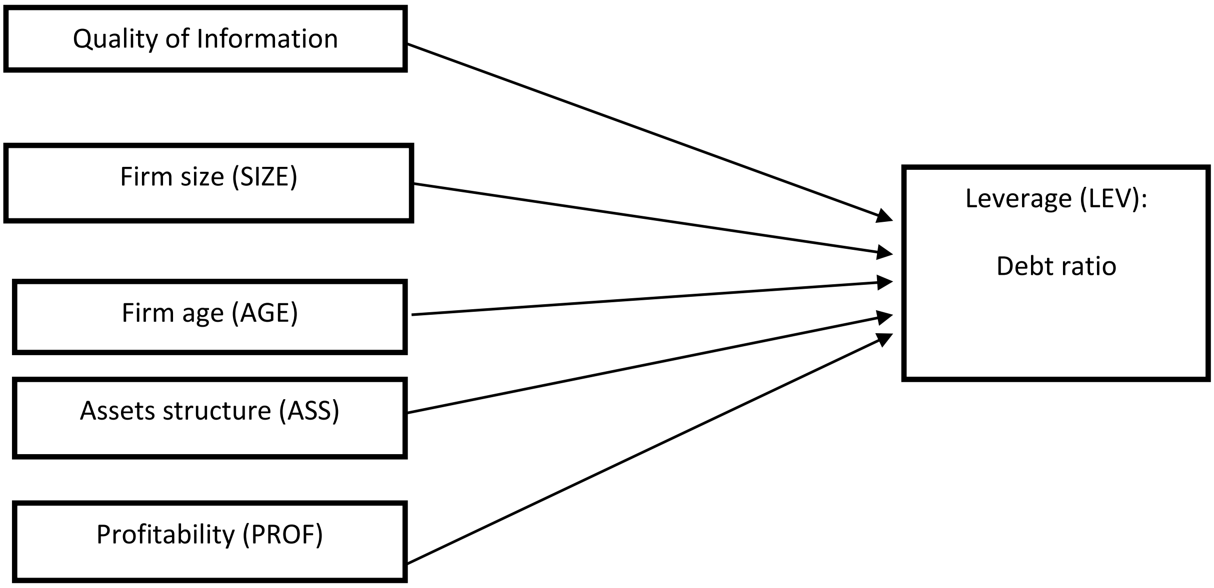
In contrast, the TOT proposes that profitability is positively related to leverage. According to this theory, firms with a higher profitability should increase their level of leverage. This is because the firms are trying to optimize their capital structure by balancing between costs and benefits. Furthermore, Liang, Li and Song, (2014) examined the capital structure in China found that there is positive the relationship between profitability and leverage. This is supported by Sherif andElsayed (2013) and (Zhang, 2010) that reported a similar result. Similarly, (Ibrahim,H.,& Masron,T.A.,, 2011) found a similar result ,(Abor, 2005)examined the impact of capital structure on profitability found a mixed result between ROE and total debt, short term debt and long term debt.

2.2 Research Framework

In this paper research, assumptions are made on how all these variables affect the capital structure .in the figure 2.1 was showed the relationship between the dependent variable and independent variables.

Figure 2.1 Figure of Research Framework

Independent Variables **Dependent Variable**



Source: Researcher Data, 2019

2.3 Definition of Variables

Basically, this study examines two types of variables, namely; one dependent variable and independent variables. This are discussed below;

2.3.1 Dependent Variable

This means a variable which can be change and depend on other variable to stand. Most of the prior studies used total debt, long term debt, short term debt and debt ratio as a proxy to measure leverage of the firm (Abor, 2005);(Ahmad, 2015); (Alipour, 2015); (Benkraiem,R.,& Gurau,C. , 2013); (Ibrahim,H.,& Masron,T.A.,, 2011); Sheikh and Wang, 2011). The dependent variable for this study was measured by using debt ratio. The formula is:

$$\text{Debt Ratio} = \frac{\text{Total Liabilities}}{\text{Total Assets}}$$

2.3.2 Independent Variables

This study used five independent variables, namely quality of information (QUAL), firm size (SIZE), firm age (AGE), asset structure (AS) and profitability (PROF).

These variables were calculated in order to test the hypothesis developed earlier. The information about these variables was taken from firm's annual report for the year.

