# THE EFFECT OF CREDIT FINANCING ON THE FINANCIAL PERFORMANCE OF MEDIUM SCALE ENTERPRISES IN KATWE – BUTEGO DIVISION, MASAKA MUNICIPALITY

A CASE OF SELECTED MEDIUM SCALE ENTERPRISES

BY

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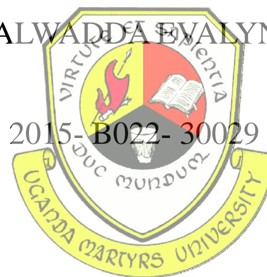


A RESEARCH REPORT SUBMITTED TO THE FACULTY OF BUSINESS ADMINISTRATION AND MANAGEMENT IN PARTIAL FULFILMENT OF THE REQUIREMENTS FOR THE AWARD OF A BACHELORS DEGREE OF BUSINESS ADMINISTRATION AND MANAGEMENT

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## DEDICATION

I Nalwadda Evalyne, with gratefulness dedicate this work to the Almighty God, the source of all wisdom and knowledge for giving me the strength and determination to complete this course despite all the hardships that prevailed.

To my father Mr. Sserwadda Joseph Kayemba (R.I.P), my mother Ms. Naddemera Margret and my guardian Rev. Prof. Kyaligonza Francis for their endless support both morally and financially in addition to their unconditional love and care. May God bless you!

This work is also with delight dedicated to my beautiful sisters; Nabisere Mary and Nakalema Mitchell, and as well to my brothers; Kalema Marvin and Kiweewa Michael who shared the dream of attaining a Bachelor's Degree with me.

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## LIST OF ABBREVIATIONS AND ACRONYMS

**UIA** Uganda Investment Authority

**MSEs** Medium Scale Enterprises

**GDP** Gross Domestic Product

**ADB** African Development Bank

**ROA** Return on Assets

**GOK** Government of Kenya

**ROI** Return on Investments

**BOU** Bank of Uganda

**CBR** Central Bank Rate

**IFC** International Financial Corporation

**IMF** International Monetary Fund

## ABSTRACT

Over the years, medium sized enterprises have been shown as the main driving forces for promoting economic growth in any nation as they encouraged entrepreneurship and wealth creation, alleviated poverty and increased productivity levels in a nation, not only in developed countries but also in developing countries and emerging economies (Sacerdoti, 2005).

The purpose of the research was to examine the effect of credit financing on the financial performance of medium scale enterprises, case of selected medium scale enterprises in Katwe – Butego Division in Masaka Municipality. Credit financing was the independent variable and the dependent variable was financial performance of medium scale enterprises. The study was based on three objectives; to examine the effect of loans on the financial performance of medium scale enterprises, to examine the effect of trade credit on financial performance of medium scale enterprises, to establish the relationship between credit financing and financial performance of medium scale enterprises, and the research questions were formulated from the specific objectives to the study.

The Researcher used a descriptive research design to undertake the study with the help of quantitative approaches. The Researcher had a sample size of 42 respondents and 10 medium enterprises in Katwe – Butego Division that were contacted. The Researcher obtained primary data through field survey as well as secondary data from libraries, journals, text books and unpublished research reports.

The Researcher used only questionnaires for collecting data from the field. Data collected from the field was collected, interpreted and analyzed using Statistical Package for Social Scientists (SPSS) version 16.0 to generate the frequency tables, pie and bar charts for which data analysis and discussions were made.

From the field findings, it was found out that medium scale enterprises use loans, trade credit and bank overdraft in financing their business operations despite the high interest rates and administrative costs attached when acquiring loans and credit supplies from suppliers.

The study therefore, concluded that; the profits made by medium scale enterprises were greatly encroached on by the high interest rate charges on loans and bank overdrafts thus resulted into poor financial performance of such businesses.

Lastly, the Researcher recommended that the central bank should set policies and procedures to prevent barriers that inhibit potential owners and managers of medium scale enterprises from accessing credit facilities from financial and other credit institutions in order create a conducive environment for MSEs' growth and expansion as well as opening up opportunities for jobs thus enhancing economic growth.

# CHAPTER ONE

# GENERAL INTRODUCTION

## 1.0 Introduction

The study dealt with the effect of credit financing on the financial performance of Medium Enterprises. This first chapter entails the background of the study, problem statement, general objective, specific objectives, research questions, scope of the study, and significance of the study, justifications, definition of key terms, conceptual frame work, and conclusion.

## 1.1 Background of the study

### 1.1.1 The historical background

Over the years, medium sized enterprises have been shown as the main driving forces for promoting economic growth in any nation as they encouraged entrepreneurship and wealth creation, alleviated poverty and increased productivity levels in a nation, not only in developed countries but also in developing countries and emerging economies (Sacerdoti, 2005). However, the financial performance of medium- sized enterprises has been deteriorating and majority of them have closed down. This trend of performance could be as a result of their failure to access credit facilities, difficulties in exploiting the technology, insufficient managerial capabilities, low productivity, regulatory burdens in their business environment and failure to keep proper books of accounts (Kihimbo, et al., 2012).

However, limitations in financing medium scale enterprises' operations may seriously limit their financial performance as well as expansion potential when it comes to lack of risk capital and their innovation (Akhtar, 2005).

In developing countries like Uganda, the performance of medium sized enterprises has continued to decline over the years. According to Uganda Investment Authority Report (2008), most medium sized enterprises have collapsed leading to the closure of some of such

enterprises that were providing 40% of the employment in Uganda, other medium businesses were auctioned while some were merged or acquired signifying questionable financial performance. Between 2001 and 2002, the medium enterprises financial performance dropped by 56% (UIA, 2008). These enterprises still experienced various difficulties in improving their financial performance since short term loans, trade credit, long term loans were not well managed in optimizing their performance .This may be as a result of such enterprises not using ideal credit financing sources in their day- to-day transactions and if this problem was not tackled, it would continue to cause financial distress and business failure in the East African markets and in that case Uganda being inclusive.

Most businesses operating in Uganda started informally as a family businesses, formalization of the business only became necessitated by the need to obtain external support services like finances, operating license, opening of business bank accounts and the need to separate the business operations from personal finances (Turyahebwa, etal., 2013).

According to centenary bank Report, 2016, it is emphasized that medium enterprises major objective in Masaka is to promote and enhance development through loans to rural farmers, processors of agricultural produce, small manufacturing entrepreneurs, and small traders in both rural and urban areas. Although, medium sized enterprises have been shown to be the primary engines of economic performance. (Brown, G., etal, 2010), few large scale studies of medium sized enterprises actually document the role that external sources of financing play in the overall financing and financial performance of these businesses.

### 1.1.2 Theoretical background of the study

A number of empirical studies have used the life cycle model as their favored approach to understanding the fiscal behavior of Medium sized enterprises (Phelps, 2007; Nofsinger, and Wang, 2011). In line with these studies, Fatoki, and Asah, (2011) observed that medium

enterprises that have been in business for more than five years have a far better chance of being successful in their credit applications compared to those established for less than five years.

From the credit perspective, experienced entrepreneurs were believed to be better performers than less experienced entrepreneurs. It is therefore, a must to factor experience into the process of appraising the solvency of the medium sized enterprises (Gompers, 2010).In the same regard, Nofsinger, and Wang, (2011) put forward that the experience of entrepreneurs was one factor that explained the difference in credit financing levels available to medium sized enterprises.

Fatoki and Asah (2011) believed that the knowledge of financial services recompenses medium sized enterprises in that they can easily prepare requirements for accessing resources on credit from financial institutions and suppliers of goods and services.

Equally, La Rocca, etal., (2011) established that access to credit finance mainly in European and American markets was influenced by the positive association between the debt ratio and the asset structure. Likewise, Fatoki and Asah (2011), postulated that relatively young medium sized enterprises are characterized by a lower portion of tangible assets in their total assets and therefore, more likely to encounter difficulties in applying for credit facilities because of their incapacity to provide collateral required.

Different theories as given below suggest different approaches entrepreneurs chose and employed by these enterprises at different profitability and growth stages which affect their financial performance.

The first theory that guided the study was the pecking order theory; this was first suggested by Donaldson in 1961 and then modified by Myers Stewart and Majluf Nicolas in 1984. It is

an approach defining the capital structure of a firm as well as how the business goes about the process of making financial decisions.

According to Myers and Majluf (1984), there is no well- defined optimal capital structure. Therefore, management has a preference to choose internal financing in form of owner's equity before external financing in form of trade credit, loans and bank overdrafts. However, this theory was based on the assertion that managers have more information about their firms than investors. This disparity of information is referred to as asymmetric information (Pandey, 2010).

Other things being equal, according to the pecking order theory, because of asymmetric information, managers need to follow a hierarchy to choose sources of finance (Pandey, 2010). The hierarchy gives the first preference to internal financing, and when that is depleted, then managers would have to shift to external financing by issuing a debt to generate funds to run the firm's activities with the aim of achieving better financial performance in the future. However, when it is not sensible to issue any more debt, equity is issued as the last option (Boateng, 2004). Thus the pecking order theory makes predictions about the maturity and priority structure of debt or credit finance and therefore, securities with the lowest information costs should be issued first before the firm issues securities with higher information costs. This suggests that short- term debt should be exhausted before the firm issues long term debt (Pandey, 2010).

The second theory that guided the study was credit rationing theory; this was advanced by Stiglitz and Weiss in 1981 and is relevant to why medium sized businesses have limited access to finance. According to the theory, information asymmetry that characterizes most developing countries results in adverse selection as banks do not possess intricate knowledge about the enterprises. Thus banks, in an attempt to decrease the negative effects of defaulting

customers, usually charge a uniform interest rate to all its customers. However, these interest rates are usually high and discriminate against medium enterprises as they lack collateral and prove to be highly risky businesses to finance (Mwangi, 2011).

### 1.1.3 Conceptual back ground of the study

Two key concepts provide a conceptual frame work for this study that is; crediting financing and financial performance of medium sized enterprises. Financing has been recognized in many business surveys as the most important factor determining the survival and financial performance of medium sized enterprises in both developing and developed countries (Brealey, 2006).

Financing is defined as the act of providing funds for business activities, making purchases or investing (Brealey, 2006).

According to De la Torre, et al., (2009) credit financing is a system of funding in which a business takes delivery on credit inform of trade credit from suppliers, bank overdrafts, long-term loans (repayable in more than a year) and short-term loans (repayable within a year) from both financial and other credit institution.

Githaiga, (2015) defines credit financing as the acquisition of capital or assets from a particular lender or supplier to run a business and repay it back within a specified period of time. Credit financing is aimed at improving the business earnings, recover its costs, benefit the proprietors and retain the surplus.

Srinivas, (2005), defines medium sized enterprises as registered businesses with more than 50 employees that contribute heavily to employment and nation GDP, often having a great difficulty in accessing financial services in many emerging markets and grow in ways linked to the formalization of an economy. They are characterized by decentralization of power to an additional management layer.

According to Odongo, ( 2014), financial performance is described as a measure of a firm's overall financial health over a given period of time and it can also be used to compare with other firms in the same industry that are similar in nature.

According to this research, credit financing means debt financing of a business operations from credit or financial institutions while, medium sized enterprises refer to businesses with total assets of more than 100 million but not exceeding 360 Million. However on the other hand, financial performance means the working capital, assets and profits made by the business in a given period of time.

**1.1.4 Contextual background of the study;**

According to ADB (2012), the major challenge facing many developing countries, especially in Sub Saharan Africa was coming up with suitable development strategies that will capture the financial services' requirement of medium enterprises which constituted about 70% of the business sector in the region. This indication aligned with (Mashenene et al., 2014) and ADB (2012) findings which revealed that in similar fashion elsewhere in the world, medium sized enterprise have been constrained with difficulties to access credit finance from financial institutions such as inadequate collateral, poor financial information systems among others.

The Uganda situation is such that even with the substantial contribution of the medium scale enterprises to Uganda's economy, the potential of such businesses have not been envisaged fully and this is a distress for all the stake holders in the economy (Kamweru, 2011). Consequently, credit financing in form of loans ( short and long term loans), trade credit and bank overdraft has become increasingly important in Uganda and world over as a major strategy in the development agenda for poverty reduction and in the promotion of medium sized enterprises (Odongo, 2014).This process is seen as paramount in amplifying private sector-led growth through supporting the medium scale sector (Odongo, 2014) and thus,

Calice, et al., (2012) recommended that if Uganda was to become competitive through growth of the private sector, it was imperative that more attention is placed on addressing the key limitations to MSEs profitability and competitiveness.

Similarly, in Uganda, although there is a high rate of business startups, Uganda is also among the countries with the highest number of medium scale enterprise that perform poorly and close business before the end of the first year in business (Hlupeko, 2013).

Expectedly, medium sized enterprises in Uganda are presently being faced with many serious difficulties such as shortage of funds and renovating equipment, low productivity, lack of experience in terms of production management and financial management (Turyahebwa, etal., 2013).

The difficulty of meeting the specified collateral requirements by the banks has been cited as a major cause of these financing problems, coupled with misuse of funds to assist medium sized enterprises to grow into sustainable ventures among other challenges (Gompers, 2010). This aims at providing an insight into the credit financing problem for Ugandan medium enterprises and how credit financing can be gainfully utilized profitability and for growth of such enterprises.

### 1.2 Problem statement

World Bank report, (2010) suggested that access to adequate credit for working capital and long-term investment was one of the cited major constraint that medium enterprises faced in their operations in Uganda and other developing countries. The report further observed that medium enterprise loans as a percentage of total bank loans were generally smaller compared to large firms where by approximately 10% of all formal medium enterprises have access to a bank credit line. Credit financing directly affects the performance of such enterprises through

facilitating their financial performance and expansion in order to generate more revenues to cover up operational costs, interest on debt and return on owners' investment (Brealey, 2006).

According to Madole, (2013)some medium sized enterprises with the ability to access credit from financial institutions and trade credits from suppliers have failed to effectively utilize the resources to improve their performance. Therefore, this makes it difficult for them to achieve their financial performance in terms of liquidity, profitability and return on the net assets hence leading to loss of business opportunities and failure to grow in terms of size and financial resources. In Uganda, most medium sized enterprises have had access to credit financing from financial institutions to promote their financial performance but only 10% of them have been successful in terms of performance (Turyahabwe, et al., 2013).

Pandula, (2011) asserted that 90% of the Medium sized enterprises ended up in poor financial state leading to business collapse before celebrating their first anniversary due to lack of entrepreneurial skills, lack of adequate technical and management support services, inadequacy of records and information relating to their operations. This discouraged the credit institutions to offer them credit services thus threatening their profitability, survival and ability to grow.

The Researcher carried out this study simply because many medium sized enterprises continued to close down in their operations and the owners ended up losing such enterprises since they cannot be sustained with their own equity, despite the availability of credit services offered to them by financial institutions and suppliers. Therefore, this enhanced the Researcher's efforts to investigate the effect of credit financing on the financial performance of medium sized enterprises in Katwe- Butego Division, Masaka Municipality.

