**THE EFFECTS OF MICROFINANCE LOANS ON PERFORMANCE OF SMALL AND MEDIUM ENTERPRISES (SMEs) IN TANZANIA.A CASE OF NMB BORROWERS IN KINONDONI MUNICIPAL, DAR ES SALAAM**

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**A DISSERTATION SUBMITTED IN PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR THE DEGREE OF MASTER OF BUSINESS ADMINISTRATION OF THE OPEN UNIVERSITY OF TANZANIA**

**2017**

# CERTIFICATION

The undersigned certifies that, he has read and hereby recommends for acceptance by the Open University of Tanzania a dissertation titled;“The effects of microfinance loans on performance of Small and Medium Enterprises (SMEs) in Tanzania. A case of NMB borrowers in Kinondoni, Dar es salaam”,in partial fulfillment of the requirements for the Degree of Masters of Business Administration (MBA) of the Open University of Tanzania.

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# DECLARATION

I,Geofrey Leonard Nyamwihula, do hereby declare that this dissertation is my own original work and that it has not been presented and will not be presented to any other university for a similar or any other degree award.

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Signature

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 Date

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# DEDICATION

This work is dedicated to the late beloved parents, Leonard Nyamwihula (father), Clesenzia Mutabuzi (mother), my beloved wife Devotha Peter Waijaha and my beloved children Agnes Geofrey, Dickson Geofrey, Alfred Geofrey , Godfrey Geofrey and Irene Geofrey.

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# ABSTRACT

The study assessed the effects of Microfinance loans on performance of Small and Medium Enterprises (SMEs) in Tanzania. A cross sectional design applying descriptive research design was adopted. The sample of 106 respondents who are clients of National Microfinance Bank were selected by using simple random sampling. Questionnaires constructed from five likert scale were used for gathering information pertaining to effects of loan received from NMB. Data were coded in SPSS and thereafter analyzed to generate descriptive and inferential statistics. Results from the study indicate that there was a significant increase in the average monthly gross profit of SMEs after employing loan obtained from NMB over time. Results found no significant relationship between collateral with SME performance in terms of socioeconomic performance. Additionally, results showed strong relationship between *Loan size* with SME performance and slightly significant relationship between *loan processing time* with SME performance. Furthermore there was no relationship found between collateral and SME performance. The study recommends that microfinance institutions should account for the social and economic impact their programs have on their clients. For the case of Micro-loan users, they should be able to utilize their loan facilities to the targeted goal so as to achieve the organizational goal.

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# LIST OF ABBREVIATIONS

CRDB Cooperatives and Rural Development Bank

DSE Dar es Salaam Stock Exchange

EMP Employment

GDP Gross Domestic Products

ILO International Labour Organization

IMF International Monetary Fund

IN Investment

MFI Microfinance Institutions

MSMEs Micro, small and medium Enterprises

NBC National Bank of Commerce

NEDF National Entrepreneurial Development Fund

NMB National Microfinance Bank

OECD Organizational for Economic and Community Development

PI Profit or Income

PLC Public Licensed Companies

SA Sales

SMEs Small and Medium Enterprises

SEDOM Small Enterprise Development Organization of Malawi

SIDO Small Industries Development Organization

SMEOP Small and Medium Enterprise Operational Performance

SPSS Scientific Package for Social Sciences

SSE Small Scale Enterprises

UK United Kingdom

URT United Republic of Tanzania

USA United States of America

TEC Technology

TRA Tanzania Revenue Authority

WB World Bank

# CHAPTER ONE

# 1.0 INTRODUCTION

## 1.1 Background to the Study

## Micro loan has been identified as an important tool for the poor, including SMEs for the Improvement of their socioeconomic status. It provides numerous benefits for beneficiaries such as SMEs for expanding their business (Ghadoliya,2012). Microcredit plays a crucial role in the socio-economic empowerment of individuals within households by promoting their participation in decision making at all levels. Providing loans to SMEs (financing) has been identified in many studies as the most important factor determining the survival and growth of small and medium enterprises (SMEs) in both developing and developed countries (Mittah, 2011).

## The micro-enterprises play a vital role in the reduction of poverty for the poor by enabling them to start prospering, economically and socially. Others in the society also get benefited from the microenterprise development as it fosters social relations or networks, civic engagement, community solidarity and social capital (Ohuche, 2013). As a result of poverty reduction policies in many countries, many banks and other financial institutions have introduced various packages of credits and deposits. Available information shows that currently there are about 68 banks and few non-banking financial institutions in Tanzania (Bank of Tanzania, 2015). The presence of more banks can be interpreted to mean more access to credit among Tanzanians and hence more investment leading to the generation of more income to reduce poverty.

## Despite the proliferation of banking institutions and the wide range of banking products and services, it seems very little attention has been paid to help the poor to come out of poverty. According to Christopher (2010) access to financing allows SMEs to undertake productive investments to expand their businesses and to acquire the latest technologies, and therefore ensuring their competitiveness and that of the nation as a whole. Poorly functioning financial systems can seriously undermine the microeconomic fundamentals of a country, resulting in lower growth of income and employment (OECD report, 2006).

Chijoriga (2005) contended that like in the globe, SMEs in Tanzania have the tendency to serve as sources of livelihood to the poor, create employment opportunities (contribution to job creation), generate income, and contribute to economic growth and social development (poverty alleviation). The contribution of the micro-enterprises is also significant to the macro-economic level. Tokaman (1996) emphasizes the importance of promoting micro-enterprise sector as a safety net for unemployed people in the societies where unemployment insurance is not available. SMEs have been recognized by several governments of developing countries to be the industry of supplying the resources to the extent that they now include them in their development plans. Despite increasing its roles, these enterprises are facing numerous obstacles that limit their performance, growth and development. Among the difficulties faced by SMEs, the access to finance is often reported as a major obstacle to the deployment and expansion of their activity.

Concept of the effect of financing SMEs for their operational performance in Africa and in the rest of the world is increasing from time to time. In pursuit of faster and more equitable development, a socialist development strategy in Tanzania was adopted in 1967.Massive nationalization of major enterprises followed; Local entrepreneurship was actively discouraged in favor of government, community-based or cooperative owned ventures. Regulations were introduced to bar civil servants and leaders of the ruling party from engaging in business activity and those educated African were civil servants, business was left to Asians and indigenous people without substantial education(Temu, 2007).The late 1970s saw a combination of other unfortunate event heralding a long economic crisis in Tanzania. The events include the international oil crisis of the early 1970s and a costly war between Tanzania and Uganda in 1978/1979. The crisis led to the erosion of real purchasing power of the national currency, forcing wage earners to undertake petty business activities to supplement their earning (Ouianoo, 2011).

Similarly, real crop prices dropped, compelling peasants and their offspring to either diversify income source by engaging in small ventures within the rural areas or migrate to urban Centre.The crisis was intensified in the early 1980s, forcing the government to liberalize trade and start implanting a radical transformation programme with the encouragement and support of the World Bank and International Monetary Fund (Bagachwa and Maliyamkono, 2008).