The quality of information

According to (Caneghem, 2012) Refers to how much publicly available financial information can be accessed by interested user particularly for decision making purpose. Tanzanian SMEs has the option to prepare their financial statement using format of accounting standard (AS). IFRS contains a higher number of accounting standards which require full and detailed information that reports all characteristics of business transactions in preparing financial statement, while PERS contains a lesser number of accounting standards which generally have less detailed information or items in the financial statement.

Firm size

Refers to the speed and growth of business that can expand its activities in the long term period. Firm size can be measured using a number of full time employees, total assets and annual sales. Some studies use total assets (such as (Ibrahim,H.,& Masron,T.A.,, 2011) or natural log of the firm's total assets (Abeywardhana, 2015;(Ahmad, 2015); (Alipour, 2015); (Benkraiem,R.,& Gurau,C. , 2013); (Kariuki, 2014). Some researchers used log of total sales (Abor, 2005); Kiong and Lean, 2011; Sheikh and Wang, 2011). This study used the natural logarithm of total assets for the variable firm size as its measurement.

Firm age

Represents the years of firm's formation or listing in incorporation for a certain period (Ezeoha and Botha, 2012). The proxies used to measure firm's age is either based on firm number of years of establishment from the date of incorporation or from the date of listing in a stock exchange ; Sherif and Elsayed, 2(Ahmad, 2015)013; (Zabri, 2012); (Zhang, 2010). However, this study used the natural.

Assets

Assets can have an impact on the collateral value of debt financing. Collateral value is used as a collective term that refers to the sum of investment in fixed assets, inventories and other intangible assets (Ezeoha and Botha, 2012). In this light, asset structure can be measured by using tangible assets (total fixed assets divided by total assets) (Ahmad, 2015); (Alipour, 2015); (Benkraiem,R.,& Gurau,C. , 2013); Sheikh and Wang, 2011; (Zabri, 2012); (Zhang, 2010). Therefore, in this study, total fixed assets divided by total assets were used to measure asset structure.

Profitability

Profitability can be expressed as the firm's profit or gain that represents the performance of a firm. It is also one of the features that can affect firm's capital structure. There are several measurements of profitability, such as profit margin, return on asset (ROA), the ratio of net profit before taxes to total assets, return on equity (ROE), profit before taxation and etc. The most widely used measurement for profitability is the return on asset (Alipour, 2015); (Benkraiem,R.,& Gurau,C. , 2013); (Ibrahim,H.,& Masron,T.A.,, 2011); (Kariuki, 2014); (Zabri, 2012). As such, return on assets (ROA) was used as the measurement of profitability variable in this study.

2.4 Chapter Summary

This chapter reviews the previous studies on capital structure. First, it explains the theories of capital structure such as MM theory, TOT, POT, agency theory and market timing theory. Second, this chapter investigates the influence of firm characteristics (quality of information, profitability, firm size, asset structure and firm age) on capital structure decisions. Finally, this chapter also summarized the empirical evidence based on capital structure theories.

CHAPTER THREE
RESEARCH METHODOLOGY

3.0 Introduction

According to (Kothari, 2004) defines research methodology as a way to systematically solve the research problems. This chapter introduces the area or place where the study will be conducted and the approach that will be used by the researcher to carry out the study's target population, and data analysis techniques.

This chapter describes the methodological procedures which were adopted in collecting useful information from various sources in order to conduct this research. Since the data collected are secondary in nature, the financial information was obtained from TAZARA. The sources are from printed and electronic bases. Examples of printed information are books, journals and Section 3.1 explains the hypothesis development. Section 3.2 describes the research design. Section 3.3 discusses the measurement of variables. Section 3.4 discusses the data collection method and sampling. Section 3.5 presents the data collection procedures. Section 3.6 represents the techniques of data analysis. Section 3.7 concludes this chapter.

3.1 Hypothesis Development

The study of the association between capital structure and firm specific characteristics leads to the development of five hypotheses as follows:

3.1.1 Quality of information (QUAL)

According to the TOT as proposed by (Myers, 1977), in order to gain an optimal capital structure, firms will raise debt as much as they can. In this study, the quality of information is based on the accounting standard adopted by SMEs. Firms that adopt IFRS are considered as having a higher quality of information because IFRS demands a higher level of disclosure of information. Importantly, regardless of the FS format used, the firm is grateful to provide all information contained in that type of format. Thus, based on the format of the FS filed, one is able to test the impact of information quality on SME financial structure. Although FS capture only one aspect of a firm's disclosure policy, ''financial statements are one of the most important means by which unlisted firms communicate the status of their business to outside stakeholders.'' (Beuselinck et al. 2008, p. 616). The first study to use information quantity and quality as the determinants of leverage was conducted by (Caneghem, 2012). Using Tanzanian SMEs, they found that both the quantity and quality of financial information are positively related to leverage. Their results is in line with TOT which stated that the firm will face the problem of using external funds if their financial statement contain less information and low information quality, or firm with high quality of information relies more heavily on debts. Hence, it is useful to test whether their findings are applicable in the Tanzanian context. Based on the results found from previous empirical studies, a positive relationship between quality of information and leverage is expected.

