THE ROLE OF MICROFINANCE INSTITUTIONS ON THE GROWTH OF SMALL AND MEDIUM SCALE ENTERPRISES (SMES) IN KYAZANGA SUB COUNTY, LWENGO DISTRICT.

CASE STUDY: KYAZANGA KWEGATTA MICRO FINANCE

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A RESEARCH DISSERTATION SUBMITTED TO THE FACULTY OF BUSINESS ADMINSTRATION AND MANAGEMENT IN PARTIAL FULFILMENT FOR THE REQUIREMENT FOR THE AWARD OF A BACHELORS DEGREE OF BUSINESS ADMINSTRATION AND MANAGEMENT OF

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DEDICATION

I dedicate my piece of work to my beloved parents, Mr. and Mrs. Mugabi Isaiah for their good support to me throughout the course and for their long lasting desire to see me succeed in life.

Secondly to my brother, sisters and friends for their encouragement they have given me to go on.

Thanks a lot and may the good Lord reward you abundantly.

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I wish to extend my gratitude to all the people who assisted me in the accomplishment of this study. May the good Lord reward your efforts.

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TABLE OF CONTENTS

LIST OF TABLES

LIST OF FIGURES

LIST OF ABBREVIATIONS

MFIs	Micro Finance Institutions
SMEs	Small and Medium Scale Enterprises
KKMF	Kyazanga Kwegatta Micro Finance
GDP	Gross Domestic Product
%	Percentage
UN	United Nations

ABSTRACT

Small and Medium Enterprises (SMEs) play an important role in the socio-economic development of any country. They provide an appropriate channel for the achievement of national macroeconomic objective in terms of employment generation at low investment cost and enhancement of apprenticeship training.

The role of Microfinance institutions on the growth of small and medium scale enterprises in Kyazanga sub county in Lwengo district.

The objectives of the study where to determine the effect of MFIs on the growth of SMEs capital in Kyazanga Sub county, to examine the effect of MFIs on the growth of SMEs human resource in Kyazanga Sub county, to examine ways of how MFIs can improve on the performance SMEs in Kyazanga Sub County.

The study used a sample of 250 respondents out of whom 100 responded. Data analysis was done using SPSS version 20.0.

The study established that the entrepreneurs in the study area accessed different amounts of loan. The study also established that accessibility to microfinance affected the performance of SMEs to a great extent. On the influence of savings and deposits to financial performance of SMEs, the study established that savings allowed the SMEs a chance to borrow from the banks and also measured their revenue generation capacity. The study also established that entrepreneurial development played a key role in the performance of SMEs. The study concluded that the accessibility of credit from credit facilities affects the performance of the SMEs to a very great extent.

The study concluded that the some of the SMEs trader have been able to make savings while others have not through their respective MFIs. The study also concluded that the training has improved the management skills of the SMEs owners in financial management, record keeping and business management.

This study therefore recommended that the management of MFIs revise their lending policies and requirements so as to ensure that most of the traders can be able to access credit more easily. The study also recommended that the MFIs use that traders savings as part of collateral since most may not have large tracts of land or the physical collateral needed. The study also recommended that the training on investment monitoring be offered more hours since it was established that the traders had not improved their skills in the area.

CHAPTER ONE

INTRODUCTION

1.0 Introduction

This study focused on Micro roles of Micro Institutions on the growth of SMEs in Uganda with Kyazanga Kwegata Micro Finance.

Many Non-Government organizations and other government organizations have struggled to make sure that small and Medium Enterprises (SMEs) flourish. Despite their efforts and the different political campaigns to end the poverty endemic, these efforts have realized both positive and negative impacts. This study therefore will explore the relationship between credit financing and the growth of small and Medium Enterprises (SMEs).

This chapter gives the background of the study, statement of the problem, purpose of the study, objectives, research questions, scope of the study, significance of the study and the conceptual framework. In the recent years, many authors have emphasized on the role of Micro Finance Institutions on the growth and the general performance of Small and Medium Enterprises (SMEs).

1.2 Background of the study

1.2.1 Historical Background

Microfinance is not a new concept. It is dates back in the 19th century when money lenders were informally performing the role of now formal financial institutions. The informal financial institutions constitute; village banks, cooperative credit unions, state owned banks, and social venture capital funds to help the poor. These institutions are those that provide savings and credit services for small and medium size enterprises. They mobilize rural savings and have a simple and straight forward procedure that originates from local cultures and are easily understood by the population (Germidis et al., 1991). Maloney, 2003 stated MFIs funds are to finance the informal sector of SMEs in developing countries and SMEs are more likely to fail (Maloney, 2003). The creation of SMEs generates employment but these enterprises are short-lived and consequently are bound to die after a short while causing those who gained job positions to lose them and even go poorer than how they were. It is not until recent that microfinance had gained recognition thanks to the noble prize winner Yunus Muhammad of the Grameen Bank. (Levine, 2005)

Kelly (2010) noted that microfinance is not a panacea but it is a main tool that fosters development in developing countries. Banks do not lend to them because they do not have what is required to be granted a loan or to be provided with the bank services. The lack of financial power is a contributing factor to most of the societal problems. These problems emanate from poverty and it is known that with poverty one is bound to suffer so many consequences ranging from lack of good health care system, education, nutrition, Microfinance has proved this bank concept to be wrong. They target the poor who are considered risky but the repayment rate turns to be positive as compared with the regular commercial banks (Zeller and Sharma, 1998). Researchers have viewed microfinance in different dimensions. Microfinance gives people new opportunities by helping them to get and secure finances so as to equalize the chances and make them responsible for their own future. It broadens the horizons and thus plays both economic and social roles by improving the living conditions of the people (Microfinance Radio Netherlands, 2010). These improvements are in a nutshell to alleviate poverty, and according to this project, it will be focus the development of small and medium size enterprises SMEs and focusing mostly in the rural areas.

1.2.2 Contextual Background

Small and Medium Enterprises (SMEs) play an important role in the socio-economic development of any country (Baumol, 2008). They provide an appropriate channel for the achievement of national macroeconomic objective in terms of employment generation at low investment cost and enhancement of apprenticeship training (Beck, Demirguc-Kunt, Laeven and Levine, 2008). SME contributes to the national objective of creating employment opportunities, training entrepreneurs, generating income and providing a source of livelihoods for the majority of low income households in an economy especially for developing countries (Beck, Demirguc Kunt & Levine, 2005). Availing financial services to SMEs plays a key role in determining how they conduct their businesses as they need a range of enabling and sustaining financial services in order to enable them effectively exploit abundant resources in their field of specialization in order to realize their full potential.

The Microfinance industry has become a major backbone in the sustenance and survival of SMEs. Microfinance Institutions (MFIs), as part of their core business, provide credit to SMEs (Abiola, 2011). In addition to these financial services, MFIs also provide non-financial services like business training, financial and business management to help improve the capacity of their clients in managing the loan resources granted them. In addition to financial intermediation, some MFIs provide social intermediation services such as the formation of groups, development of self confidence and the training of members in that group on financial literacy and management (Ledger wood, 2009). Financial services provided to SMEs include financial products and services such as savings, credit, insurance, credit cards, and payment systems. According to Ogujiuba Ohuche & Adenuga (2004) the predominant credit facility available to small and medium scale business in Nigeria is bank overdraft, and short-term loans (asset based loans).

Phillips and Kirchhoff (1989) cited by Pasanen (2006) found that young firms that grow have twice the probability of survival as young non-growing firms. It has been also found that strong growth may reduce the firm's profitability temporarily, but increase it in the long run (Pasanen, 2003a). The growth of SMEs is believed to be a desirable end as the key drivers of employment and economic development.

Small and medium scale firms play important roles in the process of industrialization and economic growth. Apart from increasing per capita income and output, SMEs create employment opportunities, enhance regional economic balance through industrial dispersal and generally promote effective resources utilization considered critical to engineering economic growth (Tagoe, 2005). However, the seminal role played by SMEs not withstanding their development is constrained by inadequate funding and poor management.

The unfavorable macroeconomic environment has also been identified as one of the setbacks encouraging financial institutions to be risk-averse in funding small and medium scale businesses (Ray, 2008). Small and Medium Enterprises have huge potential for employment generation and wealth creation in any economy, yet the sector has stagnated and remains relatively small in terms of its contribution to GDP or to gainful employment (FSD Kenya, 2007).

1.2.3 Conceptual Background

The term "micro finance" refers to the activity of the provision of financial services to clients who are excluded from the traditional financial system on account of their lower economic status (Emily Shepard 2011). These financial services will most commonly be in the form of loans and savings, through some micro finance institutions who will offer other services such as insurance and payment services. According to CBN (2004), micro finance is a development tool used to create access for the economically active poor to financial services at a sustainably affordable price.

Micro finance is about providing financial services to the poor who are traditionally not served by the conventional financial institutions. Accessing financial services by the poor enables them to have control over factors of production, be more self-reliant, generate employment, enhance household income and create wealth.

Three features distinguish micro finance from other formal financial sector. They are, the smallness of loans advanced, the absence of asset based collateral and simplicity of the operation. Therefore, micro finance is about providing finance to small scale enterprises. Looking at the emerging theory of micro-finance, recent developments in developing countries have reinforced the contention that micro finance structures are essential for development of rural areas in consideration of the fact that areas of development in these countries have been traditionally urban-centered (Iheduru, 2002). The development of micro finance institutions over the last few decades and its success have shown that micro finance is a major stimulus for combating poverty. Therefore, micro finance as a strategy for economic development should target the poor given its multiplier Role on production and marginal propensity to consume. Access to credit by this group of people accelerates their income and equally increases their savings and consumption.

Stakeholders including researchers are yet to reach any consensus on what constitute a small-scale business. Nzelibe (1991) using the position of United Nations Industrial Development Organization (UNIDO) states that a small business is characterized by localised area of operation, capital supplied by the owner with policy decisions held by individual or small group of entrepreneurs, owner's participation in all decision-making and daily operations, and owners managers.

Financial performance is a measure of how well an organization can use assets from its primary mode of business and generate revenues (Greenwood & Jovanovic, 1990).
Financial Performance Ratios is used to measure the financial performance of a business. A financial ratio is an important tool for businesses and managers to measure the progress for achieving the targeted goals. Some of the important financial ratios which a firm would like to analyze include: liquidity ratio, profitability ratios, and financial leverage ratios among others. It is also used as a general measure of a firm's overall financial health over a given period of time, and can be used to compare similar firms across the same industry or to compare industries or sectors in aggregation (Jayawardhera & Foley, 2010).

According to the findings of a study by Joeveer (2006), bank loans have a significant positive Role on most performance indicators of Small and medium sized enterprises (SMEs) in the transition economies. Microfinance encompasses the provision of financial services and the management of small amounts of money through a range of products and a system of intermediary functions that are targeted at low income clients (Asiama, 2007). A major barrier to rapid development of the SME sector is a shortage of both debt and equity financing. Accessing finance has been identified as a key element for SMEs to succeed in their drive to build productive capacity, to compete, to create jobs and to contribute to poverty alleviation in developing countries.

Beck, Demirguc-Kunt, and Maksimovic (2004) determined the financing obstacles faced by firms in over 10,000 sampled firms from 80 countries established that SMEs are faced with higher financing constraints than larger and older firms as part of the reason that limits their growth. In addition, small and medium enterprises have been forced to make extensive reports to financial institutions when applying for finances and at the same time, agree with more restrictive asset usage (Zeller and Sharma, 2010). In Uganda, although there is no reliable data to show that productivity in the SME sector has improved, the sector is still faced with a number of constraints with lack of credit availability as the principal one. The situation in Uganda is not that different from the rest of the world. Credit is the largest element of risk in the books of most banks and failures in the management of credit risk. Credit risks have contributed too many episodes of financial instability (Bakht, 2008) in relation to the small and medium enterprises in the long run (Tagoe, 2005).

Generally, the stage of development of SMEs in Uganda and the efficiency of the sector varies in the different locations of the county. Microfinance institutions recognize the importance of promoting SMEs as the basis of economic growth (Das, Shil and Pramanik, 2006). As a result, several MFIs have been established to enhance the development of SMEs and they include The Micro fiancé support center, Kyazanga Kyegatta Micro finance and others. Hence, this study aims to establish the Role of MFIs on the growth of SMEs in Uganda.

Furthermore firm’s growth in general refers to the increase in size (Emily Shepard 2011). In research, firm’s growth has been operational zed in many ways and different measures have been used. ((Pasanen, 2006). This may be one reason for the contradictory results reported by previous studies, though other explanations have also been presented (Delmar, Davidsson and Gartner, 2003). One of the typical measures for growth has been change in the number of employees. However, it has been found that these measures, which are frequently used in the SME context, are strongly inter-correlated (Pasanen, 2003). Growth can also serve as an instrument for increasing profitability by enlarging the firm’s market-share. Other similar goals include securing the continuity of business in the conditions of growing demand or achieving economies of scale. Further, growth may bring the firm’s new business opportunities, and on a larger scale growth enhances the firm’s credibility in the market. Also, achieving a higher net value of the firm can be regarded as a motive for growth (Pasanen, 2006).

1.2.4 Theoretical Background

According to Financial Sector Deepening (FSD) Journal (2007), Small Medium Enterprises (SMEs) employ between 1-99 people each and the sector is characterized by small scale level of activity, self employment, with high proportion of family workers and apprentices, little capital and equipment, labour intensive technologies, low skills and low level of access to organized markets. The development of SMEs is believed to be a desirable end as the key drivers of employment and economic growth. However, the growth of SMEs has been hampered due to great difficulties encountered when raising capital because of the pre-occupation of the microfinance institutions with collateral based lending (Hossain, 2010).
Microfinance as pioneered in Bangladesh by Mohammed Yunus was to assist low-income women and men through micro-enterprises for their economic development. Growing concerns about poverty stands out in political agendas all over the world, as stubbornness of

poverty even in the richest nations is being met with increasing impatience (Mwangi et al,1998). Governments and international aid donors have been subsidizing credit to small farmers in rural areas of many developing countries. These subsidized credit from donor Non-Governmental Organizations (NGOs) made it possible for large numbers of low-income people to have access to financial services.