The programme involved liberalization of virtually all sectors of the economy, and the privatization and retrenchment of workers from the civil services and other public institutions. The private sector is now seen as the engine of economic growth and the role of the government has been redefined to focus on facilitation rather than direct ownership and operations of enterprises and disengagement of the government from some activities have led to substantial job losses and very limited job openings.

Those who cannot find jobs, as well as salaried workers, have resorted to running micro and informal businesses to make ends meet (Bagachwa and Maliyamkono, 2008).According to the Informal Sector Survey of 2014, small enterprises operating in the informal sector alone consisted of more than 1.9 million businesses engaging about 7 million persons that were about 38% of the Tanzanian labour force, and it was estimated that about a third of the GDP originates from the SMEs sector.

Since SMEs tend to be labour-intensive, they create employment at relatively low levels of investment per job created. Considering that currently unemployment is a significant problem that Tanzania has to deal with. Estimates show that there are about 700,000 new entrants into the labour force every year. About 500,000 of these are school leavers with few marketable skills (Zavatta, 2008). The public sector employs only about 40,000 of the new entrants into the labour market, leaving about 660,000 to join the unemployed or the under employed reserve (Temu,2009).

Most of these persons end up in the SME sector, and especially in the informal sector. Given that situation and the fact that Tanzania is characterized by low rate of capital formation, SMEs are the best option to address this problem (URT Dev.policy,2009).Other study revealed that, SMEs in Tanzania are estimated to contribute 30–35% of GDP and about 20–30% of the labor force (Mittah, 2011). There are approximately 2.7 million small and medium enterprises (SMEs) in Tanzania; sixty percent of these are located in urban areas. Most (98%) of SMEs are micro enterprises employing less than 5 people (Kashangaki *et al*, 2013).

From theoretical point of view we have a number of financing models to the SMEs. Examples of these financing models includes: equity financing as external source,

debt financing, corporate bond, venture capital and many other financing. The possibilities of SMEs for using equity financing are limited since the majority of these companies are privately managed. SMEs tend to be heavily reliant on commercial banks as a source of debt financing (Berry *et al.,* 2012) Therefore from the above fact, this study will concentrate only for debt financing which are bank loans. The major objective of this work therefore is to find out whether SMEs in Kinondoni district in Dar es salaam after access to bank loans have improved their performance or not.

## 1.2 Statement of the Problem

The subject of business growth is a fertile area for a study in the Tanzanian context (Kuzilwa, 2014). Reviews examining impacts of microfinance have concluded that, rigorous quantitative evidence on the nature, magnitude and balance of microfinance impact is still scarce and inconclusive. For example, various studies have been done on SMEs and how they are influenced by microfinance services. Mbugua (2013) studied on the impact of microfinance institutions on MSMEs in Kenya and found out that they had a great impact on employment creation and poverty alleviation. Kimei (2011) studying on the impact of micro finance services on financial performance of SMEs in Tanzania and found that micro finance services enhance financial performances of SMEs.

Ojo (2013) and Waithanji (2014) studied on the financial challenges faced by SMEs and found that inadequacies in access to finance are key obstacles to SMEs growth. Subrahmanya (2015) studied on the relationship between microfinance (services) and financial performance of SMEs. The findings were that positive and significant relationships have been established between MFIs loans and SMEs performance. Gathongo (2014) in a study on the impact of microfinance services on women empowerment found that microfinance has led to expansion of freedom of choice of women.

A survey of the financial constraints hindering growth of SMEs by Temu (2011) found that the factors affecting growth were capital market, cost, capital access, collateral requirements, capital management and cost of registration. Quianoo (2011) studied on the impact of microfinance services on the growth of SMEs in Nairobi and found a strong positive impact. According to researcher’s knowledge no study had focused on the effects of microfinance services on the growth of SMEs in Tanzania. The researcher felt that there was need for a study on this area and thus this study intended to bridge this gap and focus on the effects of microfinance services on the growth of SMEs in Kinondoni district in Dar es Salaam.

## 1.3 Objectives of the Study

### 1.3.1 General Objective

The general objective of this study was to assess the effects of Microfinance loans on performance of Small and Medium Enterprises (SMEs) in Tanzania, taking a study of Kinondoni district SMEs in Dar es Salaam.

### 1.3.2 Specific Objectives

In order to attain the main objective, the following specific objectives were looked at:

1. To examine the effects of microfinance loans size on SME’s operational and social economic performance.
2. To analyze the effects of microfinance loans processing time on SME’s operational and social-economic performance
3. To explore the effects of collateral security for loans from NMB on SME’s operational and social-economic performance.

## 1. 4 Research Questions

The study was guided by the following research questions:

1. What are the effects of NMB loans size on SME’s operational and socio economical performances?
2. What are the effects of microfinance loans processing time on SME’s operational and social-economic performance?
3. What are the effects of collateral security for loans from NMB on SME’s operational and social-economic performance?

## 1.5 Significance of the Study

The study will add value to the available literature on the similar subject. It will enable the researcher to integrate both theories and empirical literature with the real work situation. It will broaden the knowledge of the researcher and if properly and strategically applied, will add value to the business community as a whole. The findings of the study may help to identify SMEs key risk areas and suggest ways to minimize the risks in the future. The expected results are expected to help in solving the problem of SMEs performance with regard to access to financial services. The findings of the study are also expected to assist the government to effectively implement the SMEs policy. The study may help to bridge the existing knowledge gap. Lastly the findings will assist future researchers on the topic and add some literature for reference.

## 1.6 Scope of the Research

The proposed study on the effect of NMB loans on performance of SMEs was conducted at Kinondoni in Dar es Salaam. The researcher decided to choose NMB bank due to the fact that, it is the largest bank in Tanzania, with over two million customers, it has one hundred seventy five (175) branches over the country, and 600 ATMs, covering more than 95% of districts(NMB,2015). It was also chosen because the researcher is more convenient in terms of proximity and time constraint. The study was conducted for a period of four months.

## 1.7 Organization of the Study

The study is divided into five chapters:

Chapter one is the general introduction and backgrounds. It explains on the setup of Small and Medium Enterprises (SMEs) and it focuses on the impact of loans on SMEs performance and presents problems identified. It also presents the research objectives, research questions, scope of the research and significant of the study. Chapter two reviews literature related to the problem under study. It mainly reviews literature on Small and Medium Enterprises and access to finance. Chapter three elaborate about research methodology including research design, area of study, population of the study, sample size and sampling procedures, data collections and data analysis. Chapter Four presents findings and discussion of findings. Chapter five presents summary of the main findings, conclusions, implications, recommendations and areas for further studies.

# CHAPTER TWO

# 2.0 LITERATURE REVIEW

## 2.1 Overview

Literature review is a summary of previous researches on a topic. Literature review summarizes and explains what previous research have done on the topic, citing the sources as you mention them, point out the different ways researchers have treated the topic, point out any connections between the sources. In this chapter, the researcher presents the literature related to the interest of the study and how other authors and researchers have said; it covers the literatures on bank financing on performance of SMEs, conceptual definitions of various terms which are crucial in literature, critical theories of related subject which clearly shows related references of the subject, empirical studies which considers various reports of related subject, research gap and the conceptual framework.