## 1.3 Objectives of the study

### 1.3.1 General objective of the study

To examine the effect of credit financing on the financial performance of medium scale enterprises in Katwe- Butego Division, Masaka Municipality.

### 1.3.2 Specific objectives of the study

- To examine the effect of loans on the financial performance of medium scale enterprises.
- To examine the effect of trade credit on the financial performance of medium scale enterprises.
- To establish the relationship between credit financing and financial performance of medium scale enterprises.

## 1.4 Research questions

- What is the effect of loans on the financial performance of medium scale enterprises in Katwe- Butego Division?
- What is the effect of trade credit on the financial performance of medium scale enterprises in Katwe- Butego Division?
- What is the relationship between credit financing and financial performance of medium sized enterprises in in Katwe- Butego Division?

## 1.5 Scope of the study

### 1.5.1 Subject scope

The research study focused on the examination of the effect of credit financing on the financial performance of medium sized enterprises in Katwe – Butego Division, Masaka Municipality. In this study, the independent and dependent variables were credit financing and financial performance respectively.

### 1.5.2 Geographical scope

The study was carried out from Katwe- Butego Division in Masaka Municipality. This area was considered because it was within the Researcher's area of location. That is to say; between the location of the university and the area of residence of the Researcher thus being convenient in terms of data collection.

The study focused on medium scale businesses in Katwe- Butego Division, Masaka Municipality in Central Uganda 119Km from the capital city of Uganda.

### 1.5.3 Time scope

The research took a period of one (1) year that is; from June, 2017 to May, 2018. This time was used to prepare the proposal, collect data, analyze it and write a final research report.

## 1.6 Significance of the study

The study is expected to be important to the government of Uganda, academia and other stake holders.

In the academia field, the results of the research might help to contribute to the existing knowledge on the subject and serve as a catalyst by other academicians for further research on innovative ways of financing medium scale enterprises.

It might also be of use as a source of reference to Researchers, academics, policy makers, students and other stake holders interested in financing challenges faced by medium sized businesses.

The research may be of use to medium scale enterprises to seek for better sources of funds that would enhance their financial performance, sustainability and survival.

The research may assist other stakeholders like investors, managers and employees to operate from an informed position when dealing with credit financing in relation to financial performance of medium scale enterprises.

The research might assist policy makers, consultants and advisors to design policies to enhance access to credit by medium scale enterprise so that they could contribute significantly to their financial performance that would result into economic development of respective sectors and the country at large.

### 1.7 Justification of the study.

Uganda is one of the countries with the highest business failure rate. The effect of credit financing to financial performance of medium scale enterprise had generally been undermined and because of that, most medium scale enterprises have failed to operate which has resulted into poor performance of the country's economy (Mwangi, 2011).

This research hopes to bring to the eyes of the policy makers an examination of the effect of credit financing on the financial performance of medium scale enterprises. This might assist policy makers in having a basis for making adjustments where necessary as far as financial or credit institutions and MSEs are concerned.

The research study is also part of the university requirements for the award of a degree in Business Administration and Management of Uganda Martyrs University.

### 1.8 Definitions of key significant terms and concepts

**Financing** is the act of providing funds for business activities, making purchases or investing (Pandey, 2008).

**Credit:** African Development Bank Group, (2012) asserts that this exists as soon as someone acquires goods or services without paying for them at once or by paying for them with someone else's money

**Performance:** According to Githaiga, (2015) performance is defined as the act of executing, accomplishing, fulfilling a given task measured against present standards of accuracy, completeness, cost and speed. Performance is used to indicate the success of the business's condition and compliance.

**Credit financing:** This refers to the acquisition of capital or assets from a particular lender or supplier to run a business and repay it back within a specified period of time. Credit financing is aimed at improving the business earnings, recover its costs, benefit the proprietors and retain the surplus (Githaiga, 2015).

**Financial performance:** This is refers to the evaluation of results of a business's policies and operations in monetary terms (Kiema, et al., 2015; p.444). It measures how well a business or firm can use its assets from its primary mode of business and generate revenues.

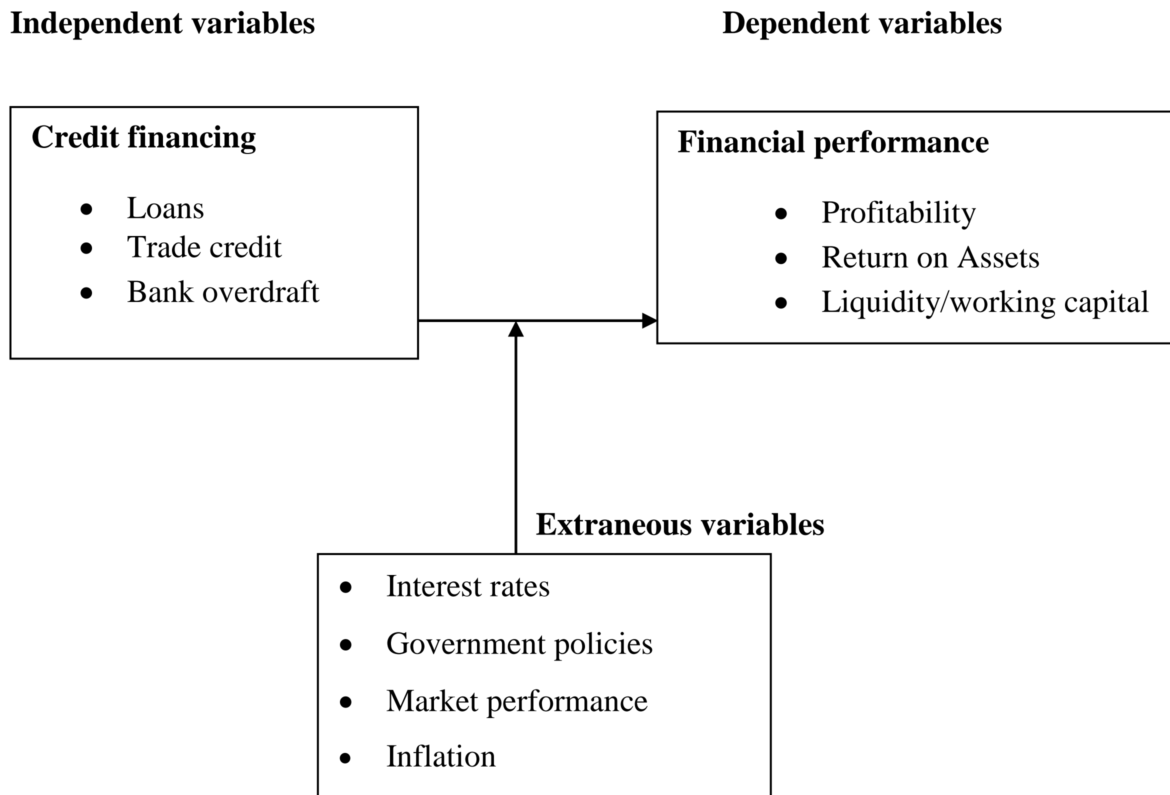
**Medium scale enterprises:** These are defined as such enterprises that employ between 30 and 99employees, with total fixed assets of more than $100million but not exceeding 360million.

**Trade credit:** This refers to providing business customers with time to arrange for the payment of goods they have already received; this period is one of interest free credit, which helps the customer's cash flow at the cost of the suppliers (Barry, et al., 2009).

**Working capital:** Frank, and Goyal., (2003) defines working capital as the difference between total current assets and total current liabilities normalized by total current assets.

## 1.9 The conceptual frame work

**Figure 1: Showing the conceptual frame work.**




**Source:** *Developed and modified by the Researcher after reviewing other related literature.*

From the diagram above, I infer that the study will examine the relationship between credit financing and financial performance of medium sized enterprises.

The conceptual frame work shows credit financing as an independent variable and financial performance of medium scale enterprises as dependent variable. Credit financing can be inform of loans, trade credit and bank overdraft while financial performance of medium sized enterprises was measured by profitability, working capital or liquidity and Return on Assets of a business. However, the dependent and independent variables are affected by the intervening factors which include; interest rates, government policies, market performance and inflation.

### 1.10 Conclusion

In this chapter, the Researcher looked at the back ground and the introductory frame work to the subject under study, general and specific objectives, addressed the problem that the study sought to solve as well as the research questions. Further, the chapter presented the scope of the study, significance of the study and definition of key terms in the study.

# CHAPTER TWO

# LITERATURE REVIEW

## 2.0 Introduction

Literature is designed to identify related research on the topic in order to set the current research project within the conceptual and theoretical context. This chapter presented a comprehensive review of literature on the study under investigation following the objectives of the study in their chronological order.

## 2.1 Theoretical frame work

Capital structure is defined as a firm's mix of debt and equity financing used to finance the business activities (Brealey, etal.,2006).At the earliest development stages, the financing of the medium sized enterprises is significantly dependent on the owners and the persons close to them.

According to Boateng, (2004) a successful medium sized enterprises develop, they soon outgrow sources of internal equity and then graduate to external capital including trade credit, loans and bank overdraft. Therefore, the capital of the business is essential as it forms the foundation of the firm.

Studying the capital structure of medium sized enterprises helps in evaluating existing models of capital structure by focusing on an environment in which many of the modeling assumptions are particularly salient. The theoretical review underlying capital structure can generally be described in terms of the static trade –off theory, the pecking order theory and credit rationing theory, and it must be noted that capital structure theories are not restricted to only those three.

### 2.1.1 The static trade-off theory

According to Andree, and Kallberg, (2008) the origin of modern capital structure theory lies in the work of Modigliani, F., and Miller, M. (1958), in their proposition which was often referred to as the "irrelevance theorem". The theorem suggests that as an implication of equilibrium in perfect capital markets, the choice of capital structure or financing decision does not affect a firm's perfect market value. However, According to Modigliani, and Miller, (1963) it is shown that the effect of personal tax on interest income reduces the attractiveness of the debt on the capital structure and expected return of the firm's shares. Firms through reduction in the interest rate of debt, could easily shift payments from going to the government and instead direct them to the firm's shareholders and creditors by increasing leverage (Pandey, 2010). The tax deductible effect of interest on debt creates tax savings for the firm and makes credit financing cheaper than equity financing. They also suggested that a firm should have 100% credit in its capital structure to enables the firm to take absolute advantage of the tax shield.

However, Hart, (1995) argued that theoretically, 100% tax shield does not exist in reality because of the interest repayment obligations of debt. Debt leads to legal obligations to pay interest and principal to debt- holders.

According to Pandey, (2008) it is argued that if a firm cannot meet its debt obligations, then it is forced into a financial distress. Pandey, (2008) continued to argue that if the firm is in a situation of financial distress, its suppliers may discontinue from granting goods and services on credit due to fearing of liquidation and liquidity problems that are associated by a financially distressed firm, the inability of investors to raise funds to undertake profitable investments and the tendency of managers to expropriate the firm's resources in form of perquisites and avoid risk which makes them start making decisions aimed at short- term rather than long term interests of the firm. Therefore, financial distress is taken to reduce the

value of the firm thus leading to poor financial performance of business activities (Brealey, etal., 2006).

### 2.1.2 The pecking order theory

The theory was first suggested by Donaldson in 1961 and it was modified by Myers Stewart and Majluf Nicolas in 1984. It is an approach defining the capital structure of a firm as well as how the business goes about the process of making financial decisions.

According to Myers, and Majluf, (1984), there is no well- defined optimal capital structure and therefore, management has a preference to choose internal financing before external financing. However, this theory is based on the assertion that managers have more information about their firms than investors. This disparity of information is referred to as asymmetric information (Pandey, 2010). Other things being equal, according to this theory, because of asymmetric information, managers will follow a hierarchy to choose sources of finance. The hierarchy gives the first preference to internal financing, and when that is depleted, then managers would have to shift to external financing by issuing a debt to generate funds to run the firm's activities with the aim of achieving better financial performance in the future and when it is not sensible to issue any more debt, equity is issued as the last option (Boateng, 2004). The theory also makes predictions about the maturity and priority structure of debt or credit finance and therefore, securities with the lowest information costs should be issued first before the firm issues securities with higher information costs, this suggests that short- term debt should be exhausted before the firm issues long term debt (Frank, and Goyal., 2003).

### 2.1.3Credit rationing theory

The theory was advanced by Stiglitz and Weiss (1981).It is relevant to why medium sized businesses have limited access to finance. According to the theory, information asymmetry

that characterizes most developing countries like Uganda inclusive results in adverse selection as banks do not possess intricate knowledge about the enterprises. Thus banks, in an attempt to decrease the negative effects of defaulting customers, they usually charge a uniform interest rate which they are willing to pay as screening device to all its borrower classes. However, these interest rates are usually high and discriminate against medium enterprises from accessing credit facilities as they lack collateral and also prove to be highly risky businesses to finance (Mwangi, 2011).

Due to the effect of interest rates on credit rationing, the risky borrowers are usually willing to pay a higher interest rates than safe borrowers.

On the other hand, risky projects are more likely to fail than safe projects which in the long run reduce the bank's profitability and the performance of medium sized businesses (Glen, 2005). Therefore, there will be credit rationing in credit markets where among loan applicants, some receive and others are denied at any interest rate.

## 2.2 Actual Review

In this review, the research attempted to bring out the key issues and the underlying credit financing and the financial performance of Medium scale enterprises as put forward by the different authors on the variables under study objective by objective.

### 2.2.1 Credit financing of medium sized enterprises

Credit financing for medium sized enterprises in developing countries like Uganda is mainly limited to the bank loans, bank overdrafts and trade credits from financial or credit institutions and suppliers of goods and services respectively (Tirole, 2006).However, Feakins, (2005) pointed out that Overdrafts and term loans are the major products offered by financial institutions to medium sized enterprises.

According to Abdulsaleh and Worthington (2013), financial institutions are principle sources of debt finance for new medium sized enterprises as they offer a wide range of services in their own right or through wholly or partial owned subsidiaries. These services cover every aspect of the financial market such as overdraft facilities, short and long-term loans, trade bill financing, and government loan guarantee schemes. Financial institutions are in better position to gather information on the medium sized businesses through established relationships which they and their staff have with medium scale enterprises and their owners.

Pandula, (2011) asserted that medium sized enterprises who are members of SME representative societies or enterprises such as the Chamber of Commerce have a high probability of accessing credit from lending institutions. These societies have close contacts and relationships with medium business owners or managers and are aware of the problems and needs of their members. (Pandula, 2011). Therefore, these societies and other business associations have played a key role in assisting their members to access loans from financial institutions. However, lack of entrepreneurial skills, inadequacy of records and information relating to business operations hinder these firms from accessing credit facilities from financial institutions thus leading to poor financial performance results of such enterprises (Turyahebwa, et al., 2013).

### 2.2.2 Financial performance of medium scale enterprises

Information on financial performance is useful in predicting the capacity of an enterprise (Levasseur, 2002).