Most of the finances available to the rural areas in Africa are through Microfinance, this method was known as traditional savings in most of the communities across the continent. According to (Aghion and Morduch, 2009), the African experience suggests that MFIs have built on pre-existing informal sector mechanisms (among the many examples are *Pride micro finance)* to create viable channels for capital infusions from formal sector banks, donors, and governments. As a result, deposit taken MFIs, informal microfinance institutions and credit only MFIs have all developed increasingly close ties with full-fledged commercial banks and other non-bank financial institutions in the formal sector.

Banks and MFIs complement each other well by servicing substantially different client bases. Banks lend and collect deposits mostly from a limited formal private sector in Africa to the government, while MFIs service poor and rural households, and small entrepreneurs often in the informal sector. (Beck *et al.*, 2004).

1.3 Statement of the Problem

In many cases, bank lending has been a prime source of credit to SMEs. However, with the current economic downturn, the credit relationship between banks and SMEs has been associated with a lot of risk, and in order to mitigate these risks, banks all over the world have used strict financing rules and collateral in financing SMEs growth (Beck *et al.*, 2004).

Bakht (2008) carried out a study on the challenges facing SMEs in Bangladesh and he acknowledged that insistence on collateral security adversely affected the growth of SMEs and the interest rates charged were prohibitive.

Tagoe (2005) conducted a study on the burden that SMEs faced in getting financial approval in Ghana. The study found out that the financing of the enterprises were strict and there was a high demand for collateral among financial institutions. In addition, there were long procedural issues such as a lot of paperwork, collateral security and high processing fees and prepayment charges, issues that affected the growth of SMEs.

Many studies have also been done in Uganda on the financing of SMEs. Some of the studies included Atieno (2011) and Nyarko (2005) empirical findings. Atieno (2011) aimed at empirically analyzing the credit policies on SME in the rural markets and their Role on SME’s growth and performance. Nyarko (2005) evaluated the financial challenges facing urban SMEs growth under financial sector liberalization in Uganda in accessing credit. In this regard, the studies excluded some important factors on the Role of MFIs services which are critical for SMEs growth, performance and therefore success. This is because there are a number of factors which interact to lead to SMEs performance such as working capital, the skills of its human resource and the satisfaction of their financial needs with the assistance of MFIs (Pasanen, 2003). It is in this context that this study was conducted primarily to address the research gaps in the Role of microfinance institutions in financing the growth of SMEs in Uganda. Lack of adequate finance from microfinance institutions is one of the most prominent issues facing SMEs seeking to expand and sustain their growth. The shortage of long-term finance was considered to be a major long-term constraint on SMEs growth and expansion plans. Most SMEs rely too heavily on short-term loans from banking institutions, which are more expensive and therefore increase the risk of failure due to strict financing rules and procedures (Nyarko, 2005). For SMEs, equity financing from MFIs could be more appropriate for their growth and expansion.

MFIs play an important role in the growth of SMEs in Uganda through provision of credit facilities like loans however in Kyazanga Sub County this growth is not yet realized by most SMEs (UBOS, 2006). Therefore this research will be aiming at investigating the role of SMEs performance of SMEs in Kyazanga Sub County with the case study of Kyazanga Kwegatta Micro Finance in Kyazanga Sub County Lwengo District as case study.

1.4 General Objective

To examine the Role of MFIs on the growth of SMEs in Kyazanga Sub county in Lwengo District.

1.4.1 Specific Objectives

The study was guided by the following research objectives:

- To determine the Roles of MFIs on the SMEs working capital in Kyazanga Sub county in Lwengo District.
- To examine the Role of MFIs on SMEs human resource in Kyazanga Sub county in Lwengo District.
- To examine MFIs contributions on the financial performance SMEs in Kyazanga Sub County in Lwengo District.

1.5 Research questions

1. What are the Roles MFIs on the SMEs working capital in Kyazanga Sub County in Lwengo District?
2. What is the Role of MFIs on SMEs human resource in Kyazanga Sub County in Lwengo District?
3. How MFIs contribute to the financial performance of SMEs in Kyazanga Sub County in Lwengo District?

1.6 Justification of the study

In trying to justify why the study is important, it is vital to mention that researchers have found this area of study very important to the development of the socio-economic activities in developing countries and their contributions to the development of small and medium size businesses in Uganda.

This research therefore focused on Role of MFIs on the growth of SMEs in Kyazanga Sub County in order to fulfill the requirement for bachelor of Business administration and management of Uganda Martyrs University

A study of this nature is equally very important because it is going to enlighten the government and the public on the role MFIs is playing in the SMEs sector. Microfinance as a whole provides the rural population a means to have access to financial services in their localities to boost their living standards in a sustainable manner in line with the millennium development goals of alleviating poverty in developing countries. They can contribute in the fight against poverty by improving the agricultural sector which is the main source of living to the inhabitants of such developing nations. Thus it will pave a way forward for potential to other stakeholders wishing to help in the sustainable development of SMEs to understand the difficulties they may come across and how they can succeed in their endeavors through accessing financial services from MFIs.

1.7 Scope of the study

1.7.1 Geographical Scope

The study was carried in Kyazanga Sub County which is found in Kyazanga Sub county Kyazanga Town council located in Lwengo District. The study will cover Kyazanga Kwegatta Micro Finance employees and customers of the same institution. Lwengo District is located in western part of Uganda, it is bordered by Sembabule District to the north, Bukomansimbi District to the northeast, Masaka District to the east, Rakai District to the south, and Lyantonde District to the west. Lwengo, the district headquarters, is located 45 kilometers, by road, west of Masaka, the nearest town.

The researcher selected Kyazanga Kwegatta Micro Finance since it was considered seeks to explain and analyze its implications and the role of microfinance institutions in Kyazanga Sub County.

1.7.2 Subject Scope

This involved collecting and analyzing of data in relation to the Role of micro finance institutions on the performance of SMEs in Kyazanga Sub County and more emphasis was put on, determining the Role of MFIs on the growth of SMEs capital in Kyazanga Sub county, examining the Role of MFIs on the growth of SMEs human resource in Kyazanga Sub county, investigate ways of how MFIs can improve the financial performance of SMEs in Kyazanga Sub county.

1.7.3 Time Scope

The study was done in a period of one and half year (November 2014, May 2016). The study used this range of one and half years since it was long enough to help the researcher establish the relationship between the study variables Micro finance of institutions and performance of

SMEs in Kyazanga Sub county in Lwengo district with KKMF as case study and to collect the required data for the research as well as writing the final research report.

1.8 Significance of the study

The management of microfinance institutions would be interested to know the contribution of this sector to SMEs economic development.. This study can therefore help the MFIs know how effective and efficient they have been towards the economic development of SMEs.

The capital required in operating SMEs is limited in supply and very few of them have access to it considering the type of collateral security required by the MFIs or banks which must be fulfilled before granting loans. Since financial institutions act as intermediaries between surplus and deficit of the SMEs, at the end of this research SMEs entrepreneurs can be able to know some sources of finance and choose the best available option.

The study can create an awareness of the role of MFIs on SME growth. The results from the study will also help the employees of MFIs understand the SMEs sources of finance, the role of MFIs in SME growth and identify ways of improving the microfinance financing activities.

Research findings can make a great contribution to the world of academia as researchers in the area of microfinance and SMEs growth. The findings can act as a point of reference.

1.9 Conceptual Framework

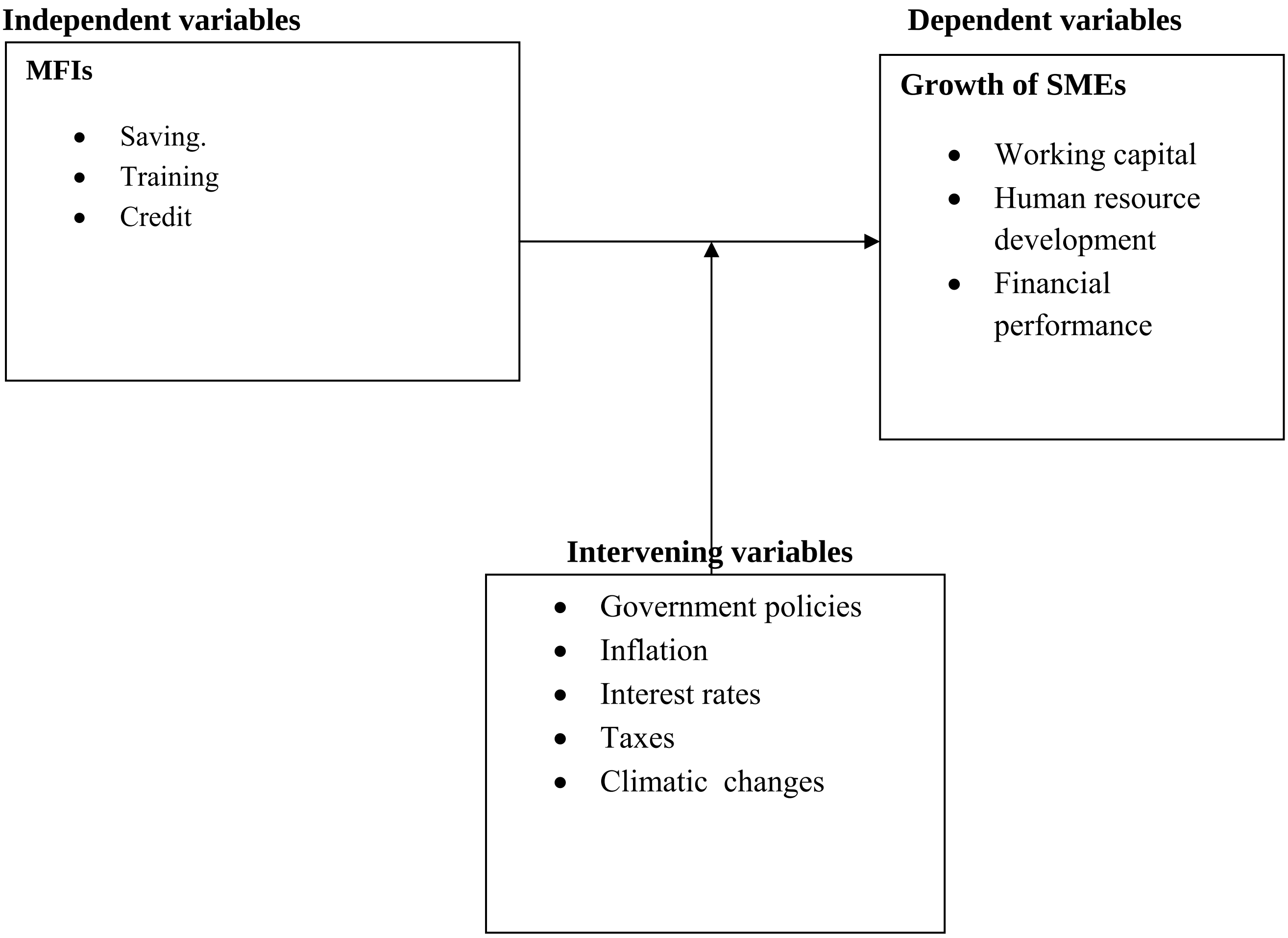


Figure 1: conceptual frame work

In order to understand the role of microfinance institutions on their clients to the growth of SMEs a conceptual framework has been developed, which is shown above. This has been developed based on an initial literature review undertaken on the roles of MFIs(savings, training of clients, lending money to customers) on the growth of SMEs(working capital, human resource development, financial performance of SMEs. .The conceptual framework consists of s there major components; MFIs, growth of SMEs and the social economic conditions of clients, government polices services, and small businesses characteristics and the clients' wellbeing.

First, the MFIs services are the driving force of the socioeconomic development of poor people and poverty reduction. The financial services of microfinance are generally known as the credit and saving, insurance, payment and repayment services (Ledgerwood, 2009). Loan is a main product of microfinance institutions which refers to the small amount of credit given to poor people at reasonable interest for generating income through self-employment. The terms of the given loan are important determinants to the SMEs continue survival and household improvement and their businesses' performance. For example, increasing the size of the given loan is important for extend the market and the size of micro and small enterprises. The flexibility of loan disbursement which includes the facilities of easy access to services, time responsiveness and providing adequate information about the terms of service is important determinants for improving the clients' wellbeing. Moreover, the flexibility of loan repayment policy which includes loan grace period, repayment period, and interest rate all are critical factors for determining the role of microfinance services on clients' wellbeing (Hulme, 2006; Ledgerwood, 2009; Robinson, 2011).

Saving service is another product of microfinance which takes two forms of mandatory and voluntary savings. The mandatory saving is referred to the value of savings that the clients of microfinance are required to save as a condition of obtaining future loan; while the voluntary savings is referred to the amount of savings kept by MFI clients which is not required as a condition of an existing to loan. Both of mandatory and voluntary savings are important for enhancing the capability of poor to cope with the uncertainty shocks and reduce the financial cost of lending and secure a sustainable fund sources (Ledgerwood, 2009; Robinson, 2011). The interest rate on the deposited savings of the clients has the power to help poor in accessing to large size of loans and consolidate their financial position.
In addition, the availability of accessing saving accounts helps poor clients to cope with uncertain shocks.