## 2.2 Conceptual Definitions

The following are conceptual definitions of key terms:

### 2.2.1 Small and Medium Enterprises (SMEs)

The SMEs nomenclature is used to mean small and Medium Enterprises. It is also referred to as micro, small and medium enterprises (MSMEs).The SMEs cover non-farm economic activities mainly manufacturing, mining, commerce and services. There is no universally accepted definition of SME. Different countries use various measures of size depending on their level of development. SMEs are widely defined in terms of their characteristics, which include the size of the capital investment, the number of employees, the turnover, the management style, the location, and the market share (Louis et al 2013). But in the context of Tanzania, SMEs are those engaging up to 4 people, in most cases family members or employing capital amounting up to Tshs.5.0 million. The majority of microenterprises fall under the informal sector. Small enterprises are mostly formalized undertakings engaging between 5 and 49 employees or with capital investment fromTshs.5 million to Tshs.200 million. Medium enterprises employ between 50 and 99 people or use capital investment from Tshs.200 million to Tshs.800 million. (Tanzania SMEs policy, 2006).

### 2.2.2 Micro, Small and Medium Enterprises (MMSE) Loans

These are small loans to Micro, Small and medium Enterprises to expand small and sustainable business. Applicant can borrow from TZS 100,000.00 to a maximum of TZS 10,000,000.00 (NMB, 2014).

### 2.2.3 Small and Medium Enterprises (SMEs) Loans

These are small and medium financing from TZS 10 million to TZS 1 billion depending on the size, nature and viability of the enterprise to be financed. The credit tenor / term depend on repayment capacity, anticipated cash flows, credit amount and credit purpose (NMB,2014).Various literatures from different authors and other scholars have tried to explain the importance of financing to SMEs for their performance.

### 2.2.4 SME’s Performance

In most cases SME’s performance is the firm’s ability to continue in operation, but this is not always the case, firm’s performance can have two different outcomes: success (continuity of operation) or failure (ceasing of operation) (Subramanian, 2010). Under this study the researcher does not know whether bank loans contribute to SMES performance. The researcher wants to find out the effect of the SMEs performance after receiving loan from the bank.

## 2.3 Theoretical Literature Review

### 2.3.1 Theoretical Link Between Microfinance Loan and SME Performance

In order to increase the development and performance of SMEs, accessing adequate amount of credits is considered to be an important factor. It boosts income increase levels, increase employment and hereby reduce poverty. It is alleged that access to credit enables low income earners to overcome their liquidity constraints and undertake some investments such as the improvement of farm technology inputs thereby leading to an increase in agricultural production (Hiedhues,1995).Navajas *et al*.(2000) assert that the main objective of microcredits to improve the well being of the poor as a result of better access to microcredit’s that are not offered by the formal financial institutions. A study carried out in Kenya in 2012; revealed that MFIs play a major role in credit provision to the SMEs. This credit has contributed to the growth of businesses in terms of number of employees, asset base, level of stocks and services of the businesses.

### 2.3.2 Small and Medium Enterprises (SMEs) Loans

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A comparative study of manufacturing firms by Snadgross and Briggs (1996) shows common pattern in the transformation of the size distribution of firms as industrialization by concluding that small-scale enterprises play a declining role as countries develop. Sanda et al (2006) comparing large and small firms ability to create employment observed that small firms are relatively better at creation of employment opportunities. A crucial element in the development of SMEs sector is to access to financing, particularly to bank financing. SMES in developing countries contribute an average of sixty per cent of total formal employment in manufacturing sector. For African economies, the contribution of SMEs sector to job opportunities is even more important, taking into account the contribution of informal sector, SMEs account for about three-quarter of total employment in manufacturing (Ayyagari *et al*, 2007,Pietro *et al,* 2012).

Financial and development assistance designed for SMEs in Bangladesh is a new and upcoming trend. In Bangladesh, both micro-finance institutions and banks begun to realize the potential for SMEs designed new financial product for it. With the aim of generating employment opportunities through SME growth, Brac Bank launched a special SME lending scheme in 2002 in Bangladesh. Brac Bank in Bangladesh started providing credit to SMEs in recognition of their special needs for their contribution in fostering growth, sustaining global economy recovery, generating employment and reducing poverty (OECD, 2004, Mehnaz and Munshi, 2007). Employment generations by SMEs in Bangladesh after taking loans from Brac Bank are growing as indicated below:

However, the SMEs sector is faced with many constraints. Among them is the most pressing one known to be financing (Idowu and Christopher, 2010).Small and Medium Size Enterprises (SME) are the most common employers across the world. In 48 out of 76 nations covered in Ayyagari (2007) SMEs employed more than 50% of the formal workforce. In addition, Clement and Terande (2012) find that small firms and mature firms have the highest levels of total employment and small firms and young firms have the highest rates of job creation. SMEs are a fundamental part of a dynamic and healthy economy.

Small businesses are started in developing countries at a considerably high rate as they make contribution to economic development. Malcolm Harper (1984) is of the opinion that income is the outcome of employment, employment generation, therefore, is the main goal of poor countries. The small business, according to Harper, has displayed a remarkable capacity to absorb. Traditional microeconomic theory treats finance as a corporate factor of production. Irrespective of firm size and age, finance is normally required for three standard uses, that is for capital investment (start up or expansion) in machinery and acquisition of premises (building), financing working capital during start- up or while expanding and purchase of operating materials.

Implementation of entrepreneurial activity can only happen when these factors are in place; otherwise the activity has to be aborted. Financing factors of production can be undertaken from own savings (in the case of start –ups), or external funds (for start –ups and on-going businesses). Credit becomes important when internal sources of finance are inadequate for an envisaged entrepreneurial activity (Kristiansen, 2001). This role is particularly critical in the national efforts to eradicate poverty. The significance of the SMEs in Tanzania is evident from more than 1.7 million businesses operating, which are estimated to employ more than 3 million people (URT, 2002). SMEs also serve as a training ground for emerging entrepreneurs as well as forming the backbone of the indigenous private sector. Finance has been observed to be one of the important determinants of the small business success. Credit is an important source of finance for the businesses start or growth.

 A number of support institutions have mushroomed in Tanzania since the onset of economic reforms in mid-1980, extending credit to SMEs, thus filling the gap left by commercial banks to large firm financing. Despite the relatively long experience with funding micro and small enterprises in Tanzania, little research has been conducted to assess the effect of such funding on the businesses. Lack of access to credit has been identified as one of the major constraints hindering the development of small businesses, and therefore the supply of entrepreneurial activities not just Tanzania, but in other developing countries (Bagachwa *et al*., 1993).

Commercial banks have traditionally concentrated on lending mainly to large formal enterprises which possess collateral and, therefore, thought to be low risky. Women World Bank (1995) estimated that worldwide, less than 2 % of low-income entrepreneurs have access to financial services.