3.1.2 Firm size (size)

The TOT assumes that bigger firms have a greater debt accessibility and are able to be highly levered, and was less prone to financial distress because of their stable financial sources. Psillaki et al., (2016) pointed that larger firms with higher debt capability are highly levered. Thus, a positive relationship is predicted between firm size and leverage as evidenced from prior studies (Boateng, 2004); Fahmi and Noryati, 2013;Mazila et al., 2013; (Chadha ,s., &Shama,A.K., 2016); Gomez et al., 2014;(Nikolaos, 2014), However, there are researchers, who found a negative relationship between firm size and leverage such as (Alipour, 2015); (Ibrahim,H.,& Masron,T.A.,, 2011); (Kariuki, 2014); Suhaila and Mahmood, 2008). Based on the results found by the majority of empirical studies, a positive relationship between firm size and leverage is expected.

3.1.3 Firm age (AGE)

Firm age can be described as how long an organization has been in operation since their establishment. (Ahmad, 2015)Stated those firms that have been in the industry for a long period tend to use less debt. It means that the firm has an ability to accumulate its internal funds which encourage the firm to reduce its reliance on debt. The firms which prefer to use internal equity as a first choice before seeking to external sources of debt or new equity which is in line with the POT. Thus, firm age is predicted to be negatively related to leverage (Ahmad, 2015); Ari and Mika, 2004; Ogbulu and Emeni, 2012; Uyar and Guzelyurt, 2015). However, a few studies found that firm age were positively related to leverage (Chadha ,s., & Shama,A.K., 2016); Sherif and Elsayed, 2013). Based on the results found by the majority of empirical studies, a negative relationship between firm age and leverage is expected.

3.1.4 Asset Structure (AS)

The other important factors that determine the capital structure is asset structure. Asset structure represents the items contained in the balance sheet which comprises of current assets and fixed assets. Numerous studies used tangibility asset as proxies to measure capital structure (such as (Ibrahim,H.,& Masron,T.A.,, 2011); Qaderi et al., 2015; Sherif and Elsayed, 2013). Gill, Biger, Pai and Bhutani (2009) pointed that firms will use more debt rather than to issue new equity if they have more collateral assets. This was supported by Ezeoha and Botha (2012) who conducted a study about debt financing in South Africa. They found that the higher the proportion of firms' tangible assets, the higher is their reliance on debt. In contrast, Jo˜eveer, (2013) contended that when a firm has low tangible asset it will be more levered.

Therefore, a positive relationship between asset structure and leverage is found (Gomez et al., 2014; (Kariuki, 2014); Memon et al., 2015; (Muscettola, 2014); Qaderi et al., 2015; Sherif and Elsayed, 2013; (Zhang, 2010). However, there are some researchers who found a negative relationship between asset structure and leverage (Amidu, 2007; Bereźnicka, 2013; (Ibrahim,H.,& Masron,T.A.,, 2011); (Nikolaos, 2014); Psillaki and Daskalakis, 2009; Sheikh and Wang, 2011). Based on the results found by the majority of empirical studies, a positive relationship between asset structure and leverage is expected.

3.1.5 Profitability (PROF)

Profitability also plays an important factor that can influence the level of a firm leverage. Kiong and Lean (2011) pointed that a highly profitable firm is expected to reduce its debt. This is in line with POT which states that a firm would prefer to use internal capital source when there is an improved profitability rather than using external capital sources. Hence, there is a negative relationship between profitability and leverage (Abeywardhana, 2015;(Ahmad, 2015); (Benkraiem,R.,&

Gurau,C. , 2013); Gomez et al., 2014; (Hussain ,S.S.,Hamza,S.,& Miras,H., 2015); (Kariuki, 2014);

However, some studies found a positive relationship between profitability and leverage (Chadha ,s., & Shama,A.K., 2016); (Ibrahim,H.,& Masron,T.A.,, 2011); Qaderi et al., 2015; Sherif and Elsayed, 2013; (Zhang, 2010). Based on the results found by the majority of empirical studies, it is expected that there will be a negative relationship between profitability and leverage.