According to Githaiga, (2015) performance refers to the act of executing, accomplishing, fulfilling a given task measured against present standards of accuracy, completeness, cost and speed. Performance is used to indicate the success of the firm's conditions and compliance

and on the other hand, Mwangi, (2016) asserts that financial performance is the evaluation of results of the firm's policies and operations in monetary terms.

Financial performance measures how well a firm can use its current assets from its primary mode of the business and generate revenues for the business (Baxter, 2007).

Performance measures play a critical role not only in evaluating the current performance of a firm but also in achieving high financial performance and growth in the future (Mwangi, 2016). Performance measurement provides useful information related to flow of funds, the use of funds and effectiveness and efficiency of the firm, it can as well be used to motivate managers to make the best and informed financing decision.

Financial measures are for the purposes of helping an enterprise analyze its activities from a financial point of view and to provide information that would be useful in the making of good management decisions. In addition, the financial measures do not provide answers themselves but instead they need to be reviewed in relation to each other and to the other firms across the same industry or to compare sectors in aggregation to enable a business make decisions on how it can improve on the prevailing situation or sustain a desirable position of the business (Mazzarol, and Clark, 2015).

Vijfvinkel, (2011) noted that financial performance analysis identifies the financial strengths and weaknesses of the firm by properly establishing the relationships between the items of the statement of the financial position and profit and loss and other comprehensive incomes account. It is important to maintain a balance relationship between profitability and the liquidity of the firm in order to have a health financial performance. Therefore, one objective should not be achieved at the expense of the other because both have their own importance to the firm.

According to Mwangi, (2016) a firm's financial performance is an essential measure to management as it is an outcome which has been achieved by an individual or a group of individuals in an organization related to its authority and responsibility, not against the law, and conforming to morale and ethics. Such performance is the function of the ability of an organization to gain and manage the economic resources in several different ways to develop competitive advantage (Abdulsaleh, and Worthington, 2013).

According to Beck, (2008a) a statement of financial performance is an accounting summary that details a business's revenues, expenses and net income. On addition, the scholar goes on to say that, "a statement of financial performance is also referred to as a statement of profit and loss or statement of income which an enterprise may prepare on a monthly, quarterly or annual basis".

Financial performance measurement can be one of the biggest challenges faced by businesses in the medium businesses sector, especially with regard to their survival if management is not trained on how to manage finances and measure performance. Performance measures are the life blood of any organization since without them, no financial decisions can be made (World Bank, 2014). However, according to Myers, and Brealey, (2003) performance measurement can be split into financial and non-financial measures but the study was much focused on financial performance measurements which generally look at the firm's financial ratios which are derived from their financial statements such as liquidity ratio, profitability ratios, and debt ratios among others.

Financial ratio analysis was defined by (Pelham, 2000) as a general technique based on some relatively standard methods used to analyze information, and developed by people who make judgments about businesses by reading their financial statement. He additionally argued that

enterprises measure their financial performance differently, but financial ratio analysis is the traditional approach to analyzing and interpreting the financial position of an enterprises.

The recommended financial measures for financial analysis in order to determine a firm's financial performance are grouped into five broad categories namely; liquidity, solvency. Profitability, repayment capacity and financial efficiency (Turyahebwa, et al., 2013) and they are extracted from the accounts of the firm.

Odongo,(2014) argued that financial performance analysis and interpretation of financial statements under takes full diagnosis of profitability performance, liquidity performance, fixed assets performance and funds flow performance. The scholar as well asserted that high financial performance reflects management effectiveness and efficiency in making use of the firm's available resources (Odongo, 2014).

The common financial indicators of financial performance include; sales growth, return on investment (ROI), return on sales (ROS), return on equity (ROE),liquidity, operational efficiency and earnings per share. (Carton, 2004).However, Khalifa, and Shafii, (2013) urged that financial measures can also be referred to as objective measures because they can be individually measured and verified by the business managers.

For the case of this research, financial performance is narrowed down to only three financial measures which are; Return on Assets, profitability, and liquidity as below;

**Return on Assets** (ROA).According to Brealey, et al., (2006) it is suggested that the ROA is often used by managers to measure the financial performance of the firm by the ratio of income to total Assets where income is usually defined as earnings before interest but after taxes.

ROA also indicates the management ability to perform their job efficiently since it shows the ability to generate profits from the Bank's assets. From its formula point of view, it measures net income after tax for each shilling invested in the assets of a bank. Basically, the higher the ROA, the better the financial performance of the firm and vice- versa (Brealey, 2008).

**ROA** =Net Income after Tax ÷Total Assets.

Frank, and Goyal, (2003) asserted that return on assets must be positive and the standard figure for return on assets is 10% - 12%. The higher the ROA the better because the business is earning more money on the capital invested thus ROA takes into consideration the return on investment (ROI) and indicates the effectiveness in generating profits with its available assets.

**Liquidity**. Brealey, (2003) defined liquidity as the ability of a firm to meet its financial obligations when they fall due in a timely manner. In essence, the assets owned by a company are liquid if they can quickly and cheaply be converted to cash (Brealey, 2003). The critical performance issue relative to liquidity is whether the enterprise has developed enough and readily accesses capital to continue to operate.

Accordingly, liquidity measures represent one aspect of a dimension of overall financial performance, and it can be measured in both absolute and percentage terms. An example of an absolute measure of an entity liquidity is working capital, or the excess of current assets over current liabilities and that of percentage measures of liquidity include; change in the working capital, current ratio, and quick ratio ( Glen, 2005).

The objective of business owners and managers is to conceive a strategy of managing their obligations as they fall due and also to increase profitability and shareholders' value (Priya, (2013).

However, Kiaritha,(2015) argued that poor management of liquidity in terms of solvency, operating efficiency is imputable to inadequate financial performances and deters the firm's payments to creditors which is harmful to the enterprise thus resulting into several consequences such as worse credit terms in future, which in the long run adversely affects the firm's profitability (Garcai- Teruel, andMartniez-Solano, 2014).

**Profitabilit**y. According to Mwangi, (2016) profitability is defined as a continuous increase in the financial profit after all expenses have been paid over a given period of time. The more the corporate profitability, the more profits a firm gets from the production and operations, and the more the firm being in better position to guarantee of debt due for repayment.

Garcai- Teruel, and Martniez-Solano, (2014) argued that the amount of profits can be a good an objective measure of financial performance as well as a promise for the company to remain a going concern in the world of business. This is because it shows the firm's continuous improvement in its operations.

### 2.2.3 Loans and financial performance of medium scale enterprises

According to Myers, and Brealey, (2003) a loan is got through borrowing from financial institutions inform of a bank loan and it is usually for a set period of time. (Brealey, 2003), continued to argue that loans can be short-term, medium term or long term. The loan can either be repaid in installments over time or at the end of the loan repayment period.

The bank normally charges an interest rate on loans which can be fixed or variable and in this case, the bank always demands collateral to provide security if the loan can't be repaid (Boateng, 2004). However, during the process such enterprises find a lot of difficulty in obtaining commercial bank financing especially long term loans for a number of reasons, including lack of collateral, difficulties in providing credit worthiness, inadequate credit history and under developed bank- borrower relationships (IFC, 2009).

According to Githaiga, (2015) it is concurred that a short term loan is from overnight to less than one year which makes medium enterprises not to perform well in their operations because of big installment payments to be remitted back to financial institutions in the shortest time like weekly, fortnight and monthly payment since the loan grows bigger in a given time with high interest rates charges. However, the loan period of lending to medium enterprises can contribute to positive financial performance and enhances such business operations and expansion to its survival and productivity in achieving its goals and objectives in the short period. On contrary, research has shown that such enterprises can perform well in the shorter period as well as they are able to maintain their financial records in order to ascertain their financial credit worth (Vijvinkel, 2011).

The short term loan is given to the enterprise known to the bank for a period of four years and below and it is argued that short term financing is positively correlated with firm's growth opportunities (Moro, 2009).

Short term loan is the best financing tool because it is perceived to be cheaper thus both entrepreneurs and financial institutions prefer such loans and does not require security but rather the firm's reputation (Ebaid, 2013). However, it is argued that the short term loans are not conducive to generate productivity while long-term loans may lead to improvements in productivity thus leading to business profitability and growth (World Bank, 2014).

Short-term loans depict conflicting effects on medium enterprises' financial performance that is positive, negative and has no relationship at all as measured by gross profit margin and return on assets (Ebaid, 2013). Long term loans limit managerial discretion by making access to new funds and over investment less likely, a feature that would enhance the firm's profitability (Moro, 2009).

Pelham, (2000) urged that in practice long term investments which are as result of long term loans are supported by proper utilization of the long term loan to generating sufficient profits

to repay loans, cover all costs and distribute the surplus accordingly. Therefore, medium sized enterprises' over dependence on the long term loan hampers business owners from re-occupying the capital invested, increases finance costs and the chances of bankruptcy are imminent (Turyahebwa, 2013).

Empirical evidence suggests that borrowers of medium sized businesses who take loans from more than one financial institution find it difficult to separate their personal finances from those related to their business which leads to default on their loans repayment, and this drops to 50% for households with membership in three or more financial institutions (Glen, 2005). This is because of the small loan size borrowed from one bank which create management problems to the detriment of their businesses.

Amirkhani, and Fard, (2009) argued that medium sized enterprises are overstrained in their repayment capacity by several loans, poor capacity to pay, inadequate income generation, and unwillingness to pay and utilizing for repayment of old loans. This has related effect on the working capital of the business as they tend to have poor business performance and later disrupt the management capacity of business owners. Regarding the borrowers stress from the loans, this hinders the financial performance of medium sized businesses thus leading to non- performing loans and diversion of the loans borrowed for a different purposes (Roodman, 2009).

Medium sized activities are short term in nature and financial assistance acquired to meet business operational needs in the short period leads to low wealth accumulation and financial performance of such enterprises. However, research showed that the rate of poor financial health state and failure of business in Uganda is one of the highest in the world. This is because most medium businesses collapse even before celebrating their fifth anniversary, (Ebaid, 2013).

Beck, et al.,(2008a)urged that despite the importance of medium businesses for the job creation and production, most of the medium sized enterprises literature points to the fact that such enterprises face higher barriers to external financing than large firms which limits their growth and development. However numerous studies that use firm- level survey data demonstrate that access to finance and cost of credit don't only pose barriers to medium businesses financing but, also constrain SMEs as a whole more than large firms.

Most medium enterprises rely on internal financing or short term credit from suppliers and some specialized financial products, often involving fresh capital injections from shareholders although in many cases medium enterprises tend to recur to long term financing from financial institution mainly in the form of outright loans from banks and some hire purchase and leasing products. While on the other hand, some use more of the short term loans to financing their day to day operations (Abor, 2007).

It is argued that many new ventures found out that credit financing is necessary. Short term borrowing is often required for working capital and is repaid out of the proceeds from sales while long-term loans of 1-5 years is used to finance the purchase of property with the purchased asset serving as the collateral for the loans (World bank, 2014), however, it is also said that the most common source of credit financing are the commercial banks and other financial credit institutions.

Bank of Uganda (BoU) official said that the reduction of the Central Bank Rate should further boost economic activity as inflation figures remain subdued. The easing of the CBR is a signal to the commercial banks to reduce interest charged on loans in order to ease the monetary policy to further boost the private sector credit growth and strengthen the economic growth momentum of the country (Sekanjako, 2018).

The governor of BoU stressed that the percentage of non- performing loans has declined to 5.6% from 10.5% which thus encouraging banks and other financial institutions to lend more

to the private sector which included medium sized businesses in Uganda. Additionally, the Governor also noted that shilling loans grew by 10.8% in December 2017, up from a decline of 21.1% in December 2016 .This indicated that improving the global economic outlook could result in better performance and prices for Uganda's exports Also noting that expensive credit to medium sized enterprises and the risk of the government crowding out the private sector in the loan market could derail growth as well as financial performance projections of the firms(Sekanjako, 2018).

Furthermore, Boateng, (2004), argued that many of the financial problems plaguing medium sized enterprises are avoidable, provided entrepreneurs analyze their own businesses funding needs objectively and with sufficient lead time to act decisively. It is also important that entrepreneurs use some personal funds for investment as the initial capital before approaching a bank for their financing needs. This is because financing institutions generally require a certain amount of the owner's investment to show that you as entrepreneurs are committed to the business and motivated to achieve success. This could be possible but however, Falkena et al, (2014) asserted that entrepreneurs in developing countries like Uganda are hit hard by poverty and lack of collateral which is coupled by their weaknesses in operational and management information systems, poor internal controls, limited access to technical assistance, difficulty in employing competent people with techniques in financial management because of the salaries such people would demand thus resulting into poor financial performance of such businesses.

### 2.2.4 Trade credit and financial performance of medium scale enterprises

Trade credit is regarded as one of the most important financial approaches for medium sized enterprises. Trade credit is defined as "a loan that is tied in both timing and value to the exchange of goods" (Yang, 2011). In other words, suppliers allow their customers to delay

their payments within the stipulated period of time thus allowing payments to occur after the receipt of the goods and services. This therefore, helps the business to better manage their short-term cash flows.

According to Mateut, (2005), trade credit can be analyzed on two different perspectives that is; firms can offer trade credits to their buyers in terms of accounts receivable in the statement of financial position and firms can also acquire trade credits from their suppliers in terms of accounts payable as well.

According to a survey by the IMF (2009), about 60% of all international trade transactions are financed via trade credits. Trade credits are extended bilaterally between firms and exist in form of supplier credits which are granted from the seller of a good to the buyer such that the buyer can delay the payment of the purchasing price for a certain period of time. However, on the other hand, cash-in-advance refers to payments made in advance by the buyer of a good to the seller.

The intensive use of inter-firm financing is surprising given that financial intermediaries such as banks are supposed to be more efficient in providing credits to firms inform of loans or overdrafts (Githaiga, 2015).

As a regular component of the market transaction and short-term finance, trade credit shows a great influence on business development and it represents about 35% of total assets in non-financial medium sized enterprises. Medium sized enterprises use trade credit as certain investment to improve firm's value and profitability (Garcai-Teruel and Martniez-Solano, 2014) thus if the owners of medium businesses understand the relationship between trade credit and profitability, it would significantly promote the business development and financial performance of their firms.

Correspondingly, trade credit can also be considered as a switching barrier. Buyers may lose access to short-term finance if they want to change suppliers. This is because suppliers only offer trade credit to those whom they have established mature understanding with (Hermes, et al., 2011) and as a result, suppliers are tied with customers in a stable commercial relationship via trade credit. However, the emerging of trade credit is accompanied with several detrimental effects for suppliers as they would pay more administrative costs such as default debts, screening and monitoring costs among others (Hill, et al, 2012).

Therefore, each time suppliers should keep eyes on the financial condition of the buyers, and this requires both direct money costs and human resource costs. When these costs exceed the benefit from revenue growth, suppliers are unlikely to offer trade credit to their customers (Hill, et al, 2012).

At the same time, trade credit increases the interconnectedness of businesses and potentially increases the risk that payment difficulties faced by one firm may spread more broadly throughout the business sector (Fisman, and Love, 2003).