Despite the above starting statistics on the low rate of access to credit, there are some concerns that the role and importance of (institutional) credit in the dynamics of business growth may be overrated (Tomeck, 2014). Important questions are to what extent is lack or inadequacy of credit contributing to the low level or failure of entrepreneurial activities in Tanzania? Are enterprises that have not received credit within a given setting? What is the effect of credit on entrepreneurial activities and how can it be measured? These are both theoretical and empirical questions. Although the role of credit as a determinant for successful entrepreneurial activity may look obvious when using a partial analysis, the dynamics in the entrepreneurial process makes this role less obvious.

The analysis of an entrepreneurial activity shows that finance does not in itself create economic opportunities. Rather it is entrepreneurial people who see ways in which they can generate income from situations, skills or contact or other push factors (Christen 1997). It is in this context that the role of credit should be seen that financing enhances the ability of entrepreneurs to take advantage of these opportunities, thereby leading to success. Lack of it could lead to business failure. Entrepreneurial success could be defined in a conventional sense in terms of a profit’s generation and growth in terms of employment, output, sales, etc. over time. Through growth a firm can graduate from one size to a higher one. In addition, firms that are also realizing results like increased employment of family members, increased household welfare (increased access to education, health, better housing) and those that are able to survive under intense competition are also included.

## 2.4 Challenges Faced By SMEs in Tanzania

### Despite the role played by SMEs in employment creation, income generation and poverty alleviation, and government effort to develop the sector, SMEs in Tanzania are currently faced with many serious challenges which act as a barrier to their emergency and growth. These barriers or challenges to the SMEs include: perception to risk, high interest rates, inadequate business skills, collateral, tax policy and transaction cost. These challenges are explained below;

### 2.4.1 Risk Perception

 In Tanzania, the death of the SMEs owner leads to the death of the business. This is because there is no difference between owners and the business, they are the same. Also another challenge for banks is to acquire information about the credit risk of the borrower, as borrowers have more information than the lender about the projects (Myers & Majluf, 1984). Existing contract theory argues that banks are not interested in offering credit to SMEs because it is particularly difficult to overcome information asymmetries and resulting screening, monitoring, and enforcement problems. Under asymmetric information conditions banks are uncertain about the future behavior of the borrower in terms of repaying the loan. Asymmetric information problem are more likely to occur when banks deal with SMEs due to higher opacity of these firms (Berger *et al.* 2001; Beck *et al.* 2004; Hyytinen and Pajarinen, 2008; Cole 2004).

By opaqueness the literature means that it is difficult to ascertain if firm have the capacity to pay (have viable project) and/or willingness to pay (due to moral hazard) (Beck, 2010). Information asymmetry between SME borrowers and the banks is reflected in inability of the majority SMEs to provide up to date reliable financial information and realistic business plans, which increases the cost of lending that banks incur while dealing with these SMEs. Consequently limits the ability of banks to assess the creditworthiness of the individual SME borrowers. The argument of information asymmetry is supported by Temu (2009) who emphasized that poorly compiled records and financial account coupled with inability of SMEs to properly express their knowledge about business opportunities aggregates the lack of adequate information in bank-SME credit transactions in Tanzania.

Temu (2009) affirm that financial institutions in Tanzania are reluctant to finance small and medium firms for fear of default risk due to unreliable financial plans and records. Satta (2003; 2006) amplify this argument by point out lack of adequate and reliable collateral, lack of appropriate instrument to manage risk, not being familiar with complicated information about SMEs and perceived risk make banks in Tanzania become unwilling to provide the much-needed finance to SMEs. Under these circumstances, literature shows that where information asymmetry exist banks will ration the supply of credit and in addition will tighten requirements such as collateral in order to protect themselves from likely opportunistic behavior of dishonest borrowers.

### 2.4.2 Interest Rate

Interest rate represents the cost of borrowing or the cost of obtaining money from the borrower’s point of view. Those who are able to access credit are faced with high interest rates and short repayment periods making it very difficult to embark on any development or expansion projects. Interest rates tend to remove some of profits that are made in business that make loans to operate. From theoretical point of view it is expected that demand for credit is positively related to low interest rates charges. This is because if borrowers are charged lower, it is easier for them to access and repay because will be having a low burden compared to high interest rate which motivates default and inability to run the business.

### 2.4.3 Business Management Skills

Managerial competencies are sets of knowledge, skills, behaviors and attitudes that contribute to personal effectiveness (Hellriegel et al., 2008). Managerial competencies are very important to the survival and growth of new SMEs. Martin and Staines (2008) found that lack of managerial experience and skills are the main reasons why new firms fail. The ability of managers to perform has a very important bearing on the performance of business.

The sources of many managerial problems in SMEs are lack of education and professional training. SMEs generally lack of managerial adequacy and competence as most of them are controlled by managers who lack modern management techniques required by ever-changing markets and increasing intensity of competition. Today, owners/managers of small firms must be familiar with many aspects of management such as finance, personnel, production etc. Many studies indicated that entrepreneurs perform poorly in many areas of management such as bookkeeping i.e. poor and unreliable financial records which makes financial review difficult., marketing, costing, stock control, warehousing, production scheduling and quality control.(Temtime and Pansiri, 2000).

### 2.4.4 Collateral

Cuevas et al. (1993) indicates that access to bank credit by SMEs has been an issue repeatedly raised by numerous studies as a major constraint to industrial growth. A common explanation for the alleged lack of access to bank loan by SMEs is their inability to pledge acceptable collateral. Collateral requirement has been identified by many literatures like Aryeetey et al (1994), Abor and Biekpe (2006) the experience from Ghana as a factor affecting the demand for credit in SMEs. Most of the SME’s lack sufficient collateral requirements compared to large firms.

When businesses commence, there is hardly any collateral to present for obtaining financial aid. Lending without collateral to SMEs is extremely risky from the lender's viewpoint. In such situation where some SMEs are able to provide collateral, they often end up being inadequate for the amount they needed to embark on their projects as SMEs assets- backed collateral are usually rated at’ carcass value’ to ensure that the loan is realistically covered in the case of default due to the uncertainty surrounding the survival and growth of SMEs (Binks et al., 1992). Example for NMB, collateral value must be of not less than 125% of loan taken. And normally accepted collateral for those banks is Land property.

## 2.5 Empirical Review

### 2.5.1 Review of studies done worldwide

According to the research which was conducted by Stokes David (1997), he revealed the importance of financing to SMEs in USA and UK for individual economic growth as well as national economy. He linked his research with the Bolton Report (1971), in view of the actual and potential contribution of small firms to the overall health of the economy there was created a small division under a Ministry for small Firms. This was implemented by the establishment of the Small Firms Service within the Department of Industry (UK).

The particular concern of the report was that Government policies should encourage and support the sector, not accelerate its decline through an unfair burden of regulations, paper work and taxes. We believe that the health of the economy requires the birth of new enterprises in the substantial numbers and the growth of some to a position from which they are able to challenge and supplant the existing leaders of the industry. This seedbed function, therefore, appears to be a vital contribution of the small firms sector to the long-run health of the economy. The growth in employment in the USA between the mid-1960s and mid-1980s was phenomena, Bolton report (1971)

Ryan (1993) adopted Bolnick and Nelson’s (1990) approach and conducted an ex post evaluation of one financial source for small businesses, Small Enterprises Development Organization of Malawi (SEDOM). He used a survey method (covering 50 firms) to assess the impact that firms have received in terms of loans from SEDOM. In assessing the impact Ryan, in addition to other effects, looked at whether or not the enterprises achieved the objectives listed as objectives of the schemes. The variables used reflecting the objectives of SEDOM were employment generation, technology employed and linkages. The results of the study showed that the scheme as a whole created about 1,873 jobs at a relatively low cost of Malawian Kwacha 1,000 per job. The study also found out that significant backward linkages to the agricultural sector were created as a result of manufacturing firms receiving loans.