Second, the nonfinancial services such as enterprises development trainings are important factors to effectively use the financial services and advance the clients' wellbeing and their businesses' performance. The commercialization of microfinance institutions led to a massive competition in the arena of microfinance market. This competition forced microfinance institutions to develop and improve their products and services which lead to enhance the sustainability of those institutions through reaching a large size of clients. However, in order to achieve deep outreach, improving the quality of microfinance services and reducing the cost are required. The entrepreneurial and business developments trainings have been recognized as the engine of effectively use the financial services which lead to enhance the performance of the clients. Thus, embedded financial services with entrepreneurial and business development training are inevitable for creating successful entrepreneurs. Ledgerwood (2009) argues that microfinance is not a simple lender; it is also a development tool of human skills and capabilities. There are different types of business development and entrepreneurial training. However, this research traces the suggested trainings of Wickham (2011) which include a) business strategy training, b) plan training, c) marketing training, d) finance training, e) project management, f) time management, g) leadership, h) motivation, i) delegation, j) communication, k) negotiation .

Thirdly, social mediation service has been known as an important factor for facilitating the process of accessing to the financial services without collateral through building social capital between the group members. Social intermediation has been defined as a process in which investments are made in the development of both human resources and institutional capital, with the aim of increasing the self-reliance of marginalized groups, preparing them to engage in formal financial intermediation (Hulme, 2006). Group forming is important for both the lenders and the borrowers. The lenders attempt to reduce the cost of microfinance services through achieving a wide and deep outreach which required free physical collateral facilities while they want to mitigate the risk of asymmetry information. The group liability has shown to be a crucial approach to overcome the challenges of asymmetry information and mitigate the risk of adverse selection through peer monitoring and screening functions. In addition, the group members have the opportunities to easily access to loan services and extend the size of the required loan as well as sharing the information and improve the overall financial performance of the group members (Levine, 2005).

1.10 Definition of Terms and concepts

Capital. Capital can be defined as wealth or property in form of money or property, sometimes the basic sum in an investment enterprise (Ray, 2008).

Collateral Security. Collateral security is a property or something valuable which is used as guarantee that someone will repay such as property, insurance policy just to mention the few which the bank is authorized to take in the event of a customer defaulting in the loan agreement (Basu and Simon, 2011).

Economic Development. Economic development is defined as the structural transformation of all the economic indexes from a low to the high strata (Ray, 2008).

Economic Growth. Economic growth is defined as a sustained increase in a nation's gross national income per capital over a long time period (Hossain, 2010).

Entrepreneur. An entrepreneur can be defined as a person who sets and starts his own small business enterprise (Ray, 2008).

Financing. Financing is the process of sourcing for fund or acquisition of funds for financial purpose (Aftab, 2011).

Loan. Loan is the sum of money borrowed at an agreed rate of interest. It can be of long term or short term (Hossain, 2010).

Micro-finance. Micro-finance can be defined as a development tool used to create access to economically active poor to financial services at a sustainable and affordable price. MFIs fulfill their outreach mission by serving poor clients, and many operate as NGOs. Also, many MFIs are similar to banks because they are regulated or supervised by a regulatory body and/or because they collect deposits (Hulme and Mosley, 2008). The regulatory body is the Central Bank of Kenya (CBK).

Conclusion

Chapter one presents the background of MFIs and SMEs growth in Uganda. The chapter also outlined the specific objectives of this research, the importance of the study, the scope of the study as well as the working definitions of specific terms used in the report

CHAPTER TWO

LITERATURE REVIEW

2.0 Introduction

This chapter provides for the review of related literature extracted from various scholars, individual opinions and report findings. The chapter explores the concept of microfinance, availability of microfinance services, related information on the growth rate of small and medium enterprises, the effect of microfinance services on the growth of small and medium enterprises, challenges faced associated with small and medium enterprises. The chapter also presents the theoretical perspective of microfinance, the research gap as sated below:

2.1 Concept of Microfinance

Mbaguta, H. (2002) indicated that "Formal credit and savings institutions for the poor have also been around for decades, providing customers who were traditionally neglected by commercial banks a way to obtain financial services through cooperatives and development finance institutions". One of the earlier and longer-lived micro credit organizations providing small loans to rural poor with no collateral was the Irish Loan Fund system, initiated in the early 1700s by the author and nationalist Jonathan Swift. Swift's idea began slowly but by the 1840s had become a widespread institution of about 300 funds all over Ireland. Their principal purpose was making small loans with interest for short periods. At their peak they were making loans to 20% of all Irish households annually.

Meanwhile, starting in the 1970s, experimental programs in Bangladesh, Brazil, and a few other countries extended tiny loans to groups of poor women to invest in micro-businesses. This type of micro enterprise credit was based on solidarity group lending in which every member of a group guaranteed the repayment of all members. These "micro enterprise lending" programs had an almost exclusive focus on credit for income generating activities (in some cases accompanied by forced savings schemes) targeting very poor (often women) borrowers.

In the early 1900s, various adaptations of these models began to appear in parts of rural Latin America. While the goal of such rural finance interventions was usually defined in terms of modernizing the agricultural sector, they usually had two specific objectives: increased commercialization of the rural sector, by mobilizing "idle" savings and increasing investment through credit, and reducing oppressive feudal relations that were enforced through indebtedness. In most cases, these new banks for the poor were not owned by the poor themselves, as they had been in Europe, but by government agencies or private banks. Over the years, these institutions became inefficient and at times, abusive.

According to Mokaddem L (2009) explained that “microfinance always existed in Africa, albeit informal. Revolving credit associations, “tontines” were the first form of microfinance; credit unions rapidly expanded; and today the panorama is quite diverse, with individual lenders, self managed groups, cooperatives, N.G.Os, regulated MFIs, and even banks, providing a wide range of financial services”. However, an overwhelming majority of the economically active population, above all in rural areas, so far remains excluded from the formal financial system; and even those who have access to the system can still not get all the services they need. Historically, microfinance in Africa has developed in different stages across the region. Financial intermediaries such as cooperatives, rural and postal savings banks pioneered the industry in the 1970s, especially in West and East Africa. In the 1980s and 90s, the sector saw a number of donor-supported credit-only non-governmental organizations (NGOs) develop and sometimes transform into new types of non-bank financial institutions by the end of the 90s. Today West Africa is dominated by credit cooperatives, while regulated non-bank financial institutions stand out in East Africa, and Southern Africa is mainly served by a large**.** (Mokaddem L, 2009).

Development Initiative Africa Report (2010) stated that Micro Enterprises, small and medium enterprises are defined by basing on three main characteristics; these include number of employees, capital invested and annual turnover. Micro Enterprises are defined as enterprises that employ at least 4 people, with assets worth and annual turnover of 12 million Uganda shillings. Small Enterprises are defined as those enterprises that employ at least 50 people, with annual turnover of 360 million ($34,000) and Medium enterprise is defined as an enterprise that employs over and above 50 people with capital investment of over 360 million and turnover of 360 million.

2.2 Role of MFIs on the SMEs working Capital.

2.2.1 Economic Growth and Development of SMEs

Credit markets worldwide are characterized by asymmetric information, moral hazard problems and credit market failures. Among the borrowers, the poor are normally considered not bankable because of their lack of collateral, prospective income or credit record, and are therefore severely credit rationed. The inability of the poor to obtain credit contributes to a variety of problems such as: low levels of consumption, malnutrition, low investment in human capital, inadequate medical care and high level of indebtedness thereby increasing their vulnerability (Youssoufou, 2002).

The growth of microfinance reflects the expansion of informal sector activities. Large volumes of financial transactions are carried out by microfinance institutions, with little or no publicity around them. Their operations are not explicitly captured in official financial statistics and their activities are hardly reported by the mass media, yet their transactions roledirectly on a large section of the population especially the poor and the small scale enterprises (Pioty and Rekowski, 2008). Kenya's increasing population requires the production of goods and services on daily basis and funding is required for the production. The microfinance institution's operations are therefore expanding and have a prominent role to play in the development of small scale enterprises in Kenya. Since the microfinance institutions are financing the small scale enterprises in order to keep them in line; they also ensure that funds are made available and at the right time to the small scale industry (Youssoufou, 2002).

2.2.2 Increase Access to Finance

A major barrier to rapid development of the small scale enterprises is the shortage for both debt and equity financing. The ability to finance working capital is vital for SMEs growth. Parker and Torres (2004) found that a shortage of working capital was cited as the primary reason for 25 percent of the Kenyan microenterprises that terminated operations. Savings remains the most important source of finance throughout the business cycle. The survey conducted by Daniels, Mead and Musinga (2005) found that almost 95 percent of the interviewed entrepreneurs used savings as the primary source of working capital.

2.2.3 Enhances Savings

Among the sources mentioned above, personal savings are the most convenient source of financing to quite a number of people. Savings are defined broadly in this study to encompass the residual capital remaining after an entrepreneur has paid household living expenses and business operating expenses. Because of the unstable nature of the household economic portfolio, savings can be easily shifted between the household and enterprise. In many instances, savings from the business are transformed into household assets. These same assets may be transformed later to invest in the business. Alternatively, savings may be deposited into the business and withdrawn as needed by the household. Investment in the business usually reflects savings accumulation (Youssoufou, 2002)

Low-income entrepreneurs save but lack adequate liquid savings options. In this case, Microfinance institutions are uniquely positioned to target this market. Few microfinance institutions have developed a mechanism to collect voluntary savings. Many, however, require members to deposit into a mandatory savings account. This provides a source of security in case of loan default. Some institutions allow clients to deposit excess savings into their mandatory savings account. The willingness of clients to deposit mandatory and voluntary savings reflects their ability and willingness to save with microfinance institutions. The experience of MFI and its mandatory savings mechanism provides insight into the potential role of microfinance institutions to collect savings. Offering saving services would provide motivation for clients to retain membership. Entrepreneurs must always engage in some form of short-term or long-term savings (Banerjee and Duflo, 2007)

2.2.4 Increase on enterprise income

SMEs provide a vital source of employment and income in the society. According to UNESCO (2007) small businesses are characterized by few employees, few assets, and informal operations. The study also finds that the average income generated per month for these different microfinance beneficiaries was higher for participants who expanded their business using the microfinance loans as compared to those who did not. UNESCO (2007) also found that employed participants are generating more income by working for lesser number of hours as compared to the newly employed participants. This may be due to their work experience that the microfinance programme increases the economic prospects of the participants which help them to have an access and control over the household economic resources such as house, land, possession of gold and jewellery. In this way, entrepreneurs become financially independent.

Experiences of these programmes show that the provision of micro-credit and savings facilities when efficiently utilized enables the poor to build strong micro enterprises, increase their incomes and encourage participation in economic growth (UNESCO, 2007). MFI also contributes greatly to the empowerment of the poor, especially women and helps raise awareness and aspirations for education, health care and other social services. In light of these achievements, microfinance is increasingly being considered as 12 an important tool for poverty reduction. Vonderlack and Schreiner (2011) argue that the success of microfinance has been to supply production loans to women who run tiny business enterprises, thereby creating new market opportunities and increasing their bargaining power in the household.

2.2.5 Improve Household Welfare

According to Sengsourivong (2006), microfinance is a significant source of finance for the poor and the lower income people in developing countries. Sengsourivong (2006) found that microfinance could improve household expenditure. Morduch (1998 cited by Sengsourivong, 2006) argued that eligible households that get involved in microfinance programs have less consumption patterns compared to eligible households not involved in the MFI programs. Deferred consumption can be used to improve the welfare and social standing of a household. Savings may be applied to socially important festivities, such as weddings or community fundraisers, which build social capital. Patronage is another form of entrustment that can be considered an abstract form of savings accumulation. “Withdrawal” occurs in the form of future favours. Savings in the household are often devoted to the welfare of children. Investment in the younger generation reflects the hope for a better future.

Savings accumulation furnishes an important tool to generate business growth. Sengsourivong (2006) suggests that MFIs have a positive roleon household assets. Direct reinvestment of profits is one option. Investing savings in an intermediate form is another option (such as cash or in a bank account). There is evidence that entrepreneurs have a higher propensity to save than salaried workers (Huddle 1977). The marginal returns from reinvesting in enterprise development may be greater than the investment opportunities available to salaried labourers’. Savings enable entrepreneurs to pursue investments that yield higher rates of return. Many of these options would not otherwise be pursued, because of the associated risks. Dercom (2006) found that the higher the level of household savings, the lower the allocation of household resources to the cultivation of low value crops in Tanzania.

2.2.6 Risk Aversion

Risk aversion is an inherent, intrinsic and inseparable element of entrepreneurship (Rahman, Hossain and Miah, 2010). According to Johnson (2007), women entrepreneurs tend to prefer to follow an organic growth model in their businesses rather than obtaining finance from external sources. This tends to slow growth when the business becomes reliant on internally generated funds from cash flow and retained profits to fund their growth due to limited capitalisation (Okpara, 2011). However, young and educated entrepreneurs tend to have a higher level of risk-taking propensity and the need for achievement than average entrepreneurs, thus their willingness to take debt financing (Johnson, 2007).

According to the ILO report (2008), women stay clear of financial institutions because they lack information and are afraid of high transaction costs and interest rates, limited amount of finance, the lack of grace period in repayments and facilities tend to be short term in nature. This is supported by the Kenya Integrated Household Budget Survey report (2006) which reflected that the largest proportion of the entrepreneurs did not feel the need to borrow, followed by those who are unable to borrow due to inadequate collateral, and in the third position were those who do not like to be in debt. Entrepreneurs save using various forms-ranging from cash to informal savings and credit associations commonly known as pyramid schemes. These forms of savings reflect aversion to risks, such as inflation or seasonal income fluctuations, and the desire to improve household livelihood. Secure liquid savings options are often not available to low-income populations, especially those in rural areas (Dercom, 2006)

2.3 Role of MFIs on SMEs Human Resource skills.

2.3.1 Human Capital and SMEs Growth

Mel, McKenzie and Woodruff (2008) highlight the importance of human capital in a growth perspective. Mel et al. (2008) suggest that it makes the labour force more productive and adoptive towards new technology. The study indicates that knowledge and abilities are important in determining returns to capital. Most developing countries have low levels of human capital, in particular evident in the informal sector where people with poor education might see entrepreneurship as a last way out to earn an income. There are a number of NGOs offering business training to small and medium scale entrepreneurs in poor countries, though there are few academic studies that investigate the causal effect of entrepreneurial training on enterprise outcome. An important research issue is whether relevant training in business management, such as cost control, accounting, market analysis, marketing, and pricing strategies can stimulate investments in feasible projects and lead to growth and expansion in the long-term (Bjorvatn and Tungodden, 2010).