Firms also use trade credit to boost sales simultaneously. Meltzer, (1960) recommends that firms use trade credit instead of direct price reduction to increase sales especially during periods of tight money. This implies that when firms' sales are sensitive to the demand fluctuations, trade credit is an especially important method to stimulate customers to acquire merchandises in a period of low demand.

Katrien, et al, (2012) argued that trade credit is used as an evaluation tool as well for customers to analyze quality of product when he claimed that prolonging payments grant buyers to verify quality of product. Buyers can refuse the payments if products have quality problems, which result in lower transaction costs thus forcing buyers to make purchasing

decisions according to credit terms and other conditions of trade credit as may be usually specified by a trade credit contract (Curiat, 2007).

Furthermore, according to Tirole, (2006), trade credit can be used as price discrimination between cash and credit customer as well. This will be advantageous whenever the elasticity of demand of cash customers exceeds that of credit customers thus helping firms in solving financial frictions and decreases the operational costs.

### 2.2.5 Bank overdraft and financial performance of medium sized enterprises

According to Glen, (2005) a bank overdraft is defined as a temporary credit facility extended by a bank to corporates and other clients to withdraw funds from their current accounts in excess of the balance. The scholar continued to argue that a bank overdraft facility is provided by the bank at a fee to a customer whenever he needs the funds. The interest is also charged on the excess amount that is withdrawn for the length of the time and as well the overdraft interest can also be deducted from income to determine the profits to be subjected to tax (Glen, 2005).

Glen, (2005) argued that a bank overdraft facility is totally different from the normal given loans when he argued that a loan can be given to both a savings and current holder account while an overdraft is only advanced to a current account holder with an active current account in that given financial institution thus making it unique from bank loans.

The bank overdraft facility is the most important short term form of financing and its balance is not normally included in calculations of the business financial gearing as it is done to normal loans (Brealey, et al., 2006). It is also usually needed for medium businesses to run their day to day operations including; payment of wages to employees, inventory ordering and supplies among others. This is because the daily debit balance interest charges and the absence of penalty for early repayment means that this form of finance can be

cheaper than a loan, thus this strongly and significantly influence credit availability (Abdulsaleh and Worthington, 2013).

An overdraft facility allows the current account holder to withdraw money from the account despite having no balance. However, Calice, et al., (2012) asserts that there is usually a limit on the amount that can be overdrawn from the current holder's account and this is usually set by the bank basing on the amount of working capital, creditworthiness, security offered and the bargaining position of the borrower. However, large and well- established borrowers with low gearing and plenty of collateral can borrow an overdraft at much more advantageous rates (Glen, 2005).

Commercial banks and other credit institutions have traditionally looked at the medium sized enterprise sector with caution and as a result, there are usually no separate medium business lending policies thus also making the loan requests being handled quite stringent (Turyahebwa t al., 2013).

Some credit institutions only give cash-secured overdrafts to enterprises for a maximum of a six-months period and after which the transaction can be renewed, pending revision (Calice, et al., 2012).This type of an overdraft can be secured by the borrower who is a current account holder upon presentation of fixed deposit or treasury bills and a maximum of 95% of their value is granted with a lien placed them to minimize the risk of default.

According to Gompers, et al., (2010) the amount of an overdraft depends on the cash flows or working capital of the business, the timing of receipts and payments, seasonal trends in the sales among others. If the business finds that an overdraft facility appears to becoming a long-term feature of the business, the bank may suggest converting the overdraft into a

medium-term loan. This is because the bank overdraft facility can be renewed each time the bank comes in to review it.

### 2.2.6 The relationship between credit financing and financial performance of medium sized enterprises

Financing is considered as the life blood of any business enterprise and no enterprise, no matter how well managed can survive without enough funds for working capital, fixed assets investment, employment of skilled employees, development of markets and new products. In this regard, the availability of finance is positively associated with productivity and growth (Beck et al, 2008a).

According to Githaiga, (2015) credit financing is defined as the acquisition of capital or assets from a particular lender or supplier to run a business and repay it back within a specified period of time. Credit financing is aimed at improving the business earnings, recover its costs, benefits the proprietors and retain the surplus whereas on the other hand, financial performance is the evaluation of results of a business's policies and operations in monetary terms (Kiema, et al., 2015; p.444). Financial performance measures how well a business or firm can use its available assets from its primary mode of business and generate the necessary revenues.

Credit financing is a credible and effective instrument for poverty alleviation and as such its contribution to economic growth and financial performance of medium scale enterprises (Hlupeko, 2013). Financing medium scale enterprises has attracted much attention in recent years and these enterprises have been considered as vital instruments for the alleviation of poverty in society (Srinivas, 2015). Therefore, medium scale enterprises play a crucial role in nation building, and providing them with the needed facilities that would assist in bridging the gap between the rich and the poor (Glen, 2005).

Lack of access to credit financing may in one way or the other deter the financial performance and development of medium enterprises simply because the proprietors may lack the ability to acquire sufficient funds in order to finance their business activities (Badagawa, 2000).Such phenomenon is most prevalent in areas where there are no sufficient bank outlets as compared to other businessmen in urban centers. The scholar also urged that, even the few financial institutions that are available impose high interest rates on their loans hence affecting the proper functioning and proper performance of these medium enterprises.

Proper management of credits lead to growth and smooth operations of businesses and improper management of credits will not only cripple the ability of commercial banks and other lending institutions to offer credit facilities to such businesses but instead it will threaten their profitability and survival (UIA Report, 2008).

Ross, et al., (2008) argued that once a firm or financial institution decides to grant credit to its customers, it must then establish guidelines for determining who will and will not be allowed to buy goods on credit. They continue to argue that credit analysis involves two steps that is; gathering relevant information and determining creditworthiness. These steps are important simply because potential losses on receivables can be substantial in determining the financial performance of an enterprise.

According to World Bank (2014), medium sized enterprises need financing for two basic purposes that is; financing the production cycle once it has stabilized and financing capital expenditures to expand the current business and create new ones in order to boost the business profitability in the long run of the business going concern.

The two basic forms of financing for medium sized enterprises are internal and external financing. The basic internal sources of finance are the retained earnings from a business obtained in previous years and fresh capital injections by the owners of such enterprises and

on the other hand, external financing can be provided by financial institutions, suppliers and other types of creditors (Ross, et al., 2008).This is in agreement with Myers, and Majluf, (1984) pecking order theory that suggests; there is no well- defined optimal capital structure. Therefore, management has a preference to choose internal financing before external financing. However, the theory was based on the assertion that managers have more information about their firms than investors. This disparity of information is referred to as asymmetric information (Pandey, 2010). According to the theory, because of asymmetric information, managers have to follow a hierarchy to choose sources of finance. The hierarchy gives the first preference to internal financing, and when that is depleted, they shift to external financing by issuing debt or credit to generate funds to run the firm's activities with an aim of achieving better financial performance in the future.

Maritala, (2012), examined the optimal level of capital structure which enables a firm to increase its financial performance and during the study the scholar found out that there is a negative relationship between the firm's debt ratio and financial performance measured by return on assets and return on equity of the business.

According to Feakins, ( 2005) it is found out that medium enterprises in Uganda that participate in business associations have better access to bank loans and other credit facilities. In addition, membership to associations is important for medium sized businesses as they facilitate access to financial services. Thus institutions like such associations, which support the medium enterprises capacity to access financial services become an important avenue for strengthening their financial performance during the business existence in operations.

The accessibility to credit affects financial performance of medium enterprises positively whereby (Tirole, 2006) argues that; the easier it is to access credit from financial institutions

and goods from suppliers on credit, the higher the financial performance of the medium enterprises. However, he also indicated that access to credit from credit institutions in form of term loans is not that easier as many requirements need to be met before advancing the credit to the entrepreneur for use in the business.

Cook, and Uchida,( 2004) argued that there is evidence that as credit becomes more available, the financial performance of business becomes better and hence creating a chance for business growth in terms of increased volume on sales made.

### 2.3Conclusion

This chapter identified related research on credit financing and financial performance of medium sized enterprises. It acted as a basis to the Researcher for further research study on the relationship between credit financing and financial performance of medium scale enterprises.

# CHAPTER THREE

# RESEARCH METHODOLOGY

## 3.0 Introduction

This chapter highlighted the particular methods the Researcher used in carrying out the research and their rational. Focus was based on the research design, study population, area of the study, sample size and selection, sampling techniques, methods of data collection, data management and analysis, reliability and validity, ethical considerations, limitations and conclusion.

## 3.1 Research Design

Research design is an overall plan for the methods to be used to collect and analyze the data of a research study (Hair et al., 2008).

A descriptive research design was used in the study. This research design was selected because it enabled the Researcher to get opinions and views of respondents, and analytical assessment about the topic from current literature by scholars. Spearman's correlation design was also used which enabled the Researcher to assess the degree of the relationship that existed between the independent variable (credit financing) and the dependent variable(financial performance) of medium sized businesses. This was so because it promoted a broad understanding of a complex problem through a detailed analysis (Oso, and Onen, 2009).

## 3.2 Area of the study

The area of the research study was in Katwe- Butego Division which is one of the three divisions that make up Masaka Municipality in Masaka district central region of Uganda,

situated about thirty seven (37) kilometers away from the equator towards the south with an average altitude of 1150m above the sea level (Fountain Publishers, 2007) with a focus on examining the effect of credit financing on the financial performance of medium sized enterprises. The Researcher chose the area conveniently due to its accessibility and proximity to the Researcher's area of residence and being the fact that the big numbers of medium scale enterprises are located there.

### 3.3 Study Population

A population refers to all elements, individuals or units that meet the selection criteria for a group to be studied, and from which a representative sample is taken for detailed examination (Odiya, 2009). This definition ensures that the population of interest is homogeneous. However, the Researcher defines population as a complete census of the sampling frames.

Odiya, (2009) continues to define target population in statistics as the specific population about which information is desired.

The study targeted a population of 48 employees of which consisted of managers / head teachers, bursars, accountants, sales officers, and cashiers from 10 medium scale enterprises comprising of private primary and secondary schools, private hospitals, hotels and wholesale shops. This is because such people were expected to be with the intimate financial information of their respective businesses and areas of operations.

**Table 1: Study Population**

| Category | Population |
| --- | --- |
| Private Primary schools | 10 |
| Private Secondary schools | 04 |
| Hotels | 10 |
| Private Hospitals | 10 |
| Wholesale | 14 |
| **Total Population** | **48** |
| Number of medium scale enterprises | **10** |

**Source:** Masaka District Local Government (2018)

## 3.4 Sampling Procedures.

### 3.4.1Sample size and selection

A sample is part of the target population that has been procedurally selected to represent it (Nicholas, 2009).The study was based on a sample size of 42 that was drawn from a population of 48computed using a formulae from Krejcie and Morgan (1970).

$$\frac{\boldsymbol{N2-N1}}{\boldsymbol{S2-S1}} = \frac{\boldsymbol{P-N1}}{\boldsymbol{S-S1}}$$

Where, N1 and N2 are two population values from the Krejcie and Morgan (1970) table and S1 and S2 are their corresponding Sample values. P is the population for the study, S is the sample size for the study.

$$\frac{45-40}{40-36} = \frac{48-40}{S-36}$$

$$\frac{5}{4} = \frac{8}{S-36}$$

S = 42.4 (Rounded off to **42**), the Sample size for the study was 42

**Table 2: Study Sample size and selection**

| Category | Population | Sampling procedure |
|---|---|---|
| Population of Respondents | 48 | |
| Sample size of Respondents | 42 | Simple random sampling |
| Number of Medium scale enterprises | 10 | |
| Sample size of Medium scale enterprises | 10 | Simple random sampling |

**Source:** Krejcie and Morgan (1970)

### 3.4.2 Sampling techniques

Sampling is the process of selecting a sufficient number of elements from the population by studying the sample and understanding the characteristics**.** The Researcher used a simple random sampling technique to select medium enterprises. This technique ensured that each and every member of the target population had an equal and independent chance of being included at any selection point in a sample and thus avoided biasness of the research findings. The research applied to head teachers and bursars / Chief Finance Officers from both private primary and secondary schools and managers, accountants, sales officers, and cashiers from hotels, private hospitals and wholesale shops from the area under the study. The Researcher also used purposive sampling technique to select questionnaire respondents. This sampling technique ensured that people investigated were considered to have the desired and reliable information readily with respect to the topic under study.

## 3.5 Data collection methods and instruments

These are the tools the Researcher employed in the process of data collection in the area of study for efficient and effective data collection.

### 3.5.1 Sources of data

Two sources of data were used for purposes of research. These were primary data and secondary data.

#### 3.5.1.1 Primary Data collection

According to Sekeran, (2003) primary data is that kind of data that has been gathered for the first time. The short comings of secondary data sources such as out datedness and inadequacy in terms of coverage necessitated the use of primary sources for the first data. Self – administered questionnaires were used and this enabled the Researcher to cover a large population quickly and at reasonable cost.

Primary data was obtained directly from the head teachers, and Bursars / Chief Finance Officers (CFOs) of both private primary and secondary schools and also from managers, accountants, sales officers and cashiers from hotels, private hospitals and wholesale businesses.

#### 3.5.1.2 Secondary Data collection

Sekeran, (2003) defines secondary data as that kind of data that is available, already reported by other scholars. Secondary data for this study was got from sources like libraries, publications, journals, online information, text books, and unpublished research reports. This was because, it was readily available and easier to comprehend as it comprised of extensively researched work.

## 3.6.0 Data collection instruments

### 3.6.1 Questionnaire

The study used some research instruments like questionnaires. A questionnaire is defined as a survey instrument intended to self-administered questions (Mannheim and Richard, 1995).Mannheim and Richard, (1995) further emphasised that a questionnaire is an information gathering technique that gathers information, attitudes, beliefs, behaviour and characteristics from selected respondents that the Researcher wishes to measure.

The structured questionnaire was developed using the 5 Likert scale using measures; Strongly Agree, Agree, Not Sure, Disagree and Strongly Disagree.Questionnaires were also chosen because all the respondents were considered literate and could answer it at the time and place of convenience while following their busy schedules.

The Researchercollected primary data using questionnaires because respondents were scattered in various places thus a need to collect and complete responses within a short time possible.

### 3.6.2 Procedure of data collection

The Researcher used a recommendation letter from the university (Faculty of Business Administration and Management) which authorized and recommended the conducting of the research. This recommendation letter was taken to the targeted businesses to obtain approval for collecting data from respondents

## 3.7 Data management and analysis

Data analysis is a process of gathering, modeling and transforming data with the goal of highlighting useful information, suggesting conclusions and supporting decision making (Welman, et al, 2005).

Data was presented using frequency tables and charts. Frequencies, percentages and correlation were used to analyze data. Statistical Package for Social Scientists (SPSS) application software tool was used in the analysis phase. Data collected was gathered, recorded and edited for completeness, legibility, consistency and accuracy through quantitative analysis. Data was summarized in form of frequency tables, bar and pie charts, ranked by percentages, compared, analyzed, interpreted and discussed to produce a final copy of research findings.