3.2 Research Design

A case study design used in this study since it narrows down a broad field of research into few easily researchable fields. The case study design is much suitable since this type of design involves looking at historical information from SMEs Financial records for past three consecutive years of business operation. TAZARA was the case of the study findings since it might be very complex to conduct the research throughout all the district and municipal of Tanzania because of time and resources constraints. Lamnek (2005) explained that “Case study is a research strategy of an empirical inquiry that investigates a phenomenon within its real life in a single representation from multiple representations.

3.2 .1 Research Approach

This study used quantitative approach since it focuses on impact of capital structure on SMEs. Quantitative approach used because the data that collected were used in computing the frequencies, percentages and tabulations. Referring back from other authors Burns and Groove (2005) defined that “Quantitative research is a formal, objective, systematic process in which numerical data are used to obtain information about the World” also John (2010) has put down some benefits of using Quantitative approach he said “Quantitative research tests a theory which is composed of variables, measuring numbers and analysing statistical procedures in order to determine whether the predictive generations of the theory hold true”.

3.2.2 Research Population

According to Kamuzora J (2oo8) population is defined as totality of the objects under investigation.It is important for the researcher to know the targeted populationhence it will simplify the process of data collection.Likewise ;Best and Kahn,(1986) defined is the target population in a group of unit with one or more characteristics in common that are of interest to the researcher.The targeted study population consisted a total of 10 SMEs registered, from which the researcher drawn the sample for data collection and analysis.

3.3 Measurements of variables

The measurement of variables is summarized as shown in Table 3.1.

Table 3.1 Measurement of Variables

Variables	**Measurements**
Leverage (LEV)	Debt ratio=total liabilities/total assets
Quality of information (QUAL)	IFRS and IAS
Firm size (size)	Natural logarithm of total assets
Firm age (AGE)	Natural logarithm of the number of years since incorporation of the firm
Assets structure (ASS)	Total fixed assets / Total assets
Profitability (PROF)	ROA (Return on Total assets) = EBIT / Total assets

3.4 Data Collection Method and Sampling

3.4.1 Sampling Technique and Sample Size

Sampling is the processs of drawing a sample from a large populatio(kothari ,2004) .A sample is a portion of the larger population tha is studied to represent the whole population of the study (kamuzora J,2008). however the credibility of the data obtained depends not only on the accuracy of analysis and presentation of tha data collected but also on the size of the sample.

3.4.2 Techniques of the Sampling

Sampling techniques is defined as procedure used to select some elements of a population **in** such a waythat they represent the actual characteristics of the total population (Kamuzora,2004).

Simple Random Sampling

This is statistical sampling technique that the researcher found suitable for choosing a representative sample of the chosen population (kamuzora J ,2008).The researcher used this method because it give freedom to the resaercher to pick accurate representative from the targeted population.

3.4.3 Sample Size

A sample size is a smaller group of subjects drawn from the population in which the researcher is interested in gaining informations and drawing conclusion about the universe if randomly is selected (kothari, 1990).By using simple random sampling each element in the identified population have an equal probability of getting into the sample and all choices were independent of one another.The random number table has been used to obtain the sample elements consistence with determined sample size that deemed appropriate for acceptable level of confidence and accuracy.Basing on the sampling techniques employed the expected sample size comprise 10 people the sample size was people bacause a researcher was abe to gether enough information and arrive at conclusion based on the same (Krejecie, 1970).It was also cost effective means of doing this research.

3.5 Data Collection Methods

Data collection methods are instruments which are used to collect data frome the field area where the research takes place (Kamuzora J ,2008) .In this study the researcher used various instruments in the collection of data which are explained below ;

3.5.1 Primary Data

The primary data collection refers to the data collected direct from the field ;it involves questionnaire .The primary data able to get the first handed data (kothari ,2000). The researcher will rely on this type of data because it is the easy way to get views directly from those concerned with the problem under study.The researcher used the following ways / instruments to collect primary data frome the field.

Questionnaires.

(Kothari, 2004) argue that the person who answers the questionnaire might feel in the telling the trust.This was the main reason why the researcher decided to make use of this data collection method .The reasonable number of questionnaire was prepared as the main tool for data collection.The questions were prepared basing on the objectives of the study and the research questions and in a manner that each respondent could easily understand .Moreover,the questions were set to get answers relavant to the study and to simlify the process of analysing and presentation.