Klinger and Schundeln (2007) find that participation in business-training programmes significantly increases the probability of establishing new enterprises and expansion of existing businesses. However, the findings indicate that there are no impacts from business training on business outcomes, such as sales and profits. Further, by restricting the sample to mature enterprises, they partly ignore the role of financial constraints in entrepreneurial activity. Klinger and Schundeln (2007) find a positive relationship between age and the probability of launching a new business. One possible explanation is that younger entrepreneurs have relatively severe capital constraints compared to their older counterpart.

Karlan and Valdivia (2006) conducted a comparable study in Peru, where they implemented a business-training programme to micro entrepreneurs in two different cities, Lima and Ayacucho. Their study differs from the one by Klinger and Schundeln (2007) in several dimensions: First of all, Karlan and Valdivia examine the roleof providing business training to entrepreneurs with lower operation scale than in the case of Klinger and Schundeln. In addition, by restricting their sample to female microcredit clients, they investigate how injections of both human and financial capital affect the enterprise performance of a group with relatively severe financial and human capital constraints. Finally, the methodology differs in that Karlan and Valdivia conduct a randomised control trial to measure the average treatment effect of their programme.

2.3.2 Training and SMEs Profits

Karlan and Valdivia (2006) find that microfinance clients subjected to the training programmes are more likely to maintain a clean repayment record compared to untrained clients. They argue that this results from the improved business outcome, which on average is 16 percent higher for trained clients in terms of sales. The results are however not similar to other business outcomes such as profit margins and change in the number of employees. Nor are there significant changes in loan size and cumulative savings due to training. In a different study carried out by Henriken and Svoldal (2010) on the roleof providing business training to microfinance clients in Tanzania, the study uncovered that training was not reflected on the entrepreneur's profits. The general judgment was that business training leads to shifts towards business structures that are associated with higher profitability. This is because entrepreneurs with business training have more often become multiple-business owners (Karlan and Valdivia, 2006).

Second, the entrepreneurs offered business training have increased their engagement in commerce at the expense of engagement in manufacturing. Parallel to this, the bulk of indicators rank commerce as the most profitable sector and manufacturing as the least profitable sector, especially in terms of profit per working hour (Bennett, 2007). Taking into account working hours, it is therefore confirm that business training enhances movements away from the least profitable sectors and towards the sectors associated with higher profits (Legerwood, 2009). Any better predictors of the future business environment are however difficult to find, and the micro entrepreneurs are also restricted to the available market information when they evaluate the profitability of different business practices. In view of this, the entrepreneurs with business training have more often exploited the profit opportunity of operating successful businesses compared to the least profitable ones (Henriken and Svoldal, 2010).

The presence of people that have gone to school also eases the sensitization process, training on business development, loan utilization and repayment. This is because educated people would grasp the ideas faster than those with low education levels (Karlan and Valdivia, 2006). It was also found that the issues of expansion and diversification of businesses, asset accumulation, interest calculations were all found to be well understood and practised by educated people in the loan groups (Bennett, 2007). Microfinance institutions also provided training and skills development to enable the clients to plan, manage and evaluate investment, keep the record of all activities of the investment and also to utilize the loan more effectively.

2.3.3 Sensitization of Members

According to Karlan and Valdivia (2006), another service provided by the MFIs is that of sensitising the clients about their policy issues new products. This is where the clients are given information about new loans, saving procedures and any other new products from the MFIs. This enables the clients to benefit from the promotions and also diversify the investment portfolio. The clients are also sensitized about food security, HIV/AIDS and other health issues. It was established that most of the MFIs sensitize their clients about HIV/AIDS so that the necessary precautions are taken for the infected persons appropriately. For example, insurance cover and collateral details are emphasized so as to enable the MFIs not to lose the funds and for the family to benefit as well in case death occurred to the beneficiary. It was established that there is a cost for insurance cover in case of fire or the death of a partner that is provided to the family.

Karlan and Valdivia (2006) explains that this insurance cover ensures that the families do not suffer with the burden of paying back the loan but are given some funds as contribution towards the funeral arrangements of the dead client. In Uganda, there have been various fire outbreaks in the markets and MFIs have encouraged the traders who lost their goods that the insurance they took could cover for their losses. A case in point is in the capital city, Kampala, where St. Balikuddembe Market got burnt in February 2009. The traders who had loans from the MFIs were told they would not repay the old debt but could apply for a new one since their insurance had covered their misfortune and losses.

2.3.4 Entrepreneurial Skills

Some MFIs actively pursue strategies to teach about entrepreneurial skills. The fast growing economies and the ones with competitive capabilities have realized the importance of Human Resource Development (HRD) as of prior importance and therefore invest heavily in HR in the form of capacity building and acquisition of modern skills. Upgrading of the human skills can make SMEs remain competitive (Bennett, 2007). A survey report by OECD for determining the relationship between the training and SMEs competitiveness and productivity shows that the nature and roleof training and skills development in firms is viewed by firm managers as being an important contributor for firm's development. Small firms continue to have a preference for arranging their own trainings in line with their particular business needs (Henriken and Svoldal, 2010).

SMEs lack managerial skills, resources and experience to motivate the potential investors to invest with them. They view them as high risk business concerns and some well to do SMEs may be hindered from critical financing (Kanichiro and Lacktorin, 2010). SMEs and providers of debt and equity need to have a cordial relationship to avoid the problem of information asymmetry and their conflicts of interests. The MFIs in Cameroon fight to meet the aspirations of their customers by organizing trainings on book-keeping, auditing and providing supervisory techniques. These services are not offered by the regular commercial banks. These activities can have a significant roleon SMEs human resource development. Bennett (2004) also adds that the clients need to be trained so as to have the skills for specific production and business management as well as better access to markets so as to make profitable use of the financial resource that they receive.

2.3.5 Enterprise Development

In most developed and developing economies, SMEs still need both entrepreneurship development and financing support for them to grow. To support the development of SMEs, some governments, particularly in the developed world provide a comprehensive set of programmes through various agencies which are broadly categorized into financial assistance and business support services (Berger and Udell, 2006). These governments' financial assistance to micro enterprises comprises of soft loans, grants, equity financing, venture capital, guarantees and tax incentives. Governments in developing countries should follow suit. While, the SMEs business support services benefit from advisory services, awareness and outreach, strengthening skills of workforce, entrepreneur development, marketing, promotion, product development, quality accreditation and technology development (Rosli and Ghazali, 2007).

According to Ledgerwood (2009), some MFIs provide financial and social intermediation services such as the formation of groups, development of self confidence and the training of members in enterprise development. The services provided by MFI include: marketing and technology services, business training, production training and subsector analysis and interventions. Enterprise development services can be sorted out into two categories (Karlan and Valdivia, 2006). The first is enterprise formation which is the offering of training to persons to acquire skills in a specific sector such as weaving and as well as persons who want to start up their own business. The second category of enterprise development service rendered to its clients is the enterprise transformation program which is the provision of technical assistance, training and technology in order to enable existing SMEs to advance in terms of production and marketing (Bennett, 2007).
Entrepreneurship training can equip business owners with all the necessary tools that can hinder them from obtaining loans. Existing businesses with part of their capital being equity is preferred by most MFIs to work with since the level of involvement is high and consequently lower risk (Ledgerwood, 2009). Enterprise development services are not a prerequisite for obtaining financial services and they are not offered free of charge. These charges are sometimes subsidized by the government or an external party since to recover the full cost in providing the services will be impossible by the MFI (Bennett, 2007). The enterprise development services may be very meaningful to businesses but the roleand knowledge that is gained cannot be measured since it does not usually involve any quantifiable commodity. It has been observed that there is little or no difference between enterprises that receive credit alone and those that receive both credit packages and integrated enterprise development services (Ledgerwood, 2009).

2.4 MFIs contribution on the financial performance of SMEs.

2.4.1 MFI Support and Access to Credit

There have been several commitments that have been recorded in favour of promoting microfinance in the least developed countries as an intervention to alleviate poverty. The UN report (2005) has emphasized the importance of private enterprise as a driver of development, highlighting Africa's need to improve its investment climate and pledging to support the region by promoting increased access to finance including strong support for the development of microfinance in Africa. The UN also pledged that through actions by the relevant international financial institutions and African Governments they would increase access to financial services through increased partnerships between commercial banks and microfinance institutions, including through support of diversification of financial services available to the poor and effective use of remittances (United Nations, 2005).

The G8 members are supporting work on access to finance, microfinance and remittances. It has been reported that in the final declaration of the 2004 G8 Summit, leaders stressed microfinance's contribution in the continuum of services needed to support the economic fabric of developing countries (United Nations, 2005). The UN report observed that the G8 members affirmed their support by stating that; "Entrepreneurs, no matter how small, need access to capital". Microfinance programmes have provided small amounts of capital to entrepreneurs for many years benefiting women in particular. Sustainable microfinance can be a key component in creating sound financial market structures in the world's poorest countries. It is often the first step in launching SMEs, the beginning of what should be a continuum of credit access necessary to support the maturation of companies in developing countries (United Nations, 2005).

The Kenyan government has not established an outreach programme to support MFIs like the Ugandan government. It has been reported that the government of Uganda has designed and established a multi donor, private sector driven microfinance outreach plan to spread sustainable microfinance services to undeserved areas in Uganda (Developing a sustainable microfinance industry, 2005). This microfinance outreach plan has the aim of benefiting as many active rural poor as possible, in support of the government's objective of eradicating poverty and building a prosperous and stable nation (Developing a sustainable microfinance industry 2005). The vision of this microfinance outreach plan is to develop a coordinated, professionally efficient and sustainable microfinance industry providing affordable financial services especially to the rural Ugandans. The objectives of this microfinance outreach plan have been identified as increasing savings mobilization, assisting microfinance apex institution to support and build capacity of their member institutions, developing and building capacity in the microfinance training market and enhancing the rural population's capacity and business orientation to access financial services for income generation (Developing a sustainable microfinance industry, 2005).

2.4.2 Sustainability of SMEs

Funding the lack of funds sets SMEs back by limiting their growth and sustainability (Cook, 2011). UNIDO (2003) also argues that the growth and the competitiveness of women entrepreneurs have been hampered by the lack of funds, training skills and weak government infrastructure in promoting entrepreneurship projects. While the lack of the necessary training and education to seriously affect the efficiency of entrepreneurs, Boter and Lundstrom (2005) explains that unstable political and economic environment, complex taxation, corruption, poor laws, long waiting times for approval of licenses and registrations are common problems faced by entrepreneurs in most developing countries such as Kenya.

Luyirika (2010) carried out a study on the role of microfinance in the socio-economic development of women in a community in Mpigi Town Council in Uganda. As one of the ways of improving the financial assistance towards SMEs growth, the findings revealed that MFIs could increase the money given to their clients so as to allow them expand and diversify their investment opportunities, reduce the interest rates so that all the profits realized do not go towards paying the interest and also increase the grace period to allow the growth of the enterprise. Luyirika (2010) explains that small amounts of money given at a time affect the growth of the enterprises. It was also noted that there were too many deductions from the money disbursed initially yet the whole amount was paid back. The respondents reported that they paid even for what they had not received and what was annoying was the deductions made from the small amount given, thus the money given was lowered even more.

2.4.3 Increase Repayment Period

Luyirika (2010) indicates that short repayment period affects the flow of money from the business to the MFI. Eighteen percent of the respondents revealed that they had to borrow from other MFI to service the loans or risk the taking of their property by the MFI. The repayment period for some MFI was weekly while for others it was bi-weekly. For the respondents, this period was too short for any meaningful profits to have been realized from which to get money for repaying part of the loan. Twelve percent of the respondents also mentioned that at times it was difficult for them to fulfil the repayment schedules and they ended up defaulting. This could have been as a result of circumstances beyond their control like weather for farmers but the MFI would call them defaulters and confiscate their collateral property.

Any government interested in the development of their economy should be involved in the provision of regulations to govern the microfinance programs, the interest rate and safe guard the property of the SMEs. For example, the Kenyan government has failed to control commercial banks' interest rates, which are now prohibitively high. Furthermore, 22 the MFIs are requested to establish loan products for social problems like school fees, weddings and funerals, collaborate and share successes and failures of businesses, harmonize the service delivery. MFI can also elicit the support of SMEs owners in the repayment of money borrowed by colleagues (Armendariz, 2004).

Luyirika (2010) also suggests that the MFIs can continuously sensitize their clients on loan utilization and repayment and discuss with their clients before they confiscate their property. This is because the clients say that if given more flexible terms they would be able to pay back the loan. However, the challenge of MFIs support to business owners is the lack of flexibility from the MFIs when their clients fall sick, loose family members or are involved in accidents (Armendariz, 2004). The respondents who were ten percent explained that "borrowed money/loan did not know sorrow, did not know sickness, did not know death" in other words, whatever the situation of the client, the loan has to be serviced.

2.4.4 Group Lending

According to Armendariz (2004), group lending refers to the practice of working with clients in small groups (typically comprised of three to seven members). Loans are made to individuals, but the group as a whole is held jointly liable should repayment difficulties arise. Economic theorists have been particularly interested in group lending, and nearly all of the economic work on microfinance focuses on the incentives induced by joint liability in group lending contracts, building on lending models pioneered by microfinance leaders like Bangladesh's Grameen Bank and Bolivia's BancoSol (de Aghion, 2010).