### 3.8 Reliability and validity

Reliability of an instrument is the ability of the instrument to collect data consistency under similar conditions (Odiya, 2009). In order to ensure reliability and validity, pilot testing questionnaires were used. This helped the Researcher to get information that was necessary for the study as well as obtaining respondents' compliance depending on the questions asked.

According to Saunders, et al., (2007) validity of an instrument refers to the extent to which the data collection instruments used in the study actually measured what they intended to measure. In order to ensure validity of information, the Researcher used pre- test questionnaires to determine whether the instruments used gave the best results. Observation was also used by the Researcher to assist in avoiding report biases from respondents.

### 3.9 Ethical considerations

The ethical standards were ensured in the study by seeking authorization from relevant people and confidentiality from the information that was given on questionnaires.

There was an assurance of respondents that information given was used against them or their businesses.

The Researcher sought respondents' consent before administering or conducting interviews and there was no need of the interviewees' names and any form of identification to be published since anonymous questionnaires were used. This will aim at making it easier for respondents to provide accurate information.

The Researcher endeavored to be honest and objective in the presentation of the research results and findings about the study to all the respondents.

All the necessary protocols were observed and all the respondents were thanked for their participation in the research study.

### 3.10 Limitations and delimitations of the study

The Researcher faced a number of challenges in the course of carrying out the research and these were;

Lack of cooperation from respondents, especially those who considered the information confidential and think that the study was for the purposes of revenue collection. However, the Researcher ensured the respondents of confidentiality of their information that it was solely to be used for academic purposes.

Financial constraints. The Researcher required substantial amount of money for travelling, stationery costs among others. However, to mitigate this challenge, the Researcher endeavored to use personal resources and also solicited funds from family members and friends as well as looking for cheaper service providers to successfully complete the research.

Slow response and non- response from some respondents since owners of medium scale businesses were busy attending to their customers and sometimes failed to spare time for the Researcher. This was reduced by keeping in touch with the respondents and the Researcher also used a convincing tongue to attract them answer to the questionnaires and also created personal relationships with them.

### 3.11 Conclusion

In this chapter, the study presented the research design, study population, sample size and selection, sampling techniques, methods of data collection, procedure of data collection, data analysis and management, reliability and validity, the ethical considerations, Limitations and delimitations as well as the conclusion.

# CHAPTER FOUR

# DATA PRESENTATION, ANALYSIS AND DISCUSSION OF FINDINGS

## 4.0 Introduction

This chapter presents the results, analysis and discussion of the findings to the study. The study aimed at examining “The effect of credit financing on the financial performance of medium sized enterprises in Katwe – Butego Division, Masaka Municipality.” Results were presented after the investigation of the three research objectives of the study which included; to 3examine the effect of loans on the financial performance of medium scale enterprises, to examine the effect of trade credit on the financial performance of medium scale enterprises and to establish the relationship between credit financing and financial performance of medium scale enterprises.

## 4.1 Demographic Characteristics of Respondents

In this section, efforts were made to document the background information of the respondents such as business category, gender, age in years and education level.

**Table 3: Title of Respondent**

| Title | Frequency | Percentage |
|---|---:|---:|
| Bursar/CFOs | 9 | 21.43 |
| Managers/head teachers | 17 | 40.48 |
| Cashiers | 10 | 23.81 |
| Accountants | 4 | 9.52 |
| Sales officers | 2 | 4.76 |
| **Total** | **42** | **100** |

***Source:*** *Primary data, 2018*

Table 3 above showed the title of Respondents, 9 bursar/ Chief Finance Officers, 17 managers/head teachers, 10 cashiers, 4 accountants and 2 sales officers. Most respondents were mangers/ head teachers (40.48%) who are the key financial decision makers in medium scale businesses.

**Table 4: Business Category**

| Category | Frequency | Percentage |
|---|---|---|
| Primary schools | 6 | 14.3 |
| Secondary schools | 5 | 11.9 |
| Hotels | 10 | 23.8 |
| Hospitals | 8 | 19.0 |
| Wholesale | 13 | 31.0 |
| **Total** | 42 | 100.0 |

***Source:*** *Primary data, 2018*

In table 4 above, the research study sought to establish the business category of the respondents. The tables showed that respondents from primary schools were 6, those from secondary schools were 5, those from hotels were 10, those from hospitals were 8 and those from wholesale were 13. The business category with the highest number of respondents was wholesale with 31% and the business category with lowest number of respondents was secondary schools with a percentage of 11.9%.

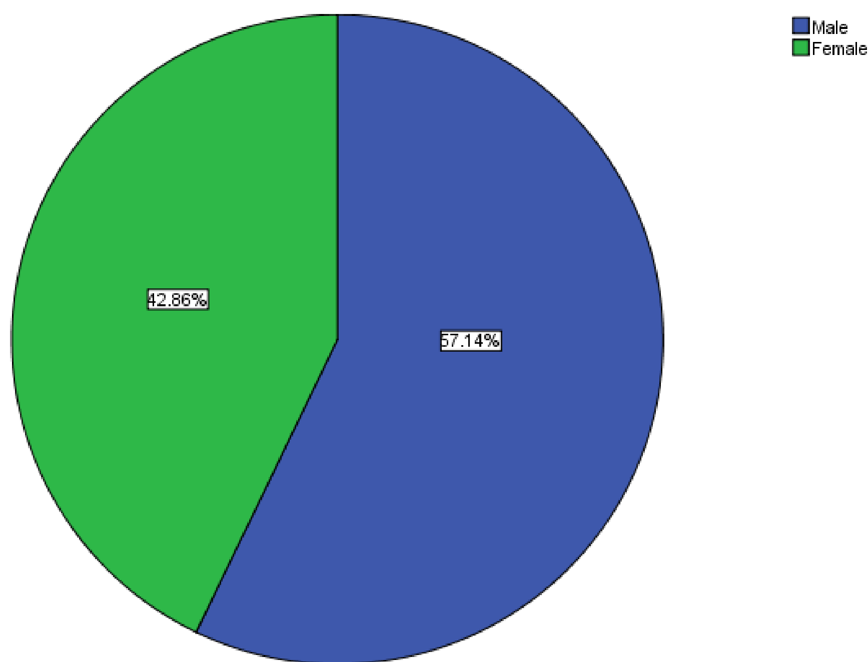
**Table 5: Gender of respondents**

| | **Sex** | **Frequency** | **Percentage** |
|---|---|---|---|
| | Male | 24 | 57.1 |
| | Female | 18 | 42.9 |
| | Total | 42 | 100.0 |

***Source:*** *Primary data, 2018*

Table 5 indicated that 24 male and 18 female respondents participated in the study thus making the number of male higher than that of females with percentages; 57.1% and 42.9% respectively. This implied that during the research, most of the respondents were male since men are more in managing financial matters of medium scale businesses in Katwe - Butego Division though the difference between the numbers of male and female; (6) was not very big thus there was no gender bias in the study.

**Figure 2: Showing Gender of Respondents**




***Source:*** *Primary data, 2018*

Figure 1 indicated that more male respondents participated in the study. This is shown by the biggest percentage of 57.1% and the lowest number of respondents being female which constituted 42.9%.

**Age ranges of the respondents**

The study captured the different age brackets of respondents in order to establish the most prevalent range, the respondents were asked to state their age and distribution was as in the table below;

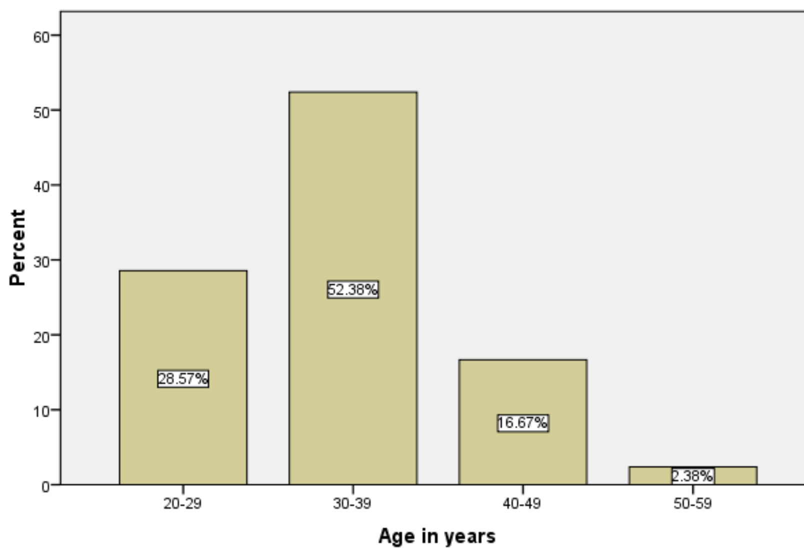
**Table 6: Age of respondents in years**

| Age's range | Frequency | Percentage |
|---|---|---|
| 20-29 years | 12 | 28.6 |
| 30-39 years | 22 | 52.4 |
| 40-49 years | 7 | 16.7 |
| 50-59 years | 1 | 2.4 |
| Total | 42 | 100.0 |

***Source:*** *Primary data, 2018*

Table 6 showed age of respondents who participated in the study; 28.6% of respondents were in the range of 20- 29 years, 52.4% were aged in the range of 30-39 years, 16.7% were aged in the range of 40-49 years and 2.4% of respondents were in the range of 50-59 years. This implied that people handling financial matters of medium scale enterprises are in the age bracket of 30 – 39 years thus making them mature enough to answer the questions designed in the questionnaires.

**Figure 3: Showing Age brackets of Respondents**




***Source:*** *Primary data, 2018*

. Figure 2 showed that majority of respondents were in the 30-39 age bracket with 52.4% and minority of them were in the age bracket of 50-59 with 2.4% respectively.

**Education level of respondents**

The study also captured data on the level of education of respondents and it is as I the table below;

**Table 7: Education level of respondents**

| Education level | Frequency | Percentage |
|---|---|---|
| Masters | 4 | 9.5 |
| Bachelors | 21 | 50.0 |
| Diploma | 12 | 28.6 |
| A- Level | 2 | 4.8 |
| O-Level | 2 | 4.8 |
| Certificate | 1 | 2.4 |
| Total | 42 | 100.0 |

***Source:*** *Primary data, 2018*

Table 7 indicated that all respondents were educated at different levels as it corresponds to their qualifications. 4 of the respondents had a degree in masters, 21 had Bachelors, 12 had diplomas, both A and O-levels had 2 and lastly 1 for certificate. The highest number of respondents was bachelor's degree holders with 50% respondents and the lowest number of respondents was that of certificate holders with 2.4%. The highest number of respondents: Bachelor's degree holders (50%) implied that most people involved in managing finance of MSEs had the necessary qualifications with the required knowledge and skills; and understood the subject under study.

## 4.2 Findings by specific objectives

### 4.2.1 Objective One: The effect of loans on financial performance of MSEs

**Table 8: The business can easily take long-term loans**

| | Frequency | Percentage |
|---|---|---|
| Agree | 17 | 40.5 |
| Disagree | 4 | 9.5 |
| Strongly Agree | 20 | 47.6 |
| Strongly Disagree | 1 | 2.4 |
| **Total** | **42** | **100.0** |

***Source:*** *Primary data, 2018*

Table 8 above showed results of a study that assessed whether MSEs could easily take long term loans. 17 (40.5%) respondents agreed, 4 (9.5%) disagreed, 20 (47.6%) strongly agreed and 1 (2.4%) strongly disagreed. The majority of the respondents 47.6% strongly agreed and 40.5% agreed that medium scale enterprises can easily take long term loans. This implied that long term loans were acquired by most medium enterprises to finance the acquisition of capital (fixed) assets thus leading to improved performance. This was in line with (Roodman, 2009) who asserted that long term credit plays a major role in promoting financial performance.

**Table 9: The business takes short term loans**

| | Frequency | Percentage |
|---|---|---|
| Agree | 25 | 59.5 |
| Disagree | 2 | 4.8 |
| Not Sure | 4 | 9.5 |
| Strongly Agree | 10 | 23.8 |
| Strongly Disagree | 1 | 2.4 |
| **Total** | **42** | **100.0** |

***Source:*** *Primary data, 2018*

Table 9 above revealed results of the study that aimed at assessing whether MSEs took short term loans and in this case; 25 respondents agreed, 2 disagreed, 4 were not sure, 10 strongly agreed and 1 strongly disagreed. The highest percentage (59.5%) of respondents agreed that their businesses took short term loans and the lowest percentage of respondents (2.4%) strongly disagreed. Most respondents in MSEs (59.5%) agreed and 23.8% strongly agreed that short term loans are needed for day to day financial needs of their businesses. Abor, (2007) argued that short term loans are mostly required by medium businesses to ensure sufficient working capital which is repaid out of the sales proceeds thus helping to ensure that the business remains solvent.

Table 10: The long term loan interest rate charges are fair

| | Frequency | Percentage |
|---|---|---|
| Agree | 11 | 26.2 |
| Disagree | 8 | 19.0 |
| Not Sure | 3 | 7.1 |
| Strongly Agree | 15 | 35.7 |
| Strongly Disagree | 5 | 11.9 |
| **Total** | **42** | **100.0** |

***Source:*** *Primary data, 2018*

Table 10 above revealed the results of the study in order to assess whether the long term loan interest rate charges are fair on medium scale enterprises. 11 of the respondents agreed, 8 disagreed, 3 were not sure, 15 strongly agreed and 5 strongly disagreed. The highest percentage (35.7%) of respondents strongly agreed and the lowest percentage (7.1%) of them were not sure.

Most medium scale business people strongly agreed (35.7%) and (26.2%) agreed that long term loan interest rates charged on loans are fair. This implied that medium business owners are encouraged to take long term loans due to friendly interest charged. This was in contradiction with IFC, (2009) which indicated that businesses found a lot of difficulty in obtaining loans due to under developed bank-borrower relationships and high interest rate charges on such loans.

**Table 11: The short term interest rate charges are fair**

| | **Frequency** | **Percentage** |
|---|---|---|
| Agree | 12 | 28.6 |
| Disagree | 18 | 42.9 |
| Not Sure | 8 | 19.0 |
| Strongly Agree | 2 | 4.8 |
| Strongly Disagree | 2 | 4.8 |
| **Total** | **42** | **100.0** |

***Source:*** *Primary data, 2018*

Table 11 above revealed the results of the study in order to assess whether the short term loan interest rate charges are fair on medium scale enterprises. In this case; 12 of the respondents agreed, 18 disagreed, 8 were not sure, 2 strongly agreed and 2 strongly disagreed. The highest percentage (42.9%) of respondents disagreed with short term loan interest charges being fair and the lowest percentages (4.8%) of respondents both strongly agreed and strongly disagreed

With the statement. The data collected from the field revealed that the highest percentage of respondents of 42.9% disagreed that short term loan interest rate charges being fair. This implied that short term loans decrease the profitability of the business. This is in support with Githaiga, (2015) argument who argued that short term loans are given from overnight to less than one year which makes medium enterprises not to perform well in their operations because of big installment payments to be remitted back to financial institutions in the shortest time like weekly, fortnight and monthly payment since the loan grows bigger in a given time with high interest rates charges before even realizing budgeted profits back to business. This was in line with IFC, (2009) which indicated that businesses found a lot of difficulty in obtaining loans due to under developed banks-borrower relationships and sometimes high interest rates charged.