### 2.5.2 Review of Studies Done in Africa

Quianoo (2011) conducted a study in Ghana. The general objective of his study was to investigate the contribution of loans to SMEs performance. The bank financing is tremendously attractive and seems to be realistic and a more reliable source to SMEs. Another study was done by Koech, (2011) conducted a study to find out the financial constraints that hinder growth of SMEs in Kenya. The researcher adapted the case study approach and targeted SMEs in Kamukunji District. The study used structured questioners as main tool for data collection. Data was analyzed and by explanatory factor analysis and descriptive analysis with the help of SPSS to obtain percentages and frequency distribution tables. The factor hindering growth of SMEs were identified as capital access, cost, capital market, collateral requirements, information access, capital management and cost of registration. The study recommended that business financiers through loans consider reducing collateral requirements to facilitate SMEs easy access to loans.

Waithanji (2011) studied the effect of microfinance credit on the financial performance of small and medium enterprises in Kiambu county, Kenya. The study was done through the use of survey design. Out of the 2,061 SMEs licensed, the study randomly sampled 60 SME‟s.The study found that there is a direct relationship of access to credit and financial performance of the companies. The study also concludes that the enterprises benefit from loans from microfinance institutions, the SMEs seek financial assistance from the MFIs due to interest rate, easy loan repayment and amount offered. There is a need to provide an enabling environment for SME‟s to grow and thrive; therefore there is a need to develop strategies to enhance increased access to microfinance credit by SME’s from commercial banks and microfinance institutions.

Idowu (2010) conducted study in Nigeria on the impact of microfinance on SMEs. The fundamental objective of the study was to assess the impact of Microfinance on Small and Medium Enterprises (SMEs) in Nigeria. Simple random sampling technique was employed in selecting the 100 SMEs that constituted the sample size of the research. The study utilized primary sources of data in which structured questionnaires were extensively used. Structured questionnaire was designed to facilitate the acquisition of relevant data which was used for analysis. Descriptive statistics which involves simple percentage graphical charts and illustrations was tactically applied in data presentations and analysis.

Many respondents claimed that they are able to access to microfinance loans and achieved their goals. The findings of the study reveal that significant number of the SMEs benefited from the MFIs loans even though only few of them were capable enough to secure the required amount needed. Interestingly, majority of the SMEs acknowledge positive contributions of MFIs loans towards promoting their market share, product innovation achieving market excellence and the overall economic company competitive advantage. Other than tax incentives and financial supports, was recommended that Government should try to provide sufficient infrastructural facilities such as electricity, good road network and training institutions to support SMEs in Nigeria.

### 2.5.3 Review of Studies done in Tanzania

Research conducted by Kuzilwa (2005) on the role of credit for small business success aimed at studying the effect of special credit to small and micro enterprises on entrepreneurial activities. The study used ex-post facto research design, in which it is systematic empirical inquiry in which the researcher cannot have direct control of variables because their manifestations have already occurred or because they are inherently not manipulated. This involves testing theories, hypotheses, identify behavioral phenomena and study conditions under which a phenomenon occurs. From this study the independent variables were identified as education, gender, size of the loan, while the dependent variable was small business performance.

 In his study, he had combined both qualitative case studies and a sample survey. Case study was actually from Morogoro Municipal while survey involved three regions namely Arusha, Dar- es-salaam and Morogoro. The choices of the regions were done randomly from cluster of twenty (20) mainland regions with a total of 1032 Small Industries Development Organisation (SIDO) clients which were distributed as follows: Dar-es-salaam 445, Arusha 464, and Morogoro 113. The researcher decided that a total of 250 clients were surveyed with proportional representation of three clusters as follows: 107 respondents of the clients were sampled from Dar-es-salaam, and 115 from Arusha. Twenty-eight (28) clients were from Morogoro. Data were collected through SIDO Profile report. The data were analyzed using descriptive statistical, cross-tabulation and chi-squared tests. The findings revealed that all three independent variables accounts for good performance for SMEs. Based on the findings of this study, the findings reveal that the output of enterprises increased following the access to the credit. It was further observed that the enterprises whose owners received business training and advice, performed better than those who did not receive training. He recommended that an environment should be created where informal and quasi-informal financial institutions can continue to be easily accessed by SMEs.

 A knowledge gap is that the study was relating to special credit small and micro enterprises on entrepreneurial activities funded under National Entrepreneurial Development Fund (NEDF) in Tanzania through SIDO loan, but this study will be related to the effect of bank (NMB) financing on performance of small and medium-sized enterprises (SMES). However the study employed both case studies and survey but this study will employ case study (exploratory) design. My challenge to the researcher is that, although the independent variables have been shown as contributors to SMEs success, but there is no proper analysis as to what extent to each variable has the effect in terms of performance. For example loan, the researcher said contributed good small business success. He did not analyse how much loan was applied for, how much was granted and what was the gap of the loan. Apart from knowledge gap stated above, part of the theory together with citation it is still relevant to this study and other studies.

 Kessy and Urio (2006) conducted study on the contribution of microfinance Institutions (MFIs) to poverty reduction in Tanzania. The general objective was to find out the extent to which the microfinance Institutions contributes to poverty reductions in Tanzania and whether they meet the objectives of the policies that led to their establishment. The study employed both primary and secondary data. The study covered four regions of Tanzania that have a high concentration of MFIs. These regions include Dar es Salaam, Zanzibar (Urban West Region), Arusha and Mwanza. In these four regions the study covered a total number of 352 SMEs supported by the selected MFIs and the SMEs were selected by random sampling. From this study, the findings revealed that, to a large extent MFIs operation in Tanzania have brought positive changes in the standard of living of clients who received loans services because it reduce poverty through increased income and standards of living; empower women; develop the business sector through growth potentials.

The surveyed micro and small enterprises revealed that their profits increased after receiving the loan. My observation regarding the study is that, the coverage of the study was on the effect of the contribution of MFLs to poverty reduction in Tanzania, while my study is based on the effect of bank financing on SMEs performance in Dar es salaam. Although both studies stress the importance of equitable, sustainable individual economy, national economy growth and improvement of the people’s welfare.

A study done by Madole (2013) on the impact of microfinance credit on the performance of SMEs in Tanzania, shows that credit obtained from NMB Bank in Morogoro, SMEs have been able to improve businesses in terms of: increased business profit, increased employees, increased sales turnover, increased business diversification, increased business capital and assets as well as reduction of poverty among customers surveyed. Result also shows that collateral, age or experience of the SMEs owners, and, size of the firm influence the access of credit. The study concluded most of the small businesses depend on bank loan for business capital growth. Bank loan especially NMB loan plays a very crucial role to promote small business growth. Although some of the small businesses fail to repay bank loan due to various reasons such as grace period, moral hazard and high interest rate. In regard to the findings, however, it was recommended that MFIs should increase credit and enhances participation in SMEs financing, in order to sustain the growth and maximal contribution to economic growth and development of the nation.