3.5.2 Secondary Data

Secondary data are the facts and figures that have already been recorded before the project at hand.On the other hand secondary data are those which have already been collected by someone else and which have already been passed through the statistical process (Kothari, 2004). The researcher collected secondary data through documentary sources.Due the natural of the study ,some especially and relevants from the organisation were used to supplement the information .These included ,management reports and annual performance reports.

3.6 Data Analysis

According to (Kothari, 2004), The researcher analysed data obtained basing on the objectives of the study .Data collectioned were edited,coded,summarised and analysed through statistical package for social science.The ideas to be collected from questionnaire and other data collection techniques will be analysed by researchers knowledge obtained from literature review. Data will be presented in form of descriptions of tables with frequency tables featured correctly ,percentages cross tabulation ,so as to establish the relationship between variables.

CHAPTER FOUR
RESULTS AND DISCUSSION

4.0 Introduction

This chapter presents the analysis ,discussion and presentation of the information or data collected from the field on the research ,In this chapter it includes research questionnaeir are formulated according to objective of the study such as specific objectives as core base of data collection be discovered and discussed ,and presented and analyses using discriptive statistical methods and some are presented in the forms of tables .The finding explained below aree based on the data collected during the field practice ,and which were categories such as details of respondent, questionnaier based on objective of the study as the intension of researcher .The determinant of capital structure evidence from SMEs in Tanzania was determined by using those data methods that employed.

4.1 Demographic Characteristics of Respondents

The characteristics of the respondents were different in work environment in research process such as sex,age,designation ,professinal qualification and level of experience.All respondents in field practical were total of 10 as sample size ,all are employees or staff member.

4.1.1 Sex of the Respondents

The management of the organisation is not only one sex ,so that the respondents concerned in this study were from different sex of female and male.In the management include 3 female and 5 male have been employed in Mufindi SMEs and other 2 male are branch manager and other are members with different level of education and experience.

Table 4. 1 Sex of the Respondent

	Frequency	Percent	Valid Percent	Cumulative Percent
Female	3	30.0	30.0	30.0
Male	7	70.0	70.0	100.0
Total	10	100.0	100.0	

Source; Research work ,2019

From the table above explain that 30% are female and 70% are male ,this show that female are 3employed less compared to male are 7in lending field.

4.1.2 Age of the Respondent

The age of respondent were acknowledging the mature of the employees in performing their duties and responsibilities on his/her respective position in the management.

Table 4. 2 Age of the Respondent

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	20-30 years	2	20.0	20.0	20.0
	31-40 years	4	40.0	40.0	60.0
	above 50 years	4	40.0	40.0	100.0
	Total	10	100.0	100.0	

Source; Research work, 2019

So that the table above describe;20% employee are still youth,and and know exactly what he do,40% also they know their duties and responsibilities and 40% are elders in Tazara kongolo quarry management that supervise the work to be done.

4.1.3 Designation of Repondent

The respondent where differ in designation this means that each respondent has each position to acts its duties in the management operation.Branch manager (superviser) was 1 respondent,senior accountant 1 respondent and assistant accountant 1respondent and clerk accountant 1 respondent and sales clerk 1 respondent and 1 cashier and other 5 respondent are members staff in Tazara kongolo quarry management.From this help a researcher to examine the position of the respondent in the management.

Table 4. 3 Designation of the Respondent

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Branch manager	1	10.0	10.0	10.0
	Senior accountant	1	10.0	10.0	20.0
	Assistant accountant	1	10.0	10.0	30.0
	Clerk accountant	1	10.0	10.0	40.0
	Clerk sales	1	10.0	10.0	50.0
	Other members	4	40.0	40.0	90.0
	Cashier	1	10.0	10.0	100.0
	Total	10	100.0	100.0	

Source; Research work, 2019

4.1.4 Education Level of Respondent

The education was the important category that examines the proffessional of respondent in the Tazara kongolo quarry management and Eucation was categories into four groups such as Certificate,Diploma,Bachelor Degree,and Masters Degree.From my field practical the respondent in 10 ,there were no certificate holder and 1 diploma respondent contribute 10% ,and 5 respondents were Bachelor Degree holder contibute 50% and 4 respondents were Masters Degree holders contributes 40%.In all 10 respondent are proffessional and majority of them have Bachelor Degree most accountant and sales clerk ,But only 1 Advanced diploma and others are staff qualified by Masters degree most are branch manager and senior accountant.In this reasons ,it helpe a researcher to examine the education level of respondent in certain position that has been performed by qualified person.