This method of providing small credits to the poor is most used by MFIs that provide loans without collateral. The interest charged is far lower than interest charged by individual money lenders (Natarajan, 2004). The Grameen bank is a typical example of MFI using group lending method. The repayment rate is very high since each member is liable for the debt of a group member (Stiglitz, 2010). Group formation is made by members who know themselves very well or have some social ties. Loans are not granted to individuals on their own but to individuals belonging to a group which act as collateral. 23 This is to avoid the problems of adverse selection and reduce costs of monitoring loans to the members who must make sure the loan is repaid or they become liable for it (Armendariz, 2004).

According to Carlton et al. (2011), group-based lending schemes provide SMEs with an opportunity to build their social assets by reinforcing reciprocal relationships and social networks. Membership of microfinance groups links individuals, households and enterprises into a vital web of business and personal relationships that enables members to better cope with the challenges of life. However, in some cases membership to groups can also become a social liability, especially where there is a consistent pattern of nonpayment and mounting peer pressure (Natarajan, 2004). Access to financial services also allows SMEs to cope with shocks or economic stress events once these take place. SMEs use MFI loans to re-stock their businesses and to smooth consumption. As most MFIs offer only inadequate savings services, only few SMEs are able to use these as source of liquidity in times of emergencies (Armendariz, 2004).

2.4.5 Individual Lending

This is the lending of loans to individuals with collateral. Carlton et al. (2011) found that individual and group methodologies require different operational and financial structures. The choice of structure is based on organizational goals, profitability objectives, and risk tolerance.

Individual lending and group lending have different cost structures. For 24 instance, because of the increase in loan amount per client, some of the administrative costs on a per client basis would be lower; however, due to increase in the due diligence and monitoring costs which get translated into decreased case load per loan officer, costs on personnel might increase. Individual lending requires careful analysis on behalf of the lending institution prior to fund disbursement (Fotabong and Akanga, 2005).

According to Fotabong and Akanga (2005), individual borrowing may not necessarily mean increase in enterprise ownership in the short run. But as time goes, it may lead to greater enterprise growth. The ability to secure collateral helps the individual-based programs and the success of microfinance programs in general (Morduch and Aghion, 2010). Many of the large micro-finance institutions provide individual loans to clients who have a track record and have improved their economic status; the provision of individual loans to first-time borrowers is not common. Despite the challenges for individual loans, the need for such a product seems to be higher amongst the mature clients (Fotabong and Akanga , 2005).

2.4.6 Self-Help Groups (SHG)

The fundamental concept of SHGs is the creation and utilization of a group savings and resource fund to make low cost loans to its members. SHGs consist of low income individuals of a particular village who come together to address their common problems, including their need for access to financial services (Swain, 2007). SHGs are usually formed and supported by NGOs, Government Agencies or Banks, but they can even be formed through the sole initiative of members of a community and MFI (Kay, 2003). A prominent feature of SHGs is that they enable members to obtain small loans on a regular basis. This has created a trend of constant borrowing whereby members apply for new loans immediately following the repayment of previous ones. As such it is possible to infer that the poor population served by SHGs is becoming reliant on a continuous flow of microcredit (Swain, 2007).

The general findings of most evaluation studies on SHGs include increase in household income, improvement in asset position, increase in savings, increase in employment, increase in consumption expenditure and overall poverty reduction. The overall roleof 25 MFI on SHG is the alleviation of poverty (Swain, 2007). Poverty is a global phenomenon which in its simplest sense refers to the deprivation of basic human needs. The most conventional approach to poverty eradication is the promotion of economic growth (Roger and Robinson, 2002). In this regard, microfinance better equips SHG to cater to the needs of its target group and improve their standards of living. Microfinance through SHG improves the ability of the poor to face shocks such as illness, price fluctuations and natural disasters, thereby improving their risk management capability. On the whole the provision of financial services to the poor through SHG is believed to increase incomes and reduce vulnerability (Tankha, 2002).

SHGs are therefore one form of community organization which can be developed for a variety of purposes, both financial and non financial. SHGs can have positive effects on social harmony and justice as they bring people of different religions and ethnicities together to work towards a common goal (Kay, 2003). The most significant roleof SHGs however, is their roleon poverty alleviation which is also identified as economic empowerment. Apart from providing its members with much needed access to timely credit at considerably lower interest rates, Tankha (2002) explains that an SHG also promotes savings and yields moderate economic benefits, and reduces the dependence on moneylenders.

2.4.7 Village Banking

Village banking is a method of lending to individual members to have constant access to money for their Micro-enterprise daily transactions (Mk Nelly and Stock, 2008). Village banking is a microcredit organization designed to provide financial services to SMEs rather than formal financial institutions. Village banking has been brought about by MFIs as a way to control costs. Village banking offers several important services such as credit in the form of a loan to a group of approximately 15-30 individuals. Village bank provides members with an opportunity to save voluntarily, over and above the amounts the members are forced to save (Hatch and Hatch, 2008).

Village banks can and do reach remote households in rural areas (Mk Nelly and Stock, 26 2008). Strengthening and expanding the operations of village banks in remote areas may work better than trying to lure urban commercial banks into the remote areas. The lack of rural lending experience of these banks may constitute a formidable barrier to their entry into rural markets. A number of village bankers show impressive levels of performance through loan recovery and sustainability as a result of microfinance activities (Nelson et al., 2006).

Borrowers are uplifted using village banking because they own SMEs that earn money sustainably. This enables them to acquire a larger loan sum which gives them higher profit when introduced into the business and of course the interest with this high sum is high making the bank financially sustainable (Mk Nelly and Stock, 2008). Village banking as of 1990s gained grounds and certain adjustments were made to suit partner institutions (Nelson et al., 2006). Hatch and Hatch (2008) say that Village banking loan and savings growth rate increases as the banks continue to exist.

2.5 conclusions

This chapter reviewed literature on the effect of MFIs on the growth of SMEs. The first section determined the effect of MFIs on the growth of SMEs capital. The second section examined the effect of MFIs on the growth of SMEs human resource and the third section investigated the ways of how MFIs can improve their financial assistance towards SMEs growth. The next chapter deals with the research methodology

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter presents the research methodology and the profile of the study area. The key issues discussed in this chapter include the research design, data required and sources, data collection tools, sampling procedures, key variables and the analysis of the data. In addition there are issues on the physical characteristics, the economic and social characteristics as well as other relevant characteristics of the study region.

3.2Research Design

This research adopted a descriptive research design. A descriptive research design is a scientific method which involves observing and describing the behavior of a subject without influencing it in any way (Kathori 2006). In addition, a descriptive study attempts to describe a subject, often by creating a profile of a group of problems, people or events, through collections of data and the tabulation of frequencies on research variables and the research reveals who, what, when, where or how much (Saunders and Thornville, 2010). A survey in form of standardized questions in a questionnaire will be used to collect data. A survey is defined by Malhotra and Birks (2007) as a method of collecting data from people about who they are, how they think (motivations and beliefs) and what they do (Behaviour). Therefore, the study adopted a quantitative approach on the effect of MFIs on the growth of SMEs in Kyazanga Sub County. The independent variables included: effect of MFIs on the growth of SMEs capital, the effect of MFIs on the growth of SMEs human resource and the ways of how MFIs can improve their financial assistance towards SMEs growth.

3.3 The area of Study

The area of the study was Kyazanga Kwegatta micro finance in Kyazanga sub county Lwengo District. The study was conducted at Kyazanga Kwegatta micro finance in Kyazanga Sub county Lwengo district since the area has many SMEs that need support from MFIs in order to improve on their performance and growth.

3.4 Population of the study

According to Frankel and Wallen (2010) a population refers to the group to which the results of the research are intended to apply. They stated that a population is usually the individuals who possess certain characteristics or a set of features a study seeks to examine and analyze. Kumekpor (2002) emphasized this by defining a population as the total number of all units of the issue or phenomenon to be investigated into which is “all possible observations of the same kind”.

3.4.1 Sampling Techniques

The sampling technique used was purposive sampling method in the determination respondents of SMEs to be included in the study. The purposive sampling was used when the various sampling units satisfy certain criteria of interest. In this study, the chosen group was MFIs client’s entrepreneurs operating in Kyazanga Sub county. This minimized bias and simplified analysis of the results.

3.4.2 Sampling Size and Selection

The study will use a mathematical approach in the determination of the sample size for the research. The mathematical sampling approach was based on Miller and Brewer (2003) formula that is stated as follows:

$$n = \frac{n}{1 + N (\alpha) 2}$$

Where n = sample size n= 200

N = Population N= 100

α = margin of error. a = 0.

$$n = \frac{n}{1 + N (\alpha) 2} = \frac{200}{1+100(0.1)2} = 100 \text{ Respondents}$$

Kyazanga Sub County and community member's .These were selected using both stratified and purposive sampling techniques. Using the purposive sampling technique. The researcher selected 100 respondents from Kyazanga Sub County while the total sample size comprised of 200 respondents.

Under the study, sample size of 100 respondents was selected from the from Lwengo District to save both time and money during the process of data collection. This sample of 100 respondents was selected as in table below.

Table 1 : Showing Sample Size

Category	**Sample Size**	**Percentage (%)**
SMEs owners	30	30
Staff of Kyazanga SACCO	20	20
Clients of Kyazanga SACCO	30	30
Community members	20	20
Total	**100**	**100**

Primary Data 2016

3.5 Data Collection Method

The data collection techniques that were employed for the research included the use of structured questionnaires. The questionnaires were used for the collection of data from the entrepreneurs from SMEs in Kiambu sub-counties. The questionnaire will embody both open and closed-ended questions for randomly selected members of the various groups. A survey questionnaire was designed to apply to a heterogeneous sample selected from the large population of SMEs (Burns, 2010). A questionnaire is defined as a formalized schedule or form which contains an assembly of carefully formulated questions for information gathering (Wong, 2009). The questionnaire was structured in three broad areas that included general information, a rating on the effect of

MFIs on the growth of SMEs capital, the effect of MFIs on the growth of SMEs human resource and the ways of how MFIs can improve their financial performance towards SMEs growth.

3.6 Data Collection Procedure

A letter of introduction of the university was obtained from was obtained from the University after authorized by the supervisor to do.

The respondents were requested for their time prior to sending the actual questionnaire. A pilot test involving 5 respondents was carried out to evaluate the completeness, precision, accuracy and clarity of the questionnaires. This ensured the reliability of the data collection instruments used. After the amendment of the final questionnaire, the researcher explained the purpose of the research and sought permission from the institution to carry out the actual research. The final questionnaires were distributed to the respondents with the help of research assistants. This enhanced the speed of data collection. Each completed questionnaire was treated as a unique case and a sequential number given to each. Filling the questionnaire took approximately 10 minutes. The collected data was edited and entered into the Statistical Package for the Social Sciences (SPSS) software to enable the carrying out of the analysis.

3.7 Management and analysis

To ensure easy analysis, the questionnaires were coded according to each variable of the study. This study used descriptive and inferential statistics. According to Mc Danile (2011), descriptive analysis involves a process of transforming a mass of raw data into tables, charts, with frequency distribution and percentages, which are a vital part of making sense of the data. In this study, the descriptive statistics such as percentages and frequency distribution were used to analyze the demographic profile of the participants. In order to describe the data, the study used means of each variable and correlation analysis between the independent and the dependent variable.

3.8 Data quality control

3.8.1 Validity

Validity is the extent to which research findings can be accurately interpreted and generalized to other populations. The researcher analyzed the results of the content validity of the scale (Bennett, 2007). The items that have CVI over 0.75 will remain and the rest will be discarded. The remaining items were modified based on the expert's opinion. By discarding those items of the scale that will not be related to the domain of computer experience, the number of items decreased from 38 to 25.

3.8.2 Reliability

This is the degree of consistency of measure obtained from the instruments. It shows the degree of precision and how dependable the instruments appear in bringing out the data for the study. (Amin, 2005). Similarly the researcher used a pilot tested the questionnaire among 15 respondents to ensure reliability.

3.7 Ethical consideration

The researcher ensured the respondents that all data provided were kept with high degree of confidentiality and that the results obtained will be used purely for academic purposes only.

The researcher respected human dignity by not revealing the identity of the respondents in the study.

An introduction letter was obtained from the faculty of business administration and management of Uganda martyrs' University and this was presented to the respondents.

3.9 Limitation of the study and possible solutions

Time was not enough since the researcher had to do course works, and concentrating for exams and this led to inadequate data collection. However the researcher drafted a time schedule to ensure competences and accuracy of data collected.

Suspicious and failure to some of the clients to open the questions put before them as they think that the researches wants to use the data against the company, since the company considers some information confidential and therefore cannot release it. However the researcher provided an introductory letter.

The study was limited by funds as the researcher had no enough funds to cater for secretarial services and other research requirements. However the researcher got some financial support from her relatives that will support her during the research study.

In addition, the researcher faced a problem of not finding all respondents in the time of the study due to them being too busy with the organization work. The researcher however drafted the appropriate time table with the top University administrators that may suit all the respondents during the process of data collection for reliable and valid information.

CHAPTER FOUR

RESENTATION, ANALYSIS AND INTERPRETATION OF FINDINGS

4.0 Introduction

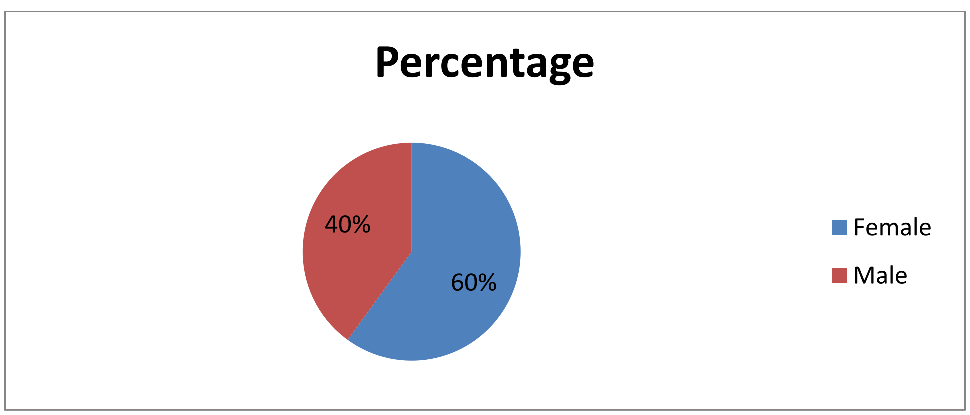
This chapter presents the findings on the effect of Microfinance Institutions on the growth of SMEs in Kyazanga Sub County. The findings were based on specific objectives of the study. The first section presents the findings on respondents' demographic profile, the second section presents the findings on the effect of MFIs on the growth of SMEs capital, the third section presents the findings on the effect of MFIs on the growth of SMEs human resource and the fourth presents the findings on how MFIs can improve their financial assistance towards SMEs growth. The response rate was 67% and was representative enough to answer the research objectives.