**Table 12: The loan repayment period is fair**

| | Frequency | Percentage |
|---|---|---|
| Agree | 22 | 52.4 |
| Disagree | 5 | 11.9 |
| Not Sure | 5 | 11.9 |
| Strongly Agree | 8 | 19.0 |
| Strongly Disagree | 2 | 4.8 |
| **Total** | **42** | **100.0** |

***Source:*** *Primary data, 2018*

Table 12 above assessed whether the loan repayment period is fair. 22 of the respondents agreed, 5 disagreed, other 5 were not sure, 8 strongly agreed and 2 strongly disagreed.

The highest percentage (52.4%) of respondents agreed that the loan repayment period by medium sized enterprises was fair while the lowest percentage (4.8%) of respondents

strongly disagreed. The study revealed that the respondents with a percentage of 52.4% agreed that the loan repayment period given on is enough to pay back the loan. This implied that financial and credit institutions give borrowers enough grace period to repay the loans due and this helps the business owners to plan and use finances effectively. This was in line with Falkena, (2014) who asserted that establishing an effective grace period by financial institutions would help business owners of medium businesses to monitor their credit portfolio since loan repayment period given would be enough to pay back the loan. This then implied that a fair repayment period encouraged MSEs to acquire loans for financing in their business operations.

**Table 13: Short term loans contribute positively to the profitability of the business**

| | Frequency | Percentage |
|---|---|---|
| None Response | 2 | 4.8 |
| Agree | 18 | 42.9 |
| Disagree | 10 | 23.8 |
| Not Sure | 4 | 9.5 |
| Strongly Agree | 7 | 16.7 |
| Strongly Disagree | 1 | 2.4 |
| **Total** | **42** | **100.0** |

***Source:*** *Primary data, 2018*

The 13 above revealed the findings of the study in order to assess whether short term loans contribute to the profitability of the medium sized businesses. According to the above table, 2 (4.8%) of respondents didn't respondent to the questions, 18 (42.9%) agreed, 10 (23.8%) disagreed, 4 (9.5%) were not sure, 7(16.7%) strongly agreed and 1 (2.4%) strongly disagreed with the statement. Majority of the Respondents (42.9%) agreed that short term loans contribute to the profitability of medium sized enterprises. The short term loan period of

lending to medium enterprises can contribute to positive financial performance through profitability which enhances such business operations and expansion to its survival and productivity in achieving its goals and objectives in the short period (Githaiga, 2015).

**Table 14: Long term loans contribute positively to the return on assets of the business**

| | Frequency | Percentage |
|---|---|---|
| Agree | 22 | 52.4 |
| Disagree | 1 | 2.4 |
| Not Sure | 3 | 7.1 |
| Strongly Agree | 16 | 38.1 |
| **Total** | **42** | **100.0** |

***Source:*** *Primary data, 2018*

Table 14 above showed the results of the study in order to assess whether long term loans contributed positively to the return on assets of medium scale enterprises. Table 11 clearly revealed that 22 of the respondents agreed, 1 disagreed, 3 were not sure and 16 strongly agreed. The highest percentage (52.4%) of Respondents agreed that long term loans contributed positively to the return on assets of medium sized enterprises and (2.4%) disagreed with the statement. This meant that medium scale businesses which take long term loans recorded improved financial performance in form of return on assets.

**Table 15: Short term loans contribute positively to the working capital of the business**

| | Frequency | Percentage |
|---|---|---|
| Agree | 22 | 52.4 |
| Disagree | 6 | 14.3 |
| Not Sure | 3 | 7.1 |
| Strongly Agree | 10 | 23.8 |
| Strongly Disagree | 1 | 2.4 |
| **Total** | **42** | **100.0** |

***Source:*** *Primary data, 2018*

Table 15 above showed the results of the study to assess whether short term loans contribute positively to the working capital of the medium sized enterprises. 22 of the respondents agreed, 6 disagreed, 3 were not sure, 10 strongly agreed and lastly only 1 respondent strongly disagreed. The table above revealed (52.4%) as the highest percentage of respondents who agreed that the short term loans contributed positively to the working capital of their businesses and the lowest percentage (2.4%) of respondents strongly disagreed with the statement.

**Table 16: Relationship between Short term loans and Profitability of MSEs**

| | | | The business takes short term loans | Short term loans contribute positively to the profitability of the business |
|---|---|---|---|---|
| Spearman's rho | The business takes short term loans | Correlation Coefficient | 1.000 | -.042 |
| | | Sig. (2-tailed) | . | .791 |
| | | N | 42 | 42 |
| | Short term loans contribute positively to the profitability of the business | Correlation Coefficient | -.042 | 1.000 |
| | | Sig. (2-tailed) | .791 | . |
| | | N | 42 | 42 |

***Source****: Primary data, 2018*

From table 16 above, spearman's correlation coefficient is -0.042. This implied that there was a negligible negative relationship between short term loans and profitability of the Medium scale enterprises.

**Table 17: Relationship between Short term loans and Working Capital of MSEs**

| | | | The business takes short term loans | Short term loans contribute positively to the working capital of the business |
|---|---|---|---|---|
| Spearman's rho | The business takes short term loans | Correlation Coefficient | 1.000 | .255 |
| | | Sig. (2-tailed) | . | .104 |
| | | N | 42 | 42 |
| | Short term loans contribute positively to the working capital of the business | Correlation Coefficient | .255 | 1.000 |
| | | Sig. (2-tailed) | .104 | . |
| | | N | 42 | 42 |

***Source:*** *Primary data, (2018)*

From table 17 above, spearman's correlation coefficient was 0.255. Therefore, the coefficient implied that there was a weak positive relationship between short term loans and working capital of medium scale enterprises in Katwe – Butego Division.

**Table 18: Relationship between Long term loans and return on assets of MSEs**

| | | | The business can easily take long term loans | Long term loans contribute positively to the return on assets of the business |
|---|---|---|---|---|
| Spearman's rho | The business can easily take long term loans | Correlation Coefficient | 1.000 | .241 |
| | | Sig. (2-tailed) | . | .125 |
| | | N | 42 | 42 |
| | Long term loans contribute positively to the return on assets of the business | Correlation Coefficient | .241 | 1.000 |
| | | Sig. (2-tailed) | .125 | . |
| | | N | 42 | 42 |

***Source:*** *Primary data, 2018*

From the table above, spearman's correlation coefficient was 0.241. This implied that there was a weak positive relationship between long term loans and return on assets of the medium scale enterprises in Katwe – Butego Division.

From the research findings of objective one, loans improved the financial performance of medium scale enterprises. Business men and women of medium scale enterprises who took long term loans from credit and financial institutions recorded improved financial performance in their businesses' operations. Short term loans contributed to the profitability of such businesses. Data which was collected from the field also revealed that; 14.3% of the respondents disagreed that short term loan interest rate charges were not fair. This is because such loans decreased the business profitability since short-term loans are required to be paid back in the short period of time like fortnight, monthly with high interest rate charges before even realizing the budgeted profits back to business.

### 4.2.2 Objective Two: The effect of trade credit on financial performance of MSEs

**Table 19: The business takes trade credit**

| | Frequency | Percentage |
|---|---|---|
| Agree | 5 | 11.9 |
| Disagree | 4 | 9.5 |
| Strongly Agree | 33 | 78.6 |
| **Total** | **42** | **100.0** |

***Source:*** *Primary data, 2018*

Table 19 revealed the results of the study in order to assess whether medium sized businesses take trade credit. 5 of the respondents agreed, 4 disagreed and 33 strongly agreed. The table above clearly showed that the highest percentage (78%) of respondents strongly agreed and the lowest percentage (9.5%) of respondents disagreed with the statement. Majority of respondents strongly agreed (78.6%) which meant that most medium sized enterprises take

trade credit in terms of supplies taken on credit with a promise to pay them at an agreed date. This agrees with Yang, (2011) who urged that suppliers allow their customers to delay their payments within stipulated period of time thus allowing payments to occur after the receipts of goods and services.

**Table 20: The payment period to suppliers is fair**

| | Frequency | Percentage |
|---|---|---|
| Agree | 17 | 40.5 |
| Disagree | 3 | 7.1 |
| Not Sure | 3 | 7.1 |
| Strongly Agree | 19 | 45.2 |
| **Total** | **42** | **100.0** |

***Source:*** *Primary data, 2018*

Table 20 indicated the results of the study in order to assess whether the payment period to suppliers by medium sized enterprises was fair. According to table 20 above, 17 of the respondents agreed, 3 disagreed, 3 were not sure and 19 strongly agreed. The above table clearly revealed (45.2%) as the highest percentage of respondents who strongly agreed that the payment period to suppliers was fair and (7.1%) of respondents disagreed and others of the same percentage (7.1%) were not sure with the statement. Most of the respondents from MSEs strongly agreed (45.2%) and (40.5%) agreed that the payment period to suppliers was fair. This allowed MSEs to have sufficient stock with limited funds to pay to suppliers.

**Table 21: Trade credit contributes positively to the profitability of the business**

| | | Frequency | Percentage |
|---|---|---|---|
| Valid | Agree | 11 | 26.2 |
| | Disagree | 2 | 4.8 |
| | Not Sure | 3 | 7.1 |
| | Strongly Agree | 26 | 61.9 |
| | Total | 42 | 100.0 |

***Source:*** *Primary data, 2018*

Table 21 above indicated the results of the study in order to assess whether trade credit contributed positively to the profitability of the medium scale enterprises. According to table 21 above, 11 of the respondents agreed, 2 disagreed, 3 were not sure and 26 strongly agreed. The table clearly indicated (61.9%) as the highest percentage for those respondents that strongly agreed and (4.8%) as the lowest percentage for those who disagreed with the statement. This indicated that trade credit positively improved the value and profitability of the business (Garcai-Teruel and Martniez-Solano, 2014).

**Table 22: Trade credit contributes positively to the working capital of the business**

| | **Frequency** | **Percentage** |
|---|---|---|
| Non response | 1 | 2.4 |
| Agree | 16 | 38.1 |
| Disagree | 2 | 4.8 |
| Not Sure | 4 | 9.5 |
| Strongly Agree | 19 | 45.2 |
| **Total** | **42** | **100.0** |

***Source:*** *Primary data, 2018*

Table 22 above indicated the results of the study to assess whether trade credit contributes positively to the working capital of medium sized enterprises. According to table 22 above, 1 respondent didn’t attempt this question, 16 agreed, 2 disagreed, 4 were not sure and 19 strongly agreed with the statement. Majority of the respondents strongly agreed (45.2%) and (38.1%) agreed that trade credit contributed to the working capital of the business.

**Table 23: The business keeps track of payments**

| | Frequency | Percentage |
|---|---|---|
| Agree | 11 | 26.2 |
| Not Sure | 3 | 7.1 |
| Strongly Agree | 28 | 66.7 |
| **Total** | **42** | **100.0** |

***Source:*** *Primary data, 2018*

Table 23 above revealed the results of the study with a view to assess whether medium sized businesses keep track of payments. According table 23 above, 11 of the respondents agreed, 3 were not sure and 28 strongly agreed. The majority (66.7%) of the respondents strongly agreed that their businesses kept track of payments and the minority (7.1%) were not sure with the statement. This implied that most MSEs kept track of their payments to avoid the detrimental effects that are associated with trade credit in form of paying more administrative costs such as default debts, screening and monitoring costs by suppliers (Hill, et al, 2012).

**Table 24: Suppliers give appropriate periods to MSEs to pay their bills**

| | Frequency | Percentage |
|---|---|---|
| Agree | 23 | 54.8 |
| Disagree | 5 | 11.9 |
| Not Sure | 3 | 7.1 |
| Strongly Agree | 11 | 26.2 |
| **Total** | **42** | **100.0** |

***Source:*** *Primary data, 2018*

Table 24 above showed the results of the study in order to assess whether suppliers give medium scale enterprises appropriate periods to pay their bills for the goods and services got on credit as they fall due. According to the above table, 23 of the respondents agreed, 5 disagreed, 3 were not sure and 11 strongly agreed. The highest percentage (54.8%) of respondents agreed and the lowest percentage (7.1%) were not sure with the statement. This meant that most MSEs are given enough time to pay their bills as they fallen due. This is in support with Katrien, et al, (2012) who argued that trade credit is used as an evaluation tool by customers to analyze the quality of products as they are granted to make prolonged payments in a given specified period.

**Table 25: The business analyses customers' financial statements**

| | **Frequency** | **Percentage** |
|---|---|---|
| Agree | 19 | 45.2 |
| Disagree | 2 | 4.8 |
| Not Sure | 6 | 14.3 |
| Strongly Agree | 14 | 33.3 |
| Strongly Disagree | 1 | 2.4 |
| **Total** | **42** | **100.0** |

***Source:*** *Primary data, 2018*

Table 25 above revealed the results of the study in order to assess whether the medium businesses analyze customers' financial statements. 19 of the respondents agreed, 2 disagreed, 6 were not sure, 14 strongly agreed and only 1 respondent strongly disagreed. The highest percentage (45.2%) of respondents agreed and the lowest percentage of (2.4%) strongly disagreed with the above statement. Most respondents agreed (45.2%) that the MSEs tracked their accounts receivables to ensure that they have enough cash to pay off supplier bills on time when they fall due.

**Table 26: Relationship between Trade Credit and Profitability of MSEs**

| | | | The business takes trade credit | Trade credit contributes positively to the profitability of the business |
|---|---|---|---|---|
| Spearman's rho | The business takes trade credit | Correlation Coefficient | 1.000 | .300 |
| | | Sig. (2-tailed) | . | .053 |
| | | N | 42 | 42 |
| | Trade credit contributes positively to the profitability of the business | Correlation Coefficient | .300 | 1.000 |
| | | Sig. (2-tailed) | .053 | . |
| | | N | 42 | 42 |

***Source:*** *Primary data (2018)*

From table 26 above, spearman's correlation coefficient was 0.300. This implied that there was a weak positive relationship between trade credit and profitability of the medium scale enterprises.

**Table 27: Relationship between trade credit and working capital of MSEs**

| | | | The business takes trade credit | Trade credit contributes positively to the working capital of the business |
|---|---|---|---|---|
| Spearman's rho | The business takes trade credit | Correlation Coefficient | 1.000 | .235 |
| | | Sig. (2-tailed) | . | .139 |
| | | N | 42 | 41 |
| | Trade credit contributes positively to the working capital of the business | Correlation Coefficient | .235 | 1.000 |
| | | Sig. (2-tailed) | .139 | . |
| | | N | 41 | 41 |

***Source:*** *Primary data, (2018)*

From table 27 above, spearman's correlation coefficient was 0.235. The coefficient implied that there was a weak positive relationship between trade credit and working capital of the medium scale enterprises.