Table 4. 4 Education Level of the Respondent

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	advanced diploma	1	10.0	10.0	10.0
	bachelor degree	5	50.0	50.0	60.0
	masters degree	4	40.0	40.0	100.0
	Total	10	100.0	100.0	

Source; Research work, 2019

4.1.5 Level of Experience

From the work experince in the quarry management opertion respective position as respondents ,6 employees are more than ten years of work experience contribute 60% and 2 employees are five years work experience contributes 20% and other 2 employees between 6 and 10years work experience also contribute 20%.All employees have intenson to attain the mission and objectives of the quarry and CSP

Table 4.6 Experience Level of Respondent

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	1-5 years	2	20.0	20.0	20.0
	6-10 years	2	20.0	20.0	40.0
	above 10 years	6	60.0	60.0	100.0
	Total	10	100.0	100.0	

Source ;Research work, 2019

4.1.6 Responses from Quastionnaire

After distribute the questionnaire to all respondent within the quarry management ,I believe will be answered accordingly from them.All distributed questionnaire were returned by respondents will indicate 100% in finaly.Whereby ,I ensure that all questionnaire were returned and filled and to avoid the questionnaire returned without filled,This help the researcher in collecting the valid and reliabity of information ,analysis and meeting the research objectives.

Table 4. 5 Response from questionnaire

	Frequency	Percent	Valid Percent	Cumulative Percent
Agree	10	100.0	100.0	100.0

Source; Research work, 2019

4.1.7 Department of the organisation of respondent

Tazara kongolo quarry have many department but the below are the department which help to obtained the information concerned of my research which is conducted my work

Table 4.8 Department of the respondent

		Frequency	Percent	Valid Percent	Cumulative Percent
	Accounting department	4	40.0	44.4	44.4
	Human resource depatment	1	10.0	11.1	55.6
	Marketing department	1	10.0	11.1	66.7
	Procurement and supply department	1	10.0	11.1	77.8
	Administration department	2	20.0	22.2	100.0
	Total	9	90.0	100.0	
Missing		1	10.0		
Total		10	100.0		

Source; Research work,2019

4.2 Research Questionnaire Based on Specific Objectives of the Study

4.2.1 Examine the relatioship between independent variables and firm leverage

Specically the objective of the study was to examine the relationship between independent variables and leverage of the firm.In the process of achieving this objective the question was set and information collected from targeted respondents through questionnaires.The following findings was observed and evaluated by the researcher;

Table 4. 6 Descriptive Analyisis

Dependent and independent variables (n=10 peoples)					
	N	Minimum	Maximum	Mean	Std. Deviation
leverage are the significantly to the smes?	10	1	1	1.00	.000
does quality of information is positively related to firm leverage?	10	1	2	1.40	.516
does firm size is positively related to firm leverage?	10	1	2	1.40	.516
does firm age is negatively related to the firm leverage?	10	1	2	1.30	.483
does assets structure is positively related to firm leverage?	10	1	1	1.00	.000
does profitability is negatively related to firm reverage?	9	1	2	1.22	.441
	9				

Source; Research work, 2019

Note:

Leverage is total liabilities /total assets, quality of information is fake that takes a value of 2 max if a firm use a complete FS (IFRS) and 1 min, firm size is natural logarithm of total assets; firm age is natural logarithm of the number of years since incorporation of the firms; assets structure is tangibility assets (net fixed assets+inventory) /total assets ,and profitability is ROA (return on total assets =EBIT /total assets).

Zikmund et al., (2013) noted that descriptive statistics presents the pattern and general trends of a data set. Table 4.1 presents a summary of descriptive statistics for the all variables employed in the study. It shows the mean, standard deviation, minimum and maximum values. Leverage (LEV), which is the dependent variable shows a mean value of 99%. The maximum level of leverage is 90% and the minimum level is 10%.Shows that some SMEs in my sample (10 peoples)have large retained losses on their balance sheet (i.e. negative equity).