4.1 General Information

This section presents the general information on the respondents' age, gender, marital status, year of business establishment, educational level attained and the type of business.

4.1.1 Gender of Respondents

Figure 2: Gender of Respondents



Source: Primary Data, 2016

The researcher sought to find out the gender of the target respondents involved in the study. The findings in Figure 1 shows that majority of the respondents were female (60%) as compared to 40% males. This implies that at KKMF women has access to credit facilities than men. This according(Mk Nelly, 2008) who stated that Credit Programmes are specifically targeting struggling women entrepreneurs and farmers who have the willingness to pay back their loans as compared to their male counterparts. A female borrower will always meet her obligations to repay the loan on time (Mk Nelly, 2008).

4.1.2 Age of Respondents

Table 2. Age of Respondents

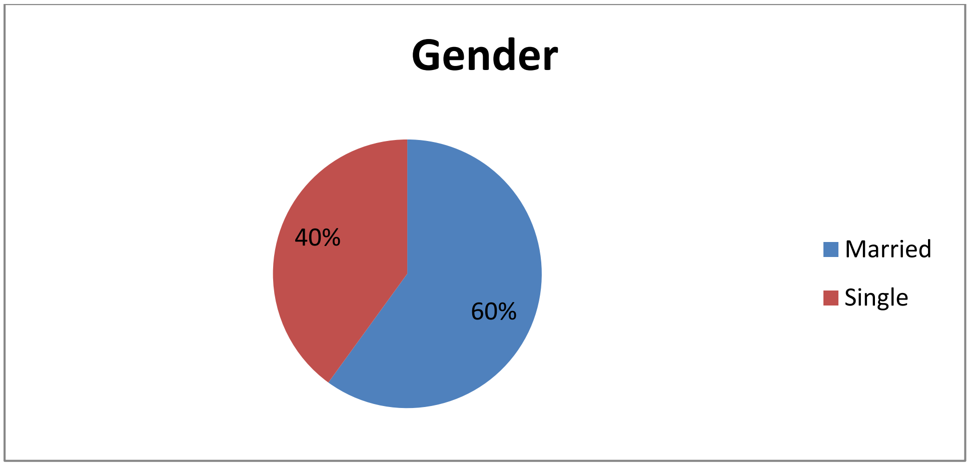
Age of Respondents	**Frequency**	**Percentage**
25-29yrs	10	10
30-39 yrs	30	30
40-49 yrs	40	40
50 yrs +	20	20
Total	**100**	**100**

Source: primary Data, 2016

Findings from table indicates majority 40% where between the age of 40-49 years, 30% were between 30-39 years, above 50 years and 10% were between 25-29 years. This therefore implies that people between 40-49years years have more access to MFIs in Kyanzanga Sub County followed by 30-39years. This is in line with Shahidur (1998) on study of micro finance institutions and repayment of bank loans in South Africa which concluded that people between the age of 41 years and above always access credit facilities because if many responsibilities they have.

4.1.3 Gender

Figure 3: Gender



Source: Primary Data, 2016

The results in Figure 2 two above shows that a majority of the respondents were married (60%) and 40 % were single. This implies that women have access to MFIs services than men at KKMF. In an interview with some customers they argued that family responsibilities and needs drive them to interact with financial institutions to make ends meet thus much loans according to study' establishment went to married clients because they cannot easily leave their homes to avoid loan repayments and in case one partner fails to pay, the other one is liable of payment more so other items like deposits are made most often by married persons compared to single ones.

This is in line with Nyarko, 2005 who argued that married people with regular sources of income to meet their daily expenses in their homes also pay loans in time though this is subject to the type of family

4.1.4 Level of education

Table 3: Respondents level of education

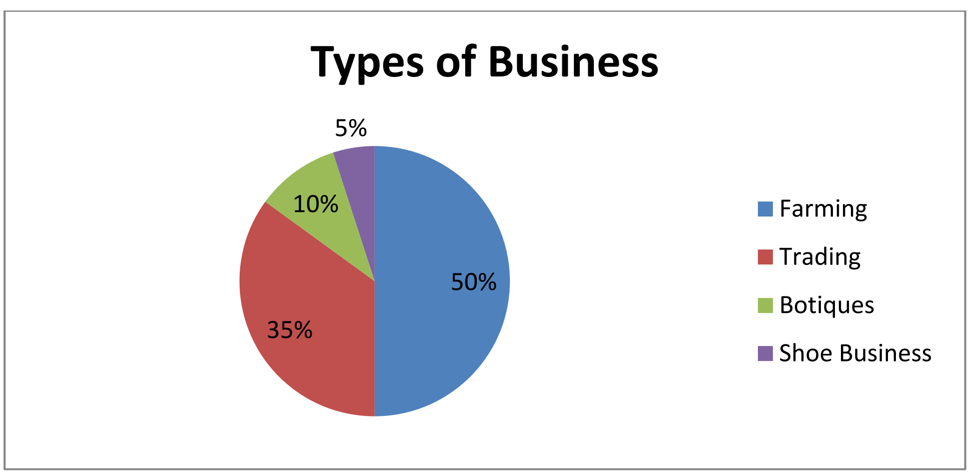
Level of education	**Frequency**	**Percentage**
Primary	20	20
secondary	45	45
University/tertiary	25	25
None	10	10
Total	**100**	**100**

Source: Primary data, 2016

Findings from table 3 above indicate that majority 45% had attained secondary level of education, 25% had attained university, 20% had attained primary while 10% never went to school. This implies that most clients of KMMF had attained some level of education. This is in line with Karla et al., (1993) that groups with emphasis on proper record keeping and educational training of managers have had success stories like co-operatives in Korea, Camilla projects in Bangladesh and some credit groups in Cameroon.

4.1.4 Type of Business

Figure 4: Type of Business



Source: Primary Data, 2016

The study intended to determine the type of businesses operated by the respondents. The findings in Figure 4 show that 50% of the respondents were in farming, 35% were in trading, 10% operated boutiques and 5% of the respondents operated in shoe business. Findings from the study imply that farming is the dominant economic activity carried out in by clients of Kyazanga Kwegatta Micro Finance, followed by trading, boutiques and shoes business.

These findings are similar to the ones by Marguerite (2001) and Todd (1990) where MFIs provide credit to borrowers who have experience in a particular type of enterprise and who are believed can and will repay the loan and interest on time.

4.2 Roles of Microfinance Institutions on the Growth of SMEs Capital

This section presents findings on source of business start-up capital, amount of start-up capital, capital increment, meeting loan criteria, problems repaying loans, MFIs help in promoting businesses and MFIs ensuring SMEs' access to credit finance.

4.2.1 Contributions of working capital

Table 4: Source of Business Start-up Capital

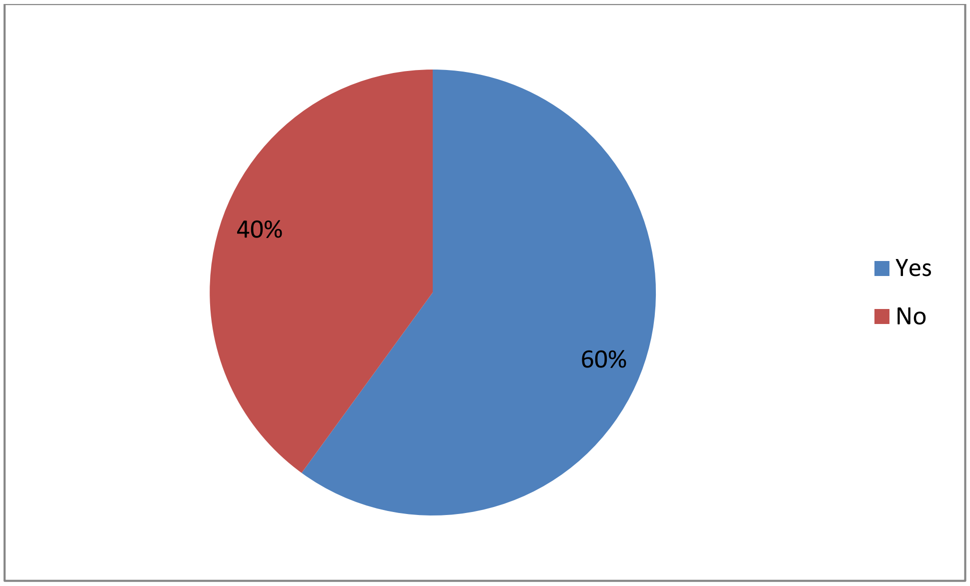
Contributions of working capita	Frequency	Percentage
Savings	60	60
Loans	40	25
Total	**100**	**100**

Source: Primary Data, 2016

The study sought to determine the respondents Contributions of working capital. The findings in Table 4 show that majority of the respondents (60%) started their businesses with their own savings, while 45% of the respondents borrowed money to start up their businesses. This implies that most people in Kyazanga Sub county start up their businesses using their own savings followed by borrowed funds and retained earnings. This is in line with Jain, (1996) who argued that for any business to survive there is need to be with enough savings by the owners of that particular business.

4.2.3 Savings contributions to working capital

Figure 5: Savings contributions to working capital



Source: Primary Data, 2016

Findings from the figure 4 above indicate that majority of respondents 65% agreed that indeed savings have contributed to their working capital while 35% disagreed. This implies that savings contributes to working capital of people in Kyazanga sub county. This is in live Mutungi (2010) study carried out on the relationship between savings and working capital management of SMEs in Kenya which concluded that indeed savings contributes to working capital of SMEs in Nakuru Kenya.

4.2.4 Challenges faced in saving with MFIs

Table 5: Challenges faced in saving with MFIs

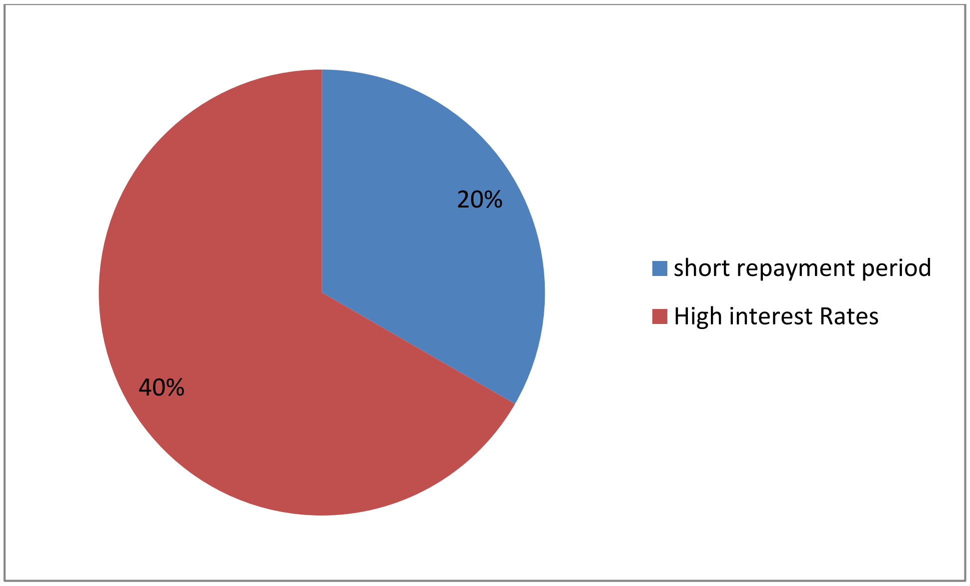
Percentage of Capital Increment	**Frequency**	**Percentage**
High interest rate	55	55
Long lines in the micro finance institutions.	25	25
Lack of collateral security	15	15
Too much paper work	05	05
TOTAL	**100**	**100**

Source primary data, 2016.

The study sought to determine the challenges people face while saving with MFIs in Kyazanga Sub County. The findings in Table 6 indicates that 55% of the respondents stated high interest rates as the major challenges they face while saving with MFIs, 25% mentioned making long lines while making their deposits as a challenge, lack collateral security was also mentioned as another challenge that people face while saving with MFIs, and other 5% mentioned too much paper work in micro MFIs as the a challenge they face while saving with MFIs. This implies that indeed micro MFIs most respondents had some challenges the face while saving with MFIs in Kyazanga Sub County.

4.2.5 Solution to the challenges facing customers while saving with MFIs

Figure 6: solution to the challenges facing customers while saving with MFIs



Research findings from figure 6, above indicates that majority of respondents 65% mentioned reduction on interest rates as a solution to the challenge they face while saving with MFIs while another 35% mentioned introduction of mobile banking in order to reduce on the time spent by clients in MFIs. This is in line with Hulme and Mosley (1996,) in a comprehensive study on the use of microfinance to combat poverty, argue that well-designed programmes can improve the incomes of the poor and can move them out of poverty.

4.2.6 Findings on whether respondents have acquired loans.

Table 6: Findings on whether respondents have acquired loans.