 Mwinyimvua (2012) conducted study on Policy issues and SMEs development in Africa. It is recognized that the private sector plays a development role as a key engine of growth and that growth is the most powerful weapon in fighting poverty. SMEs are important in providing goods and services and opportunities for employment for unemployed and the second source of income for formal sector employees. It is estimated that SMEs employ over 20 per cent of the adult population in developing countries (Kayanula and Quartey, 2008). To be able to apply new methods and expand, firms need finance or capital. Lack of access to capital is one of the major constraints in SMEs development; this is because of poor domestic SME’s policy and regulatory environment. Although capital may not by itself solve all the key problems of SMEs, most developing country entrepreneurs, especially those in Africa, say it is their number one need (World Bank 2001; Batra et al 2002). In Tanzania, for example a survey of SMEs in the furniture industry found that lack of access to finance is a binding constraint for all SMEs. Not only is informal financing limited for the small firms even firms of adequate size and experience have difficulty borrowing from banks, and if they do borrow, have difficult relations with their lenders (Levy, 1993).

The difficulty of accessing finance by business enterprises was also noted in a year 2000 survey of 248 manufacturing establishments in Tanzania (Mbelle, 2001). The survey found SMEs to be more disadvantaged than large-scale enterprises in accessing finance, with 80.6 per cent of SMEs indicating that they find it difficult to access finance compared with 61.5 per cent for large-scale enterprises. Increased SME growth has direct effect on GDP growth to increased output, value added and profits. As growth proceeds, private sector employment becomes the major source of economic support for the majority of workers and their families.

One of the best ways to build the private sector is from the bottom up, focusing on small-scale enterprises, which hold the promise of providing a base for the emergence of dynamic and efficient large-scale firms and consequently a more flexible and competitive domestic economy. This means listening to their concern, identifying their biggest obstacles, and helping them compete in an increasingly global economy (World Bank, 2001). The researcher recommended that, Government should provide stable business environment, improving the legal and regulatory system, reducing bureaucratic procedures, dismantling trade barriers and reforming the tax system.

**Table 2.1: Summary of Variables from Other Studies**

| **Author**  | **Topic of the study** | **Variables** | **Methodology** | **Findings** |
| --- | --- | --- | --- | --- |
| Joseph. Kuzilwa (2005) | The role of credit for small business success: A study of the National entrepreneurship development | Education, size of the loan, gender, | The study involved both the case study and survey with total population of 1032. Sample of 250 clients were randomly selected from three regions with the cluster of twenty regions | Two key results:1.Access to credit had increased farm output2.Enterpreses whose owners received business training performed better than those who were not trained |
| Kessy and Urio (2006) | Contribution of microfinance Institutions to poverty reduction in Tanzania |  |  The survey employed both primary and secondary data. It covered four regions 352 SMEs which was selected at random. | There were positive changes in the standard of life of the clients who received loans. 81.3% of the surveyed SMEs revealed that, their profit increased after receiving the loans.  |
| Quianoo (2011) | Examining the impact of loans on SMEs in Ghana | Loan, sales, returns/profits, stock levels | Population of 303 comprised all SMEs who keep accounts with bank. Simple random sampling techniques was employed in selecting the 100 SMEs | 96.3% of the total respondents indicated that the loans improved the overall performance of their firms. |
| Idowu. (2010) | Impact of microfinance on SMEs in Nigeria | Loans, sales, market share, profits | The study utilized primary sources of data in which structured questionnaire were extensively used. To constitute sample size out of the population of the study, simple random sampling technique was used to select 100 SMEs operators in Nigeria. | The findings of the study reveal that significant number of the SMEs benefitted from the MFIs loans even though only few of them were capable enough to secure the required amount needed. Interestingly, majority of the SMEs acknowledge positive contributions of MFIs loans towards promoting their market share, product innovation achieving market excellence and the overall economic company competitive advantage. |

**Source:** Extracted by researcher

According to research which was conducted by Massawe (ILO, 2012), it was revealed that the small and medium-enterprises (SMEs) sector is one of the leading employers (next only to peasant agriculture) in Tanzania. It is estimated that there are over one million enterprises in this sector, employing between 3 and 4 million people or 20-30 per cent of the total labor force. The SMEs sector is considered to have the brightest potential for making the highest contribution to employment growth and increased at 10 per cent per annum. Operators are able to generate between 2.5 and 10 times the minimum earnings of civil servants. The SMEs have also shown great potential for creation of wealth. Their aggregate contribution to national income is estimated at 35 and 40 per cent of GDP (Finseth, 1998).SMEs are generally regarded as the driving force of economic growth, jobs creation, and poverty reduction in developing countries. They have been the means through which accelerated economic growth and rapid industrialization have been achieved (Harris and Gibson, 2002; Sauser, 2005.)

## 2.6 Research gap

By considering the above reviewed empirical literature it’s evident that a good number of similar researches have been done, but there are a number of gaps left ranging from geographical to time as well as nature of the organization studied. Banjabeen (2010) conducted a research on the impact of bank loans on households in Pakistan. Despite the study relevance the research conducted in Pakistan where geographical attributes, political and socio culture values differ from Tanzania. (Ohuche and Adenuga, 2013) studied the relationship of credit offered by financial institutions in Nigeria and the growth of SMEs.The study left a gap in time. Lee *et al* (2013) studied the relationship between financing SMEs and actual performance in business in the tourism industry and its effect on growth of enterprises.

The study conducted in China where most of the SMEs operates in an advanced working environment compared to those found in Tanzania. Therefore, their findings cannot be in favor of the Tanzania environment. Despite the fact that a number of research have been done to explore the effect of loan given by financial institutions in relation to SMEs performance, most of them were carried in other countries particularly Asian countries. Very few studies have been done in African countries and Tanzania in particular. According to researcher’s knowledge no study had focused on the effects of microfinance services on the performance of SMEs in Kinondoni in Tanzania. The researcher felt that there was need for a study on this area and thus this study intended to bridge this gap and focus on the effects of microfinance services on performance of SMEs in Dar es salaam Tanzania.

## 2.7 Conceptual Framework

The conceptual framework of the study is the system of concepts, assumptions, expectations, beliefs, and theories that supports and informs your research. Miles and Huberman (1994) state that a conceptual framework “explains, either graphically or in narrative form, the main things to be studied the key factors, concepts, or variables—and the presumed relationships among them”( p.18).Thus, the conceptual framework is a formulation of what you think is going on with the phenomena of this study. Below is the conceptual framework model for this study.