Findings from objective two indicated that majority of respondents strongly agreed (78.6%) that medium sized enterprises took trade credit in terms of supplies taken on credit with a promise to pay them at an agreed date. Majority of the respondents strongly agreed (45.2%) and agreed (38.1%) that trade credit contributed to the working capital of the business. Most of the respondents from MSEs strongly agreed that the payment period given by suppliers was fair. The highest percentage of respondents strongly agreed that trade credit positively

improved the value and profitability of the business. Medium scale enterprises kept track of their payments to avoid the detrimental effects that are associated with trade credit inform of paying more administrative costs such as default charges, screening and monitoring costs by suppliers of goods and services (Hill, et al, 2012). Most medium enterprises are given enough time to pay their bills to suppliers when they fallen due. Most respondents also agreed (45.2%) that the MSEs kept track of their receivables to ensure that they have enough cash to pay off supplier bills on time. All in all trade credit improves financial performance of medium scale businesses.

#### 4.2.3 Objective Three: Relationship between credit financing and financial performance of medium scale enterprises

**Table 28: Loans contribute positively to the profitability of the business**

| | Frequency | Percentage |
|---|---|---|
| Agree | 13 | 31.0 |
| Disagree | 3 | 7.1 |
| Strongly Agree | 26 | 61.9 |
| Total | 42 | 100.0 |

***Source:*** *Primary data, 2018*

Table 28 above indicated the results of the study to assess whether loans contributed positively to the profitability of MSEs. According to the above table, 13 agreed, 3 disagreed and 26 strongly agreed. The highest percentage (61.9%) and the lowest percentage (7.1%) of the respondents strongly agreed and disagreed with the statement respectively. Most respondents strongly agreed (61.9%) that loans contributed positively to the profitability of their businesses.

**Table 29: Short term loans contribute positively to the working capital of the business**

| | Frequency | Percentage |
|---|---|---|
| Agree | 22 | 52.4 |
| Disagree | 6 | 14.3 |
| Not Sure | 5 | 11.9 |
| Strongly Agree | 9 | 21.4 |
| Total | 42 | 100.0 |

***Source:*** *Primary data, 2018*

Table 29 above revealed the results of the study with a view to assess whether short term loans contributed to the working capital of medium scale enterprises. 22 of the respondents agreed, 6 disagreed, 5 were not sure and 9 strongly agreed. The highest and the lowest percentages of respondents were (52.4%) and (11.9%) respectively. Most of the respondents (52.4%) agreed that short term loans contributed positively to the working capital of the business.

**Table 30: Long term loans contribute positively to the return on assets of the business**

| | Frequency | Percentage |
|---|---|---|
| Agree | 20 | 47.6 |
| Disagree | 1 | 2.4 |
| Not Sure | 3 | 7.1 |
| Strongly Agree | 18 | 42.9 |
| Total | 42 | 100.0 |

***Source:*** *Primary data, 2018*

Table 30 above indicated the results of the study to assess whether long term loans contributed positively to the return on assets of medium scale enterprises. According to table 30 above, 20 of the respondents agreed, 1 disagreed, 3 were not sure and 18 strongly agreed. The highest and the lowest percentage s of respondents were (47.6%) and (2.4%) respectively. Most of the MSEs respondents agreed (47.6%) and 42.9% strongly agreed that long term loans contributed positively to the return on assets of medium scale enterprises.

**Table 31: Trade credit contributes positively to the profitability of the business**

| | Frequency | Percentage |
|---|---|---|
| Agree | 11 | 26.2 |
| Disagree | 1 | 2.4 |
| Not Sure | 4 | 9.5 |
| Strongly Agree | 26 | 61.9 |
| Total | 42 | 100.0 |

***Source:*** *Primary data, 2018*

Table 31 above showed the results of the study in order to assess whether trade credit contributed positively to the profitability of MSEs. According to the table above, 11 of the respondents agreed, 1 disagreed, 4 were not sure and 26 strongly agreed. The highest and the lowest percentage of respondents were (61.9%) who strongly agreed and (2.4%) who disagreed with the statement respectively. From the data collected from the field, (61.9%) of the respondents strongly agreed and 26.2% agreed that trade credit contributed positively to the profitability of medium scale businesses.

**Table 32: Trade credit contributes positively to the working capital of the business**

| | Frequency | Percentage |
|---|---|---|
| Agree | 13 | 31.0 |
| Disagree | 3 | 7.1 |
| Not Sure | 3 | 7.1 |
| Strongly Agree | 23 | 54.8 |
| Total | 42 | 100.0 |

***Source:*** *Primary data, 2018*

Table 32 above revealed the results of the study in order to assess whether trade credit contributed positively to the working capital of MSEs. According to the table above, 13 of the respondents agreed, 3 disagreed, 3 were not sure and 23 strongly agreed. The highest and the lowest percentage of respondents were (54.8%) who strongly agreed and (7.1%) who both disagreed and not being sure with the statement respectively. According from the data collected from the field, 54.8% of the respondents strongly agreed and 31% agreed that trade credit contributed positively to the working capital of medium scale businesses.

**Table 33: Bank overdraft contributes positively to the working capital of the business**

| | Frequency | Percentage |
|---|---|---|
| Agree | 17 | 40.5 |
| Disagree | 6 | 14.3 |
| Not Sure | 4 | 9.5 |
| Strongly agree | 12 | 28.6 |
| Strongly Disagree | 3 | 7.1 |
| Total | 42 | 100.0 |

***Source:*** *Primary data, 2018*

Table 33 above revealed the results of the study in order to assess whether a bank overdraft contributes positively to the working capital of medium sized businesses.17 of the respondents agreed, 6 disagreed, 4 were not sure, 12 strongly agreed and 3 strongly disagreed. The highest percentage (40.5%) of respondents agreed and the lowest percentage (7.1%) strongly disagreed with the statement. Basing from the data collected in table 33 above, (40.5%) of the respondents agreed and 28.6% strongly agreed that bank overdraft contributed positively to the working capital of medium scale enterprises.

**Table 34: A financial information system contributes positively to the financial performance of the business**

| | Frequency | Percentage |
|---|---|---|
| Agree | 9 | 21.4 |
| Disagree | 1 | 2.4 |
| Not Sure | 1 | 2.4 |
| Strongly Agree | 31 | 73.8 |
| Total | 42 | 100.0 |

***Source:** Primary data, 2018*

Table 34 above indicated the results of the study to assess whether a financial information system contributed positively to the financial performance of MSEs. According to table 34 above, 9 of the respondents agreed, 1 disagreed, 1 was not sure and 31 strongly agreed. The highest and the lowest percentages of respondents were (73.8 %) who strongly agreed and (2.4%) who both disagreed and not being sure respectively. From the data collected from field, (73.8%) of respondents strongly agreed and 21.4% agreed that a financial information system contributed positively to the financial performance of medium scale enterprises (Falkena et al, 2014).

**Table 35: Skilled and competent financial management personnel contributes to the financial performance of the business**

| | Frequency | Percentage |
|---|---|---|
| Agree | 10 | 23.8 |
| Not Sure | 1 | 2.4 |
| Strongly Agree | 31 | 73.8 |
| **Total** | **42** | **100.0** |

***Source:*** *Primary data, 2018*

Table 35 above revealed the results of the study in order to assess whether skilled and competent financial management personnel contributed to the financial performance of medium businesses. According to table 35 above, 10 of the respondents agreed, 1 was not sure and 31 strongly agreed. The highest percentage 73.8%) of respondents strongly agreed and the lowest percentage of (2.4%) were not sure with the statement. Majority of respondents (73.8%) strongly agreed and 23.8% agreed that skilled and competent financial management personnel contributed to the financial performance of medium scale enterprises. However, this disagrees with Falkena et al, (2014) who asserted that entrepreneurs in developing countries like Uganda are hit hard by poverty and lack of collateral due to poor internal controls and difficulty in employing competent people with techniques in financial management matters. This is because of the salaries such people would demand thus resulting into poor financial performance of medium scale enterprises.

**Table 36: Other Determinants of Financial Performance**

| Category | Frequency | Percentage |
|---|---:|---:|
| Interest Rate | 39 | 28.1 |
| Government policy | 34 | 24.5 |
| Market performance | 28 | 20.1 |
| Inflation | 30 | 21.6 |
| Defaulting suppliers | 1 | 0.7 |
| Customer tastes and preferences | 1 | 0.7 |
| Customer base | 2 | 1.4 |
| Seasonal changes | 1 | 0.7 |
| Political climate | 1 | 0.7 |
| Business processes | 1 | 0.7 |
| Management style | 1 | .0.7 |
| **Total** | **139** | **100** |

***Source:*** *Primary data, 2018*

From the research findings, the other determinants of financial performance specified by respondents included; interest rates, government policies, market performance and inflation having percentages; 28.1%, 24.5%, 20.1%, 21.6% respectively as showed by table 33 above . However, some respondents also mentioned some other determinants such as defaulting suppliers, customer tastes and preferences, customer base, seasonal changes, political climate, business processes and management style that also affected the financial performance of medium scale businesses.

Findings from objective three indicated that most respondents strongly agreed (61.9%) that loans contributed positively to the profitability of the business. Most of the respondents (52.4%) agreed that short term loans contributed positively to the working capital of the business. Most of the medium scale enterprises respondents' agreed (47.6%) and 42.9% strongly agreed that long term loans contributed positively to the return on assets. From the data collected in the field, (61.9%) of the respondents strongly agreed and 26.2% agreed that trade credit contributed positively to the profitability of medium scale businesses. According to the data collected from the field, 54.8% of the respondents strongly agreed and 31% agreed that trade credit contributed positively to the working capital of medium scale businesses. In most MSEs, (40.5%) of the respondents agreed and 28.6% strongly agreed that bank overdraft contributed positively to the working capital of medium scale enterprises. From the data collected from field, (73.8%) of respondents strongly agreed and 21.4% agreed that a financial information system contributed positively to the financial performance of medium scale enterprises. Majority of respondents (73.8%) strongly agreed and 23.8% agreed that skilled and competent financial management personnel contributed to the financial performance of medium scale enterprises. However, there were other determinants of financial performance that were specified by respondents. These included; interest rates, government policies, market performance and inflation among other factors.

# CHAPTER FIVE

# SUMMARY, CONCLUSIONS AND RECOMMENDATION

## 5.0 Introduction

This chapter presents the discussion of the findings, conclusions and recommendations for the study and it is arranged according to the specific objectives, thus to examine the effect of credit financing on the financial performance of medium scale enterprises in Katwe- Butego Division, Masaka Municipality.

## 5.1Summary of findings

### 5.1.1 Effect of loans on financial performance of MSEs

The study findings showed that majority of respondents agreed that medium enterprises easily take long term loans to finance the acquisition of capital or fixed assets thus leading to improved performance, the findings revealed that most of the respondents agreed that medium businesses take short term loans for running day to day financial needs and ensuring sufficient working capital such that the businesses remain solvent.

From the questionnaires, results also showed that short term loan interest charges were not fair which discouraged MSEs from borrowing and even when MSEs do borrow, loans are given in small amounts and this is basically because of the large amounts of funds used in the repayment of the loan obtained. Short repayment periods inhibited large amounts being borrowed from financial and credit institutions hence having an effect on the financial performance of the medium scale enterprises in such a way that they decrease the profitability of the businesses before even realizing profits back into the business. Most of respondents said that as the costs of borrowing on loans increased, the profits decreased and so were the returns of the business.

Results also showed that most respondents agreed that short term loans contributed positively to the profitability of their businesses as well as long term loans contributing positively to the return on assets of medium sized businesses. This therefore, revealed that businesses that took long term loans from financial or credit institutions recorded a better and improved financial performance in their operations.

### 5.1.2 Effect of trade credit on financial performance of MSEs

Findings of the study indicated that majority of respondents (78.6%) strongly agreed that medium sized enterprises took trade credit in terms of supplies taken on credit from suppliers with a promise to pay them at an agreed date. This was in agreement with Curiat, (2007), who urged that trade credit motivated business owners to go for more of supplies on credit. This is so because trade credit reduced transaction costs and payments for the merchandise are made later on rather than cash on delivery.

The results from the field also showed that medium businesses payment periods to their suppliers were fair and this allowed such businesses to have sufficient stock on credit terms with suppliers.

Findings from the field showed that, trade credit contributed positively to the working capital of the business through improved value and profitability of the business. The findings further revealed that medium scale enterprises kept track of their payments in order to try as much as possible to avoid the detrimental effects that are associated with trade credit inform of paying more administrative costs such as default charges, screening and monitoring costs by suppliers of goods and services (Hill, et al, 2012).

It was also realized that, most medium enterprises are given enough time to pay their bills to suppliers when they fall due. This was evidenced when most respondents agreed (45.2%) that their businesses kept track of the accounts receivables with an aim of ensuring that they have

enough cash to pay immediately or in advance to supplier bills on time, thus making trade credit improve financial performance of medium scale businesses.

### 5.1.3 Relationship between credit financing and financial performance of MSEs

Findings from the field study revealed that loans contributed positively to the profitability, return on assets and working capital of medium businesses. Results from the field also showed that most of the respondents strongly agreed that trade credit contributed positively to the profitability and working capital of medium sized businesses.

Research findings showed that most respondents strongly agreed that financial information system, skilled and competent financial management personnel contributed positively to the financial performance of medium enterprises. However, this contradicted with Pandula, (2011) assertion that stated that 90% of the medium scale businesses had ended up in poor financial position that has led to the business collapse before even celebrating the first anniversary due to inadequate technical and management support services, inadequacy of records and information relating to their operations.

## 5.2 Conclusions

The research which was undertaken to examine the effect of credit financing on the financial performance of medium scale enterprises revealed that loans contributed positively to the financial performance of the business. However, the short term loan interest rate charges were considered to be unfair due to the short repayment period accorded to such loans before the business realizes the expected profits.

From the field data collected, it was argued by the respondents that the profits made by medium scale enterprises were greatly encroached on by the high interest rate charges on loans advanced thus resulting into poor financial performance of medium scale enterprises.

The more medium businesses accessed suppliers for the supply of goods and services on credit, the more the working capital of the businesses increased. This therefore, helped businesses increase their productivity, hence leading to increased profitability and financial performance of the enterprises. However, all this could be achieved through suppliers being tied up with customers (buyers) in a stable commercial relationship via trade credit.

### 5.3 Recommendations.

In view of the findings made and conclusions drawn from the study, the following recommendations are provided to help enhance accelerated and successful yardsticks towards credit financing and financial performance of medium scale enterprises;

The central bank should set policies and procedures to prevent barriers that inhibit potential owners and managers of medium scale enterprises from accessing credit facilities in form of loans and bank overdrafts from financial and other credit institutions. This will create a condusive environment for MSEs' growth and expansion as well as opening up opportunities for jobs thus enhancing economic growth.