Problems with Loan Criteria	**Frequency**	**Percentage**
Yes	60	60
No	40	40
Total	**100**	**100**

Source: Primary Data, 2016

Majority of the respondents (60%) agreed that indeed they have acquired loan from MFIs while 40% of the respondents had never taken any loan from MFIs. This implies that MFIs provide loans to people in Kyazanga town Sub County. This is in line with the study by Hatch and Hatch (2008) which concludes that Village banking loan and savings growth rate increases as the banks continue to exist

4.2.7 Loan Repayment period

Table 7: Loan Repayment period

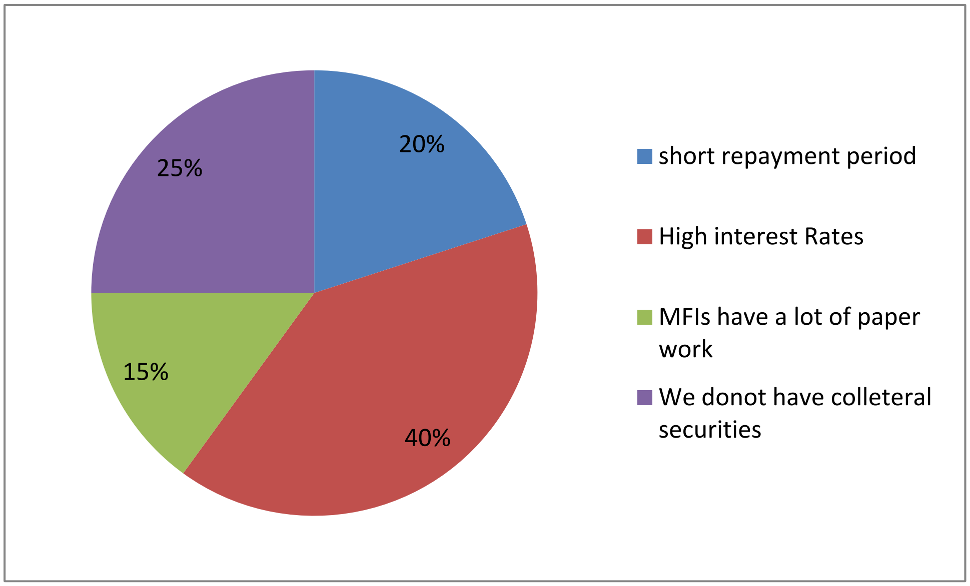
Loan repayment period	**Frequency**	**Percentage**
6month	10	10
One year	70	70
One and half year	10	10
2years	6	6
2years and above	4	4
Total	**100**	**100**

Source: Primary data, 2016

Findings from table 8, above shows that majority of respondents (70%) said that the repayment period for the loan is one year, 10% mentioned 6 month and one year and half as the repayment period of the one while 6% mentioned one year and another 4% mentioned two years and half as the repayment period for the loan to MFIs. This clearly demonstrates that most MFIs require clients to pay back their loans in a period of one year. This finding is in line with that of Luyirika (2010) on the study of microfinance in the socio-economic development of women in a community in Mpigi Town Council in Uganda which indicates that short repayment period affects the flow of money from the business to the MFI.

4.2.7 Respondents Reasons for not acquiring loan from MFIs

Figure 7: Respondents Reasons for not acquiring loan from MFIs



Source: Primary Data, 2016

The study intended to determine the reason as to why some respondents never acquire loans from MFIs. The findings show that 40% of the respondents mentioned high interest rates as the reason as to why they did not acquired loan from MFIs, 25% said that they did not had collateral securities required by MFIs, 20% mentioned short loan repayment period as the reason as to why they never acquired loans from MFIs while 15% said that MFIs have a lot of paper work. This is in line Luyirika (2010) in the study which indicates high interest rates affects the flow of money from the business to the MFI.

4.2.8 Responses on whether MFIs Loans have contributed to their working capital.

Table 8: Responses on whether MFIs loans have contributed to their working capital.

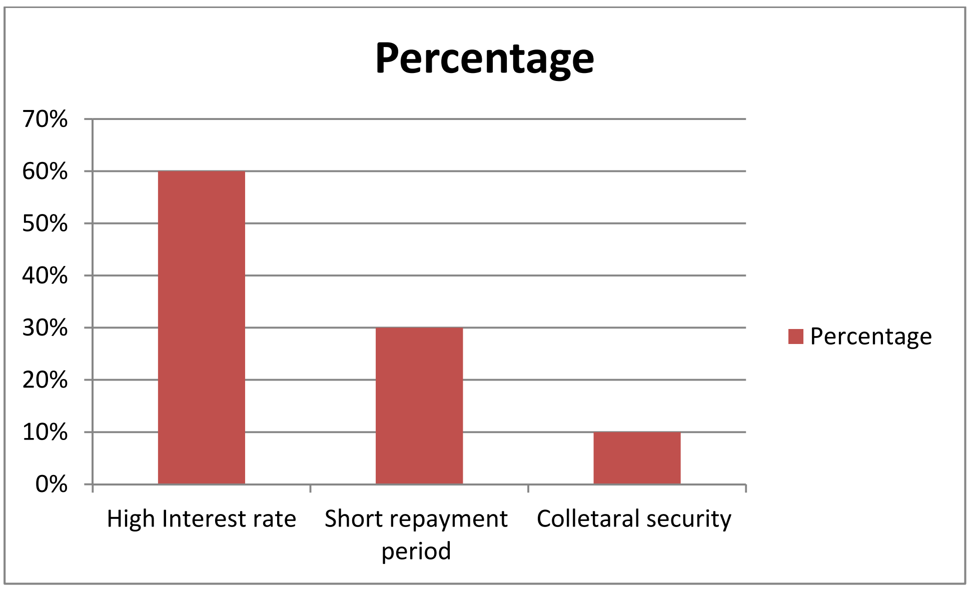
MFIs loans contributions to working capital	Frequency	Percentage
Yes	55	55
No	45	45
Total	**100**	**100**

Source: Primary data, 2016

Findings from table 8, above shows that majority of respondents (55%) agreed that MFIs loans have contributed to their working capital while 45% disagreed. This implies that MFIs loans have contributed to the working capital of people in Kyazanga Sub County. This is in line Robinson (2001) in a study of 16 different MFIs from all over the world which shows that having access to microfinance services has led to an enhancement in the quality of life of clients, an increase in their self-confidence, and has helped them to diversify their livelihood security strategies and thereby increase their income.

4.2.9 Challenges of using loans as working capital

Figure 8: Challenges of using loans as working capital



Source: Primary Data, 2016

Findings from figure 8, above indicates that majority of the respondents (60%) mentioned high interest rate as a challenge of using loan as working capital, 30% mentioned short loan repayment period while 10% said that MFIs require collateral securities which some do not have in order to get MFIs loans. This is in line with Armendariz, 2004 who argued that the challenge of MFIs support to business owners is the lack of flexibility from the MFIs when their clients fall sick, loose family members or are involved in accidents

4.3 Roles of MFIs on SMEs human resource

4.3.1 Responses on why they have Employees in the business

Table 9: Responses on why they have Employees in the business

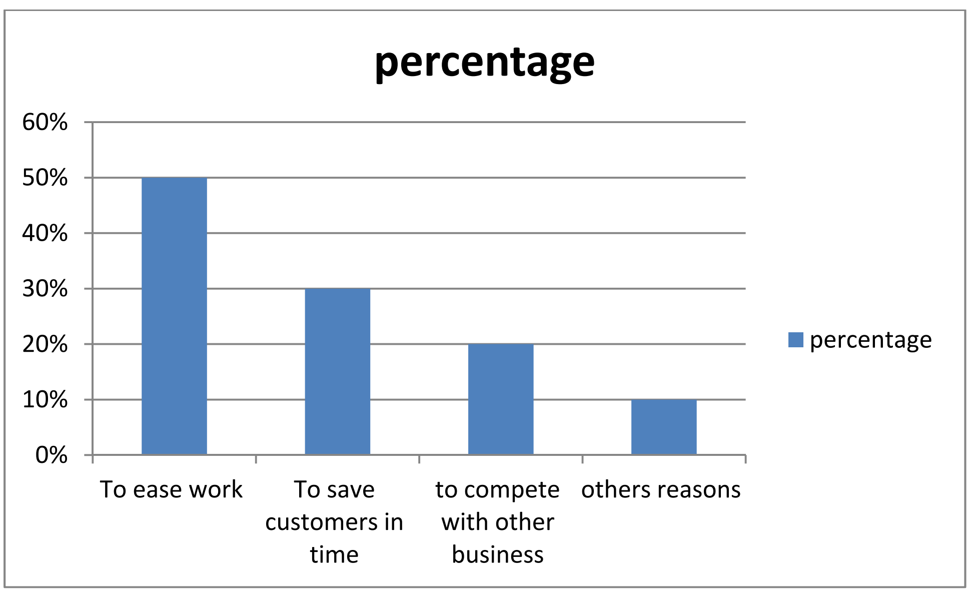
Response	**Percentage(%)**
Yes	80
No	20
Total	**100**

Source: primary Data, 2016

Findings from table 9, indicates that majority of the respondents (80%) agreed that they have employees in their businesses while 20% said that they do not have employees in their business. This implies that indeed most business owners in Kyazanga sub county employee some employee in their business.

4.3.2 Responses on why they employee in their businesses

Figure 9: Responses on why they have employee in their businesses



Source: Primary data, 2016

Research findings from figure 9, above indicates that majority of the respondents 50% motioned ease completion of work as the reason as to why they employ some employees in their business, 30% mentioned saving customer in time as the reason, 20% stated to compete favorably with other businesses while 10% give other reasons.

4.3.3 Responses on why they do not have employee

Table 10: Responses on why they do not have employee

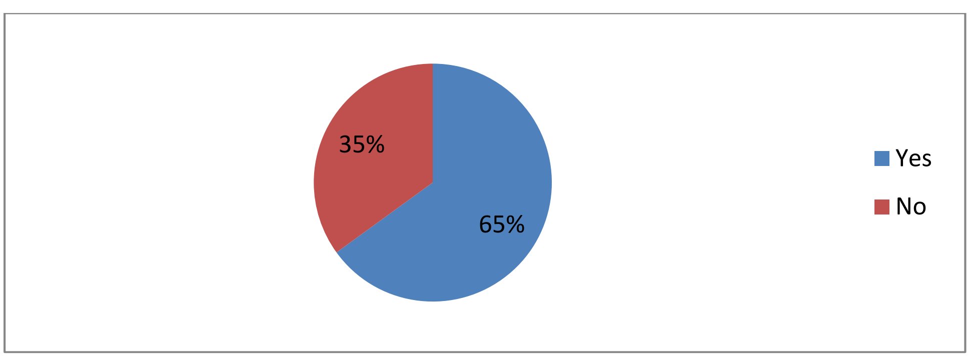
Response	Frequency	Percentage (%)
They are expense to be employee	10	50
Employees are not trustworthy	5	25
Employees do not have experience in managing businesses	5	25
Total	**20**	**100**

Source: Primary data, 2016

Findings from table 10, majority of respondents (50%) said that they do not have employees in their business because employees are expensive to be employed, (25%) said that they do not have .employees in their business because employees are not trust worthy while (25%)said that employees do not have enough stills to manage their businesses.

4.3.4 Training of SMEs Human resource by MFIs

Figure 10: Training of SMEs Human resource by MFIs



Source: Primary data, 2016

Majority of employees 65% agreed that they have ever got training by MFIs while 35% disagreed. This implies that KMMF offer training to its clients and staff. This is in line with Henriken and Svoldal (2010) on the role of providing business training to microfinance clients in Tanzania, the study uncovered that training was reflected on the entrepreneur's profits.

4.4. MFIs contributions on the Financial of performance of SMEs

4..4. 1 Responses on when respondents opened up an account with MFI

Table 11: Responses on when respondents opened up an account with MFI

Response	Frequency	Percentage (%)
Less than 1 year	30	30
1 year and half	50	50
2 years	10	10
2 years and above	10	10
Total	**100**	**100**

Source: Primary data, 2016

Findings from table 11, above shows that majority of respondents (50%) stated that they have open up their accounts with KKMF for a period more than 1 year and half, 30% had open their accounts for a period less than one year back, 10% had opened up in a period of 2 years back while 10% had opened their accounts in a period of more than 2 years and above back. This indicates that indeed majority of respondents had opened up their accounts early enough .

4.4.2. The uses of MFIs account

Table 12: The uses of MFIs account

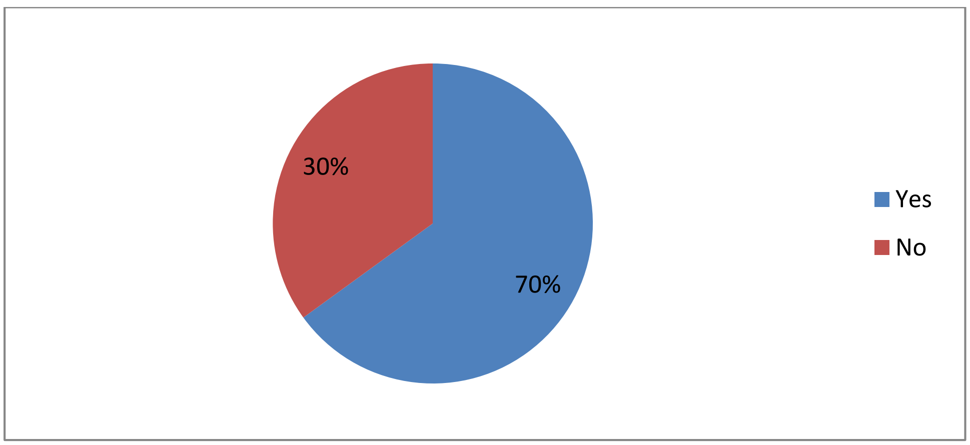
Uses of account	Frequency	Percentage
It is used for saving	70	70
Helps to access to microfinance credit	20	20
Charges	10	10
Total	100	**100**

Source: Primary Data, 2016

The study sought to examines the uses of the MFIs account to the clients of KKMF and their results obtained were as follows. Majority of respondents (70%) mentioned savings as the major use of a bank account, (20%)said that they use the account to help them access credit while (10%)said that charges are high. This is in line with Gibson, (2004) who asserted that individuals with bank accounts can effectively safe their deposits in Croatia.