For the independent variables, the mean value for firm size (SIZE) shows the highest mean value of 1.40, with minimum and maximum values of 2 and 1 respectively. Firm age (AGE) is the second highest variable with a mean value of 1.30, with minimum and maximum ages of firm1 and 2, respectively. Profitability (PROF) shows a mean value 1.20, and with minimum and maximum values of 1 and 2, respectively. This finding is consistent with (Benkraiem,R.,& Gurau,C. , 2013) who argued that SMEs with high profitability tend to finance their firm's activities by using their own funds. With respect to asset structure (AS), on average, total assets represent about 56% of total assets, with minimum and maximum values of respectively. The mean value is slightly higher than those reported in previous studies e.g. (Caneghem, 2012); Heyman, Deloof and Ooghe, 2008; Sogorb-Mira, 2005). For the quality of information (QUAL), 31% of the SMEs filed their financial statements using the new accounting standards (MFRS).

Overall, the mean value of leverage was 93%, which indicates that the most important source of fund for Tanzanian SME firms is derived from debt. From this result, the higher leverage (LEV) ratio of Tanzanian SME shows that they rely heavily on debt.

4.3 Summary

After research findings the results show that the firm size and liquidity are significantly affect the debt ratio of SMEs in Tz .On the other hand ,profitability and tangibility are found that insignificant to the debt ratio.

CHAPTER FIVE
CONCLUSION AND RECOMMENDATIONS

5.0 Introduction

This chapter concludes this present study and consists of five sections. Section 5.1 discusses the conclusion of the study, followed by section 5.2 which presents the limitation of the study, while section 5.3 discusses the contribution of the study. Section5.4 provides suggestion for the future research and section 5.5 summarizes the chapter.

5.1 Conclusion

This study provides a picture about the financing behavior of Tanzanian SMEs in choosing the best source of capital to run their business operation. The relevant theories of capital structure, namely the MM theory, TOT, POT, agency theory and the market timing theory were discussed, and empirical evidences were collected by using one dependent variable and five independent variables. Consequently, this study aims to provide a better understanding on the determinants of capital structure of Tanzanian SMEs.

As mentioned in Chapter 1, the objective of the study is to examine the determinants of capital structure of Tanzanian SMEs in the manufacturing industry. The sample used in this study comprised of 1 SMEs firm in Tanzania with the elimination of firms operating in the banks, insurance, services and other financial institutions industries. The study had formulated five hypotheses to be tested.

Overall, the percentage value of leverage was 100%, which indicates that the most important source of capital used by Tanzanian SME firms is derived from debt. This high percentage shows that Tanzanian SMEs relies heavily on debt.

The results shows that, profitability (PROF) and firm size (SIZE) are negatively and significantly related with leverage (LEV) as the dependent variable. On the other hand, three other variables, namely asset structure (AS), quality of information (QUAL) and firm age (AGE) shows no relationship with leverage.

This study indicated that the relationship between profitability (PROF) and leverage (LEV) is significantly negative. In terms of quality of information (QUAL), the study finds that there is a negative but non-significant relationship with leverage. The variable asset structure (AS) also has a negative relationship with leverage, but the relationship is not significant. For firm's size (SIZE), this study finds that there is a significant negative relationship with leverage. Lastly, this study finds a negative and non-significant relationship between firm age (AGE) and leverage.

The Pearson relationship measurement results show that quality of information (QUAL) and firm size (SIZE) are negatively and significantly correlated with leverage (LEV) at the 30 percent level, whereas for asset structure (AS), it is negatively and significantly correlated with leverage (LEV) at the 70 percent level. On the other hand, two other variables, namely, profitability (PROF) and firm age (AGE) shows no correlation with leverage.

Finally, the finding suggests that the traditional capital structure theories such as the TOT and POT are significant in clarifying the capital structure in Tanzanian SMEs. For instance, the relationship showed a positive relationship between firm size and quality of information. The positive association is in line with TOT which proposed a similar correlation. The result therefore supports that larger firms prepare a higher quality of information in preparing their financial statements. Meanwhile, the negative correlation between profitability and leverage is in line with POT which proposed an inverse correlation. It means that high profitability firms will reduce the using of debt and vice versa. The result obtained is also consistent with agency theory, as it shows a positive relationship between asset tangibility and leverage.

Therefore, the study contends that every theory has their own specific explanation for firms' financing behavior. As argued by Myers (2001) there is no single theory that provides a general explanation of firms' financing strategies.

5.2 Limitation of the study

Similar to other empirical studies regarding SME's choice of capital structure, this study also has its own limitations. The first limitation is the generalizability of the results of this study. This study focuses only on one financial year, which may not be sufficient to explain everything about the financing behavior of Tanzanian SMEs.