**MICROFINANCE LOAN**

Loan size/amount

Loan processing time

Collateral security

*Dependent variable*

*Independent variable*

**SME PERFORMANCE**

**Operational performance**

Profit / income

Sales

 Investment

**Socio-Economical performance**

 Education

 Health care

 Family affairs

**Figure 2.1: Conceptual Framework**

**Source:** Researcher, 2017

## 2.8 Variables of the Study

### 2.8.1 Independent Variables

An independent variable is the variable that a researcher has control, what researcher can choose and manipulate. It is usually what researcher thought affected the dependent variable. Independent variables under this study are Loan size/amount, loan processing time, and collateral security. These variables were considered to influence the SMEs performance.

### 2.8.2 Dependent Variable

A dependent variable is what researcher measures in the study and what is affected during the study. The dependent variable responds to the independent variable. It is called dependent because it depends on the independent variable (Patton, 1990). In this study the SME Performance was considered as a dependent variable. It was divided into operational and social economic performance of SMEs.

1. Operational performance of SMEs has the following measurements: profit or income generated, sales and investment.
2. Social performance was measured using the following variables: education, health care and family affairs.

# CHAPTER THREE

# 3.0 RESEARCH METHODOLOGY

## 3.1 Overview

This chapter discusses the methodology that was used to collect and analyze data. It shows the research design, area of the study, population and sampling methods. The methodology also shows data collection methods, data collection instruments and data analysis methods.

## 3.2 The Research Design

Research design is the framework or a detailed plan for the study used as a guide in collecting and analyzing data. Gill and Johnson (1997) suggest that research design is the road map used to guide the implementation of the study. Therefore; it is a blueprint that is to be followed in completing a study of activities to be carried out systematically to achieve the research objective**.** This study employed a descriptive research design and was a case study. A case study entails studying a phenomenon within its real-life setting rather than studying a phenomenon in general, a specific example within time and space is chosen for study. This allows a particular issue to be studied in depth and form a variety of perspectives (Barreiro and Albandoz, 2011). In this case the researcher tried to find out the effects of microfinance loans on performance of small and medium enterprises (SMEs) in Tanzania.

## 3.3 Area of the Study

The study was conducted in Dar es salaam to assess the effects of Loans from NMB on performance of small and medium enterprises (SMEs) in Tanzania.NMB is a leading bank in Tanzania. Established in 1997, today it provides quality financial services and insurance products to its retail and corporate customers over two million through its countrywide branch network of 175 outlets, 65 mini-branches and 600 ATMs (NMB, 2015). All NMB branches are connected via satellite communication, and it is regarded locally as a leader among the domestic banks in Tanzania. The researcher selected SMEs borrowers from NMB Bank branches in Dar es Salaam. Dar es Salaam region was chosen because it has many branches of NMB hence constitute a good number of SMEs borrowers from that bank who produced enough data regarding effects of loans they borrowed from the bank on performance of their enterprises. Furthermore, Dar es salaam was chosen as a case study for this study because it has many branches of NMB hence access to data on time and at a reasonable cost.

## 3.4 Target Population of the Study

Population is defined as a full set of cases from which a sample is taken (Saunders et al, 2002). Thus a population refers to the people that the researcher has in mind from whom data can be obtained. Polit and Hungler (1999) define population as the totality of all subjects that confirm to a set of specifications, comprising the entire group of persons that is of interest of the researcher and to whom the research results can be generalized. The study population involved credit beneficiaries from NMB branches in Kinondoni district, estimated to be 600 hence making a total population to have 600 people.

##

## 3.5 Sampling Design and Sample Size

Sampling is referred to as the process of selecting units from a population of interest so that by studying the sample a researcher may fairly generalize his results back to the population from which they were chosen.(Churchill and Iaccobucci,2002) has defined sampling as a selection of a subset of elements from a large group of objects.

### 3.5.1 Sampling Design

### Sampling is done due to constraints of time, money and accessibility of data to the entire population (Cohen, *et al*., 2007). This study employed probability sampling technique. Probability sampling involved a simple random sampling. Simple random sampling was used to select SMEs borrowers from six branches of NMB from Kinondoni district in Dar es Salaam. These borrowers included those who own small and medium businesses and whose business depends on loans from NMB.The aim of using simple random sampling was to make sure that each SMEs borrower had equal chance of being chosen. The study employed a simple random sampling technique in picking the respondents. Brian(2000)noted that: “… this technique allows the researcher pick the sample he/she thinks will deliver the best information in order to satisfy the research objectives in question…”

### The simple random sampling technique was appropriate here since it provides an opportunity for each and every element in the target population or sample to get an equal chance of being selected or included in the final sample and thus increasing the objectivity of the results of the research. The sampling design so selected resulted in cost effectiveness, rendering a possible small sampling error, truly represented the population (true representative sample), minimized and controlled the extent of biasness and the one which presented a good generalization of the findings for the population that was understudy.

### 3.5.2 Sample Size

According to Kothari (2006) sample is a collection of some parts of the population on the basis of which judgment is made, small enough for convenient data collection and large enough to be a true representative of the population from which it has been selected. Sample size refers to a number of items to be selected from the universe to constitute a sample. The sample size consisted of one hundred and six (106) respondents (borrowers from NMB) selected from NMB branches.According to Kothari (2006) in order a sample to be a true representative of a population, it must be at least ten percent of the population. In this study a sample is about 17.7 per cent of the whole population, hence it is a true representative of the population.

## 3.6 Data Collection Methods

In order to accomplish the objectives in this research and come up with the correct results the researcher used primary data. Primary data are those data which are collected afresh from the respondents and for the first time and thus happened to be original in character (Kothari, 2006). Therefore Primary data are original works of research or raw data.

### 3.6.1 Primary Data

Primary data are data collected for the first time. In this study primary data were collected from owners of SMEs who uses loans from NMB to facilitate their businesses.The number been one hundred and six (106). Primary data was obtained through self-administered semi-structured questionnaires. Personal interviews provided the opportunity for the interviewer to clarify issues.

## 3.7 Research Instruments

This study employed three research instruments.

### 3.7.1 Questionnaire

Questionnaire is a set of questions, which are usually sent to selected respondents to answer at their own convenient time and return back the filled questionnaire to the researcher (Kothari, 2004).In this study self-administered questionnaires were distributed to the respondents who filled them and the researcher administer them. This study employed semi structured questionnaire with five likert scale.

### 3.7.2 Interview

According to (Kothari, 2006), an interview is a set of questions administered through oral or verbal communication between the researcher and the interviewee respondent. In this study, semi structured interview was employed in order to get clarifications of some matters from loan beneficiaries.

## 3.8 Instrument Validity and Reliability

### 3.8.1 Instrument Validity

This study employed construct validity whereby the obtained data through the questionnaires represented a theoretical concept meaningfully and accurately. This method was considered reliable after a pilot study was conducted using test-retest method to same group of respondents yielding consistent results. The test-retest method that was used in testing instrument validity yielded consistent results (100% consistency). The questionnaires were also tested for reliability using test-pre-test method to ensure reliability. Some writers acknowledge that validity is concerned with the question of goodness of fit or concurrence between what the researcher has defined as a characteristic of the phenomenon under study and what the researcher is reporting in terms of measurement. The instrument’s validity was further diagnosed as hereunder:

**Internal Validity:** Pilot study was used to test questionnaires. Piloting by testing the questionnaires prior to sending them to the selected sample ensured internal validity of the study. The testing was done so that the questionnaires were reviewed and tested as appropriate. This was done to ensure that the questions asked concentrated on the issues essential to the survey. This also ensured that the right questions with proper ingredients were asked. This increased the reliability of answers and their consistency throughout the survey questionnaires. The questions were checked against a set of questions used in similar researches that were undertaken previously.

**Face Validity:** Validity is the degree to which the findings correctly map the phenomenon in question. The researcher utilized other professionals, research colleagues and other experts to examine the questionnaires to ensure facial validity and the contents. Their comments and suggestions were used to revise the questionnaires before preparing the final instrument.

**Content Validity:** The content validity refers to the representativeness of the item content domain: the manner in which the questionnaire and its items are built to ensure the reasonableness of the claims of content validity. The rigorous procedures used to select the questionnaire constructs to form the initial items, personal interviews with experts, and the iterative procedures of scale purification imply that the instrument had strong content validity.

### 3.8.2 Instrument Reliability

Reliability defined as the extent to which results are consistent overtime (Saunders, Lewis & Thornhill, 2012). Reliability has to do with accuracy and precision of measurement procedures. Pilot study was done to test whether the tools are truly measuring what they intended to measure (Kothari 2007). Reliability of the tool was made by piloting the questionnaires before a comprehensive exercise of data collection to see if the tool can give consistent response from different respondents.

## 3.9 Data Processing and Analysis

After data have been collected, the task that followed was that of analyzing the data for the study. This involved the establishment of categories, the application of the categories to the raw data through coding, tabulation etc., which led to drawing statistical references. In this case, therefore, raw data was classified into some purposeful and usable categories. Tabulation and subsequent analysis of data was made. The researcher employed the use of tables and frequencies and findings represented with the aid of statistical tables. Tabulation, as noted by Kothari (2004; 2006) is the use of tables in analysis and presentations of research data. Tabulation conserves space, reduces explanatory and descriptive statements to a minimum, facilitates comparison and summation of items and provides a basis for various statistical computations. The responses of the subjects were entered into the computer using Statistical Package for Social Science (SPSS) research. The responses from closed ended questions were coded into frequencies and percentages for easy analysis and interpretation. The 5-point Likert Scale and Mean interpretation was made as follows:

**Table 3.1: The 5-Point Likert Scale Interpretation**

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Rating**  |  | **Response Mode**  |  | **Description**  | **Interpretation**  |
| 5  |  | Strongly Agree  |  | Agree with no doubt at all  | Very Satisfactory  |
| 4  |  | Agree  |  | Agree with some doubt  | Satisfactory  |
| 3  |  | Undecided  |  | No idea  | Nil  |
| 2  |  | Disagree  |  | Disagree with some doubt  | Fair  |
| 1  |  | Strongly Disagree  |  | Disagree with no doubt at all  | Poor  |

**Source:** researcher, 2017

The Mean Interpretation was undertaken with the following key:

Strongly Agree 4.5 - 5.0

Agree3.5 - 4.4

Neutral 2.5 - 3.4

Disagree 1.5 - 2.4

Strongly Disagree 0.5 - 1.4

**Model Specification**

Mathematically the model is expressed as follows;

**Model for specific objective 1**

**Equation 1:**

SMEOP = f (LS, LT, COL)

SMEOP = β0**+** β1LS + β2LT + β3COL + ε

Where:

SMEOP = Small and Medium Enterprise Operational Performance

LS = Loan size

LT= Loan processing time

COL = Collateral/security

β0 = intercept, β1 through β3 = Coefficient of the independent variables, ε=error term.

**Model for specific objective 2**

**Equation 2:**

SMESP = f (LS, LT, COL)

SMESP = β0**+** β1LS + β2LT + β3COL + ε

Where:

SMESP = Small and Medium Enterprise Social Performance

LS = Loan size

LT= Loan processing time

COL = Collateral/security

β 0 = intercept, β1 through β3= Coefficient of the independent variables, ε=error term.

## 3.10 Definition and Measurement of Variables

**Table 3.2: Overview the Variables under Discussion in This Research**

|  |  |  |
| --- | --- | --- |
| **Types of Variable** | **Name of Variable** | **Definition of variable/Measurement** |
| Dependent Variable | SME’s Operational performance  | Profit/Income, Sales and Investment |
| SME’s Social economic performance | Education for children, ability to pay medical expenses and family affairs |
| Independent Variables | Loan size | Success factors that measure the effectiveness of loan |
| Loan processing time | Success factors that measure the duration from the time loan application is filed to the time the loan is granted |
| Collateral security | Success factors that measure the creditworthiness of the loan applicants (SMEs). |

**Source:** Researcher (2017)

## 3.11 Measurements of Variables of the Study

The main variables of the study are microfinance loans, SME Operational performance and SME Social-economic performance.

### 3.11.1 Profit/Income Generation

Financing SMEs are important because they are considered as profitable business prospect and provide an opportunity for new job creation. Business profit is considered as a key factor which facilitates entrepreneurial success by providing for the nourishment of competencies such as innovativeness and ability to acquire resources. These competencies are regarded as imperatives to success in many entrepreneurial ventures (Bird 1993; Ronstadt 1984). A researcher didn’t know whether amount of loan offered by bank has the effect on the profit / income of SMEs. Therefore under this study the researcher wanted to examine the effect of loan size given by bank on the SMEs operational performance.

### 3.11.2 Sales

In order to enlarge business through working capital, the SMEs need to request bank loan. Sales data are usually readily available and business owners themselves attach high importance to sales as an indicator of business performance. In addition, sales growth is also easier to measure compared with some other indices and is much more likely to be recorded. Sales are a good indicator of size and growth. Sales may also be considered as a precise indicator of how a firm is competing relative to their market (Barringer *et al*., 2005). Under this study, the researcher investigated the sale volume before and after the bank loan.

### 3.11.3 Investment

The consideration focused on the level of investment attained. Addition of investment may include start of new business which is different from what an entrepreneur is doing or open branch or purchase of new machines or working tools for the purpose of efficient running of the business. The researcher investigated whether there is addition or expansion of investment after utilization of NMB loan.

 **(b) Effect on Socio-economic performance**

The role of SMEs is improving the standard of living of the population and transforming the economy of a nation at large. It aims at improving people’s lives by promoting social changes. Social services or non-financial services that focus on advancing the welfare of SMEs. Enhancing SMEs through financing can solve some of the social problems (Mair and Marti, 2006).

### 3.11.4 Education

The social services which were considered under this study included education.The researcher assessed SMEs before and after bank loan, to see whether there was any improvement, and whether they afford social service costs, for instance payment of scholastic materials.

### 3.11.5 Health care

The social services which were considered under this study included health care. The researcher assessed SMEs before and after bank loan, to see whether there was any improvement, and whether they afford social service costs, for instance payment of medical expenses.

### 3.11.6 Family Affairs

The social services which were considered under this study included family affairs. The researcher assessed SMEs before and after bank loan, to see whether there was any improvement, and