4.4.3 Responses on whether the account has helped them in the budgeting their business.

Figure 11: Responses on whether the account has helped them in the budgeting their business



Source Primary Data, 2016

The study sought to examine whether the MFIs accounts have helped respondents in budgeting for their businesses. Findings from figure 11, above indicates that majority of respondents (70%) agreed that indeed MFIs accounts have helped them to budget for their business, while 30% disagreed. This therefore implies that KKMF has helped people in Kyazanga Sub County for effectively manage their businesses. This concurs with Gardiol, (2004) that micro finance accounts are a critical in providing knowledge and skills to customers and this help them to properly budget for their business.

4.4 Responses on how the account has helped Respondents in the budgeting of their business

Table 13: Responses on how the account has helped Respondents in the budgeting of their business

Benefits of the account to clients in budgeting for their businesses.	**Frequency**	**Percentage(%)**
Savings in the MFIs accounts are safe.	50	72
MFIs offer training with clients with accounts.	15	21
Others	5	7
Total	**70**	**100**

Source: Primary data, 2016

The study sought to find out how the MFIs accounts have helped respondents in budgeting for their businesses in Kyazanga Sub County. Findings from table above indicates that majority of respondents (72%) stated that savings on the MFIs are safe which enable them to budget for their businesses effectively, (21%) stated that MFIs offer training with clients with accounts while (7%) mentioned other benefits such as sharing of dividend and safe custody of valuable documents. This clearly indicates that MFIs help customers to properly budget for their businesses in Kyazanga Sub County These findings concur with a study conducted by Akisimire (2010) in Uganda which states that people with accounts in MFIs can properly budget and manage their businesses.

4.4.5 Responses on how the account has helped them in the growth of their sales

Table 14: Responses on how the account has helped them in the growth of their sales.

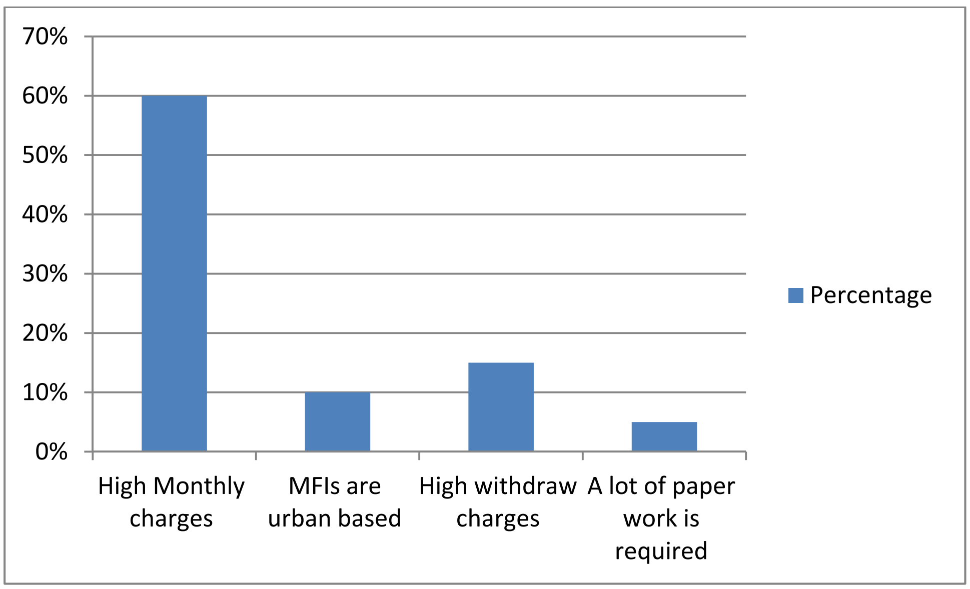
Respondents Responses	Frequency	Percentage (%)
Yes	80	80
No	20	20
Total	**100**	**100**

Source primary data, 2016

Findings from above shows that majority of respondents (80%) agreed MFIs accounts have helped them in growth of their sales, while (20%)disagreed. This implies that MFIs accounts help customers to increase their sales in Kyazanga Sub County. These findings concur with a study by Ahiawodzi and Adede (2012) indicating that opening with MFIs exerts a significant positive effect on the sales growth of SMEs. However those who disagreed give reasons like there is a lot of paper work in MFIs which delay their business transactions and that MFIs services are time consuming when there are many clients depositing and withdrawing.

4.4.6 Challenges of running the account

Figure 12: Challenges of running the account



Source: Primary data, 2016

Research findings from figure, above indicates that majority of the respondents (60%) mentioned high monthly charges as the challenge of running an account in MFIs, (15%) mentioned high withdraw charges as a challenge, (10%) said MFIs are urban based while (5%) said that a lot of paper work is required in the running of the account. This implies that indeed customer face some challenges in running accounts with MFIs in Kyazanga Sub county. This concurs with as study by Mwobobia (2012) in Kenya that identified High monthly charges as most serious constraints challenge facing customers while maintaining their accounts with MFIs in Kyazanga Sub County and this determines the smooth financial performance of their business entities.

4.4 Chapter Summary

The study established that MFIs remains the most important source of finance throughout the business cycle as most of the respondents access the MFIs for their startup capital for the training of human resource and for the financial performance of their business entities

CHAPTER FIVE

SUMMARY OF THE FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

This chapter presents the major findings on the effect of MFIs on the growth of SMEs in Kyazanga Sub county .The findings are spelt out in consonance with the objectives of the study. The researcher delves into a deeper discussion on the major findings in relation to the literature reviewed presented in chapter two.

5.2 Summary of the Findings

The study found out that the majority of respondents agreed that KKMF plays a major role in SMEs startup capital through saving their funds with the MFIs. This is in line with Jain, (1996) who argued that for any business to survive there is need to be with enough savings by the owners of that particular business. However some of the respondents disagreed and the reasons they gave included, high interest rates, shorter payback period, and a lot of paper work among others.

In the same line most of the respondents agreed that they had acquired a loan from KKMF and the major repayment period was one year and this affects the flow of money from their businesses to the MFIs. This is in line with Luyirika (2010) findings on the study of microfinance in the socio-economic development of women in a community in Mpigi Town Council in Uganda which indicates that short repayment period affects the flow of money from the business to the MFI. However some respondents do not access loans from MFIs and the reasons which were given included high interest rates, short repayment period and a lot of paper work. This concurs with the findings of Luyirika (2010) in the study which indicates high interest rates affect the flow of money from the business to the MFI

MFIs play a critical role on the growth of human resource capital. The results indicated that (80%) of respondents agreed that they have employees in their businesses. This indicates that the MFIs play a big role in making the labour force to be more productive through training SMEs Human resource. This is in line with study by Mel *et al.* (2008) which indicated that knowledge

and abilities are important in determining the returns SMEs capital especially in areas where there are low levels of human capital. This is more relevant in the informal sector where people with poor education might see entrepreneurship as a last way out to earn an income.
However some respondents do not employ people and they cited reasons such they are expensive to be employed, that they are not trust worth and that employees do not have skills in managing business.

The findings of the study revealed that majority of respondents agreed that they have opened up accounts with KKMF which they use for savings and accessing loans. Furthermore saving accounts help them to budget for their businesses and hence the growth of the businesses.

5.3 Conclusion

KKMF plays a major role in the growth of SMEs startup capital through saving and accessing loans,as most of the respondents, depended on MFIs loans. MFIs can also promote savings and yield moderate economic benefits that reduce the dependence on moneylenders. Access to finance has been identified as a key element for small scale enterprises to succeed in their drive to build productive capacity, to compete, to create jobs and to contribute to poverty alleviation in the county. Without finance, small scale enterprises cannot grow or compete in the turbulent business environment.

KKMF also plays a major role training of SMEs Human resource to be more productive and the study found out that it has helped in the growth of SMEs.
The account holders in KKMF use the accounts for savings and accessing loans. Furthermore the saving account help them to budget for their businesses and hence the growth of the business.

5.4 Recommendations

The study recommends that MFIs should come up with innovative ways to finance SMEs for successful growth. This would enable MFIs play a great role in economic empowerment of SMEs in Kyazanga Sub County. MFIs should also collaborate with self help groups and pyramid schemes in generating startup capital for SMEs. SME owners should be made aware on loan interest rates, grace period in repayments to have confidence in approaching MFIs for capital. This will lead to access to adequate finance which is critical for the growth of SMEs.

The study recommends that MFIs should play a critical role on the growth of human resource capital. This will make SMEs labour force to be more productive. MFIs should also intense and continuous business training to small and medium scale entrepreneurs in Kyazanga Sub county. The training should cover critical areas of business management that range from cost control, accounting, market analysis, marketing, and pricing strategies that can stimulate investments in feasible projects and lead to growth and expansion in the long-term. The training can also enable SMEs owners to plan, manage and evaluate investment, keep the record of all activities of the investment and also to utilize the loan more effectively.

The study recommends that the government should be involved in business growth. MFIs should assist SMEs in marketing of their business products and making credit available to SMEs at an affordable rate. The MFIs should continuously deal with trust worthy Self Help Groups. MFIs should also create flexible periods of loan repayment; collaborate with other MFIs in assisting SMEs and sensitization of entrepreneurs in giving them information about new products. This will enable the SMEs to benefit from the promotions and also diversify their investment portfolio.

While this study is on Kyazanga Kwegatta Micro Finance, it can be applicable to many other Micro Finances with the same level of development. Other studies can also be conducted on the formal and informal institution’s lending policies and access to credit by small scale enterprises in Kyazanga Sub County.

5.5 Areas for further study

- To examine the role of village SACCOs on the growth of SMEs
- To examine the role of micro credit on the growth of SMEs.
- To analyze the challenges face by MFIs in accessing credit from MFIs.

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APPENDICES I: QUESTIONNAIRE

QUESTIONNAIRE FOR STAFF OF KYAZANGA KWEGATTA MICRO FINANCE

QUESTIONNAIRE

Dear respondent,

I am Mande Douglas carrying out a research on ***"the Role of micro finance institutions on the performance of small scale business in Kyazanga Sub County".*** The study is purely academic leading to the award of the degree of Bachelor of Business Administration of Uganda Martyrs University. Please, I request you to spare a few minutes and answer the following questions. Information provided will be treated with utmost confidentiality.

SECTION A: BIO DATA

1. Gender

(a) Male ☐ (b) Female ☐

2. Age

(a) 25-29 ☐ (b) 30-39 ☐

(c) 40-49 ☐ (d) 50 years and above ☐

3. Marital Status

Single ☐ Married ☐ Widow ☐ Separated ☐

4. Educational Level

a) Primary ☐ b) Secondary ☐

c) University ☐ d) None ☐

5. What is the type of business?

a) Farming ☐ b) Trading ☐

c) If Others please Specify……………………………………………………………

…………………………………………………………………………………………………

6. Name the Micro Finance Institution ?

……………………………………………………………………………………………………

…………………………………………………………………………………………..

SECTION B: ROLES OF MFIS ON THE SMEs WORKING CAPITAL

7. What contributes to your working capital?

Savings ☐ Loans ☐

8. Has your savings contributed to your working capital?

If yes, specify,

i)………………………………………………………………………………………………

ii)………………………………………………………………………………………………

If no, specify,

i)………………………………………………………………………………………………

ii)………………………………………………………………………………………………

9.What challenges have you met saving with the MFI?

i)………………………………………………………………………………………………

ii)………………………………………………………………………………………………

b) Suggest Solutions to the above challenges

i)………………………………………………………………………………………………

ii)………………………………………………………………………………………………

10. Of recent, have you acquired a loan?

a) Yes ☐

b) No ☐

c) If yes, what was the repayment period?

…………………………………………………………………………………………………

If No, why

………………………………………………………………………………….

……………………………………………………………………………………………

11.Has this loan contributed to your working capital?

a) Yes ☐ b) No ☐

If yes, Specify

……………………………………………………………………………………………….

…………………………………………………………………………………………………….

If No, Specify

…………………………………………………………………………………………………

…………………………………………………………………………………………………

12. What are the challenges of using the loan as working capital?

…………………………………………………………………………………………………

…………………………………………………………………………………………………

Solutions

……

……

SECTION C: ROLES OF MFIs ON SMEs HUMAN RESOURCE.

13. Do you have employees in your business?

Yes ☐ No ☐

If yes, why do you employ the above employees?

……

……

If No, Specify,

……

………………………………………………………………………………………………………..

14. Have you and your employees ever got any training by MFI?

If yes, Specify,

…………………………………………………………………………………..………………

……

IF NO, Specify,

……………………………………………………………………………………………………….

………………………………………………………………………………………………………..

15. Has the training helped the growth of your SME?

Yes ☐ No ☐

If yes, Specify,

……………………………………………………………………………………………………..

………………………………………………………………………………………………………

If No, Specify,

………………………………………………………………………………………………………

………………………………………………………………………………………………………

SECTION D: MFIs CONTRIBUTIONS ON THE PERFORMANCE OF SMEs

16. When did you open up an account with this MFI?

…………………………………………………………………………………

b) What are the uses of your account?

…………………………………………………………………………………

……………………………………………………………………………………………

17. Has this account helped you in the budgeting for your business?

Yes ☐ No ☐

If Yes, Specify,

…………………………………………………………………………

……………………………………………………………………………

If NO, Specify,

…………………………………………………………………………..

…………………………………………………………………………..

18. Has this account helped you in the growth of your sales?

Yes ☐ No ☐

a) If Yes, Specify,

…………………………………………………………………………………………………

……
..

b) If No, Specify,

………………………………………………………………………………………………….

……
…………….

18. What are the Challenges of running the account?

……

……

b) Suggest solutions to the challenges

……

……

THANK YOU FOR YOUR COOPERATION