Second, the number of companies taken as the sample size is limited to the small and medium enterprises, excluding the micro enterprises. Besides, SMEs are not compulsory to publish their financial information like public listed firms. Since SMEs are not obliged to publish their financial statement, then they can choose whether to publish it partially or incomplete information unless they are required to do so. The sample size of this study is limited to only 10 SMEs due to lack of transparency and incomplete data which could lead to an unbalanced dataset. The accessibility of data for SMEs is mainly restricted by two factors: number of firms and history of financial data. The most crucial limitation of SMEs research is the adversities to obtain data.

Third, all the selected firm in this study came from the manufacturing sector. In fact, there are many other sectors such as consumer sector, service, trading and others. Therefore, the results of the study may not be generalized to other sectors. In order to get a clearer picture of SMEs financing choice, a representative sample from each sector may be employed in future research.

5.3 Contribution of the Study

This study theoretically contributes to the existing literature by introducing a new variable, namely the quality of information, which has not been used in prior studies, to examine its impact on capital structure. The findings of this study will shed light on firms' specific variables which might influence financing behavior of Tanzanian SMEs.

Therefore, practically, this study might be useful for the manager who wish to set up a business in Tanzania. Thus, this study will help managers to make a good decision on the proportion of their capital structure. They will also be able to determine the best financing pattern for their company either via equity or debt.

5.4 Suggestion for Future Research

For future research, there are several ways that can be employed by researchers.

Firstly, a bigger sample size should be used. As this study only used 1 SMEs firm as the sample, a bigger sample size is needed in order to generalize the findings and also to avoid biased conclusion. Secondly, this study focused only on Tanzanian SMEs in the manufacturing sector because they serve as the backbone to the country's economic growth. According to Ibrahim and Masron (2011). A study that covers other sectors would provide a more accurate picture of SMEs financing behavior in the Tanzanian context.

5.5 Chapter Summary

This chapter concludes the study by summarizing the major findings, limitation of the study, contribution of the study and suggestion for future research. It is hoped that this study would provide the ways for more research to be conducted for those who want to do a similar topic.

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APPENDICES

QUESTIONNAIRES

Questionnaire to head of sections and staffs

Dear Respondent,

I am David Yosia Simbeye, a master student at Mzumbe University in Mbeya Campus College pursuing a Master of Business Admnistration in corporate Managent . I am currently conducting a field research at Mufindi SMEs. My case study is ‘The factors affecting the Growth of SMEs in Tanzania.’The purpose of this questionnaire is to ask your views on the study and the obtained information is strictly used for academic purpose only and treated with maximum caution and confidentiality.For the study to be successful ,I am kindly requesting you to lend me your time to fill in this questionnaire brought to you.

The aim of this study is to achieve the following specific objectives,

i. To examine the relationship between quality of information and firm leverage.
ii. To examine the relationship between firm size and firm leverage.
iii. To examine the relationship between firm age and firm leverage.
iv. To examine the relationship between profitability of the firm and firm leverage.
v. To examine the relationship between asssets strucrure of the firm and firm leverage.

SECTION A :Respondents details

Please answer the following questions by ticking the relevant response provided down your answer in the space provided.

1. Gender of the respondent.
    a) Male ( )
    b) Female ( )

2. Respondents age
   a) 20-30 years ( )
   b) 31 -40 years ( )
   c) 41 -50 years ( )
   d) 51 and above years ( )
3. What is your education level?
   a) Certificate ( )
   b) Advanced diploma ( )
   c) Bachelor degree ( )
   d) Masters degree ( )
4. In which SMEs are you working with?
   a) Accounting and finance department ( )
   b) Marketing and sales department ( )
   c) Human resource deparment ( )
   d) Production department ( )
   e) Procurement and supply department ( )
5. What is the level of experience?
   a) One -Five years ( )
   b) Six –ten years ( )
   c) Above ten years ( )

Section B : Specific questions

Choose the best answer ,fill the answer and give the reasonsof your answer

6. Are the firm factors of capital structure affects SMEs in Tanzania?
   a) Yes ( )
   b) No

   If yes,explain

   ....

   ....

If no ,explain

....

....

7. There is any relatioship between firm leverage and other factors of capital structure?

   a) Yes ( )

   b) No

   If yes,explain

   ....

   If no,explain

   ....

8. there is the relatioship between factors influencing growth and performance of SMEs?

   a) Yes

   b) No ( )

   If yes ,explain

   ....

   if no ,explain

   ....

9. What is the performance of SMEs in Tanzania?

   ....

10. How long have you been operating your business?

....

11. How much capital injected in your business?

....