Financial institutions should also provide financial advisory services to individual proprietors when advancing credit to them; lower the lending rates while improving service delivery, train people on credit risk management and financial management.

The government through the central bank should also regulate financial and credit institutions to ensure that the owners and managers of medium get access to financial information in order to make right investment and financing decisions.

Financial institutions should not only consider collaterals and securities as the main requirements for lending to MSEs since most of the MSEs in Katwe- Butego Division do not have these collaterals and securities yet they can borrow funds and repay the loan without

defaulting. In other words, credit and financial institutions should put much focus and emphasis on the projected cash flows and the viability of the borrower's business.

Financial and credit institutions should revise and ensure that the loan repayment period accorded to medium businesses is fair in order to encourage such businesses have access to borrowing both short and long term loans to boost their business operations.

Medium business owners should ensure up to date business records through proper financial record keeping of their daily operations since businesses without proper business financial information system discourage credit and financial institutions and suppliers of goods and services from offering credit facilities. This in the end threatens their profitability, survival and ability to grow. According to the credit rationing theory by Stiglitz and Weiss (1981), it is asserted that; firms with asymmetric information result into adverse selection as banks and other credit institutions do not possess intricate knowledge about the enterprise and thus, in an attempt to decrease the negative effects of defaulting customers, they usually charge high interest rates This is because such enterprises are perceived to be highly risky to finance in the eyes of financial institutions (Mwangi, 2011).

Medium businesses should use trade credit instead of direct price reduction to boost their sales simultaneously especially during periods of tight money. This is because business's sales are sensitive to the demand fluctuations (Katrien, et al, 2012), thus trade credit is an important method that stimulates customers to acquire merchandises in a period of low demand.

### 5.4 Suggestions for further research

The findings of the study suggest research in examining the effect of credit financing on the financial performance of medium scale enterprises in Masaka Municipality, Katwe- Butego Division. The research focused majorly on medium scale businesses and was carried out

within a short period of time, thus this calls for a long period of time for further research on the suggested topics as below;

1. Effect of credit facilities and financial performance of small scale enterprises (SSEs).
2. Effect of credit policies and financial performance of small and medium enterprises
3. Relationship between credit risk management on financial performance of medium scale enterprises.
4. Effect of loan management on the financial performance of commercial banks.

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## APPENDIX1: RESEARCH QUESTIONNAIRE

Dear Respondent(s),

I am Nalwadda Evalyne, a final year student of Uganda Martyrs University, in the Faculty of Business Administration and Management. I am carrying out research under the topic entitled **"The effect of credit financing on the financial Performance of medium sized enterprises in Katwe- Butego Division, Masaka Municipality."** as a requirement for attaining my Bachelor's Degree in Business Administration and Management of Uganda Martyrs University, Nkozi.

I request you kindly to answer the following questions without any fear since your information will be treated with a high level of confidentiality and will be used for **academic purposes only**. Your sincere response to this questionnaire will be highly appreciated.

Allow me to thank you in advance.

### PART A: DEMOGRAPHIC CHARACTERISTICS OF RESPONDENTS

Please tick or fill the right response that describes you for each of the following items

(Tick in the box where applicable)

1. Title of Respondent: …………………………………

2. Business Category: A) Primary school ☐ B) secondary school ☐ C) Hotel ☐

D) Hospital ☐

E) Wholesaler or retail shop ☐

3. Gender: A) Male ☐ B) Female ☐

4. Age in years: A) 20-29 ☐ B) 30- 39 ☐ C) 40-49 ☐ D) 50-59 ☐

F) 60- Above ☐

5. Education level: A) Masters ☐ B) Bachelors ☐ C) Diploma ☐

D) Certificate ☐ E) A- Level ☐ F) O- Level ☐

**Description of abbreviations used in the Questionnaire**

| **Abbreviation:** | SA | A | NS | D | SD |
|---|---|---|---|---|---|
| **Meaning:** | Strongly Agree | Agree | Not sure | Disagree | Strongly Disagree |

**PART B: THE EFFECT OF LOANS ON FINANCIAL PERFORMANCE OF MEDIUM SCALE ENTERPRISES.**

**Please respond to the following statement or activity by indicating the extent to which you agree or disagree with the statement or activity (Tick one option for each question)**

| **Statement / activity** | **SA** | **A** | **NA** | **D** | **SD** |
|---|---|---|---|---|---|
| 1. The business can easily take long term loans | | | | | |
| 2. The business takes short term loans | | | | | |
| 3. The long term loan interest charges are fair | | | | | |
| 4. The short term loan interest charges are fair | | | | | |
| 5. The loan repayment period is fair | | | | | |
| 6. Short term loans contribute positively to the profitability of the business | | | | | |
| 7. Long term loans contribute positively to the return on assets of the business | | | | | |
| 8. Short term loans contribute positively to the working capital of the business | | | | | |

**PART C: THE EFFECT OF TRADE CREDIT ON FINANCIAL PERFORMANCE OF MEDIUM SCALE ENTERPRISES.**

**Please respond to the following statement or activity by indicating the extent to which you agree or disagree with the statement or activity (Tick one option for each question)**

| **Statement / Activity** | **SA** | **A** | **NA** | **D** | **SD** |
|---|---|---|---|---|---|
| 1. The business takes trade credit | | | | | |
| 2. The payment period to suppliers is fair | | | | | |
| 3. Trade credit contributes positively to the profitability of the business | | | | | |
| 4. Trade credit contributes positively to the working capital of the business | | | | | |
| 5. The business keeps track of payments | | | | | |
| 6. Suppliers give appropriate periods to their customers to pay their bills as they fall due | | | | | |
| 7. The business analyze customers' financial statements | | | | | |

**PART D: RELATIONSHIP BETWEEN CREDIT FINANCING AND FINANCIAL PERFORMANCE OF MEDIUM SCALE ENTERPRISES.**

**Please respond to the following statement or activity by indicating the extent to which you agree or disagree with the statement or activity (Tick one option for each question).**

| Statements / Activities | SA | A | NA | D | SD |
|---|---|---|---|---|---|
| 1. Loans contribute positively to the profitability of the business | | | | | |
| 2. Short term loans contribute positively to the working capital of the business | | | | | |
| 3. Long term loans contribute positively to the return on assets of the business | | | | | |
| 4. Trade credit contributes positively to the profitability of the business | | | | | |
| 5. Trade credit contributes positively to the working capital of the business | | | | | |
| 6. Bank overdraft contributes positively to working capital of the business | | | | | |
| 7. A financial information system contributes to the financial performance of the business | | | | | |
| 8. Skilled and competent financial management personnel contribute to the financial performance of the business | | | | | |

9. What are the other determinants of financial performance of the business (tick all that apply)

1. Interest rates ☐

2. Government policies ☐

3. Market performance ☐

4. Inflation ☐

5. Others (Specify) ________________________________

**Thank you for participating in this research**

**May the Almighty God bless and rewards you abundantly**

## APPENDIX II: WORK PLAN

| MONTH | ACTIVITY |
|---|---|
| February - March , 2018 | • Submission of the 1st draft of the proposal to the research supervisor. |
| April, 2018 | • Submission of the 2nd draft of the proposal to the research supervisor. |
| 14th May – 30th May , 2018 | • Data analysis, discussion and presentation.<br>• Submission of draft on data analyzed.<br>• Preparing summary of findings, conclusion and recommendations. |
| 31st May, 2018 | • Printing and final submission of the entire dissertation to BAM office. |

## APPENDIX III: BUDGET RESEARCH FRAME WORK

| ITEMS | QUANTITY | UNIT COST(UGX) | TOTAL COST (UGX) |
|---|---|---|---|
| **Stationery** | | | |
| Reams of papers | 2 | 12,000 | 24,000 |
| Pens | 3 | 500 | 1,500 |
| Pencil | 1 | 200 | 200 |
| Note book | 1 | 1,500 | 1,500 |
| **Research Proposal** | | | |
| Printing of proposal | 1 | 25,000 | 25,000 |
| Binding | 1 | 3,000 | 3,000 |
| **Dissertation** | | | |
| Airtime | - | 40,000 | 40,000 |
| Transport | - | 55,000 | 55,000 |
| First draft printing | 1 | 30,000 | 30,000 |
| Second draft printing | 1 | 30,000 | 30,000 |
| Compact Disk (CD) | 1 | 2,000 | 2,000 |
| Printing final and personal copy | 3 | 40,000 | 120,000 |
| **Field personnel** | - | 25,000 | 25,000 |
| **Refreshments** | - | 30,000 | 30,000 |
| **Miscellaneous** | - | 35,000 | 35,000 |
| **TOTAL COSTS:** | | | **422,200** |

## APPENDIX IV: KREJCIE AND MORGAN TABLE

Table 3.1

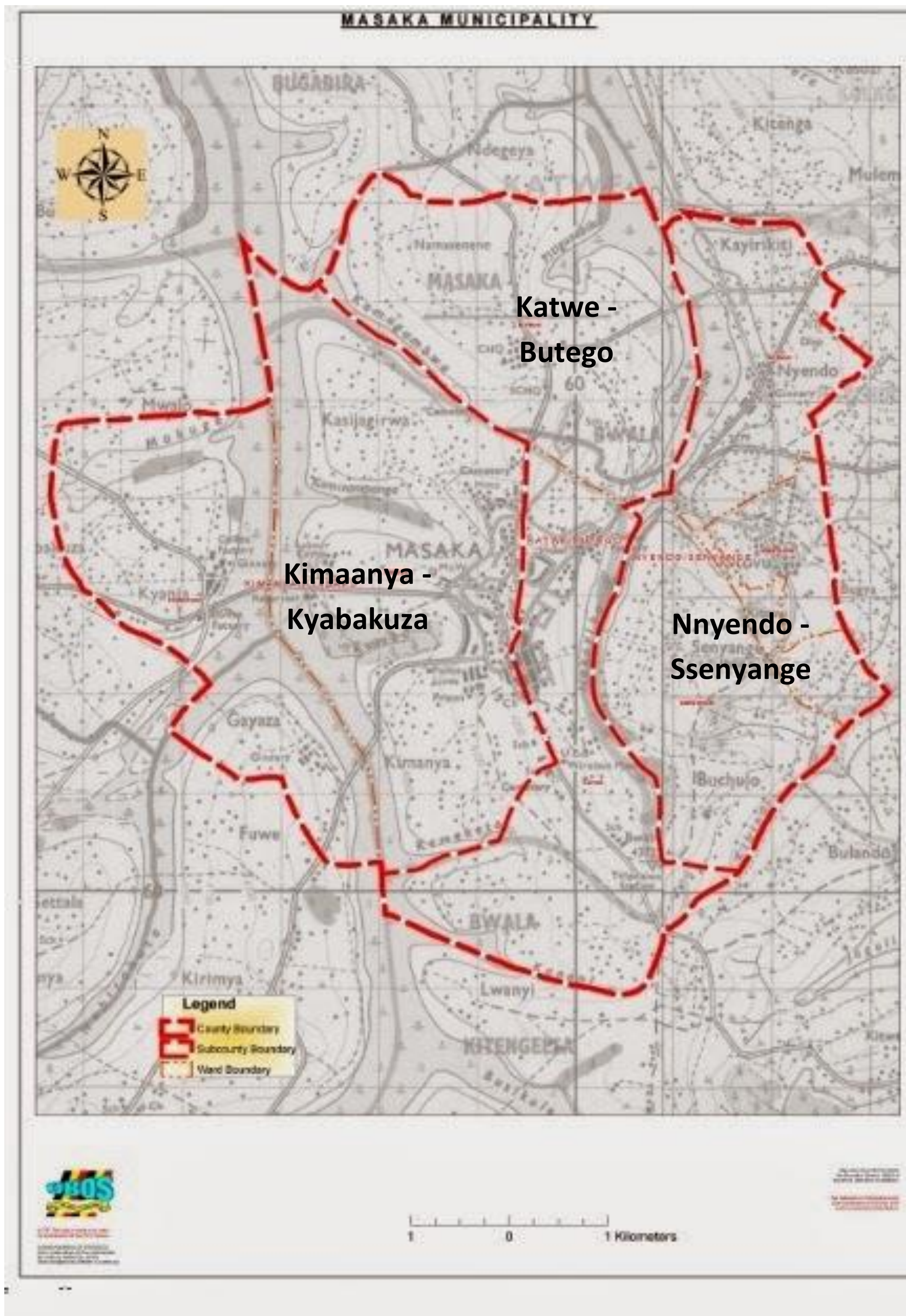
*Table for Determining Sample Size of a Known Population*

| N | S | N | S | N | S | N | S | N | S |
|---|---|---|---|---|---|---|---|---|---|
| 10 | 10 | 100 | 80 | 280 | 162 | 800 | 260 | 2800 | 338 |
| 15 | 14 | 110 | 86 | 290 | 165 | 850 | 265 | 3000 | 341 |
| 20 | 19 | 120 | 92 | 300 | 169 | 900 | 269 | 3500 | 346 |
| 25 | 24 | 130 | 97 | 320 | 175 | 950 | 274 | 4000 | 351 |
| 30 | 28 | 140 | 103 | 340 | 181 | 1000 | 278 | 4500 | 354 |
| 35 | 32 | 150 | 108 | 360 | 186 | 1100 | 285 | 5000 | 357 |
| 40 | 36 | 160 | 113 | 380 | 191 | 1200 | 291 | 6000 | 361 |
| 45 | 40 | 170 | 118 | 400 | 196 | 1300 | 297 | 7000 | 364 |
| 50 | 44 | 180 | 123 | 420 | 201 | 1400 | 302 | 8000 | 367 |
| 55 | 48 | 190 | 127 | 440 | 205 | 1500 | 306 | 9000 | 368 |
| 60 | 52 | 200 | 132 | 460 | 210 | 1600 | 310 | 10000 | 370 |
| 65 | 56 | 210 | 136 | 480 | 214 | 1700 | 313 | 15000 | 375 |
| 70 | 59 | 220 | 140 | 500 | 217 | 1800 | 317 | 20000 | 377 |
| 75 | 63 | 230 | 144 | 550 | 226 | 1900 | 320 | 30000 | 379 |
| 80 | 66 | 240 | 148 | 600 | 234 | 2000 | 322 | 40000 | 380 |
| 85 | 70 | 250 | 152 | 650 | 242 | 2200 | 327 | 50000 | 381 |
| 90 | 73 | 260 | 155 | 700 | 248 | 2400 | 331 | 75000 | 382 |
| 95 | 76 | 270 | 159 | 750 | 254 | 2600 | 335 | 1000000 | 384 |

*Note: N is Population Size; S is Sample Size* *Source: Krejcie & Morgan, 1970*

**APPENDIX V: INTRODUCTORY LETTER**

## APPENDIX VI: A MAP OF DIVISIONS IN MASAKA MUNICIPALITY




**Source:** *UBOS,(2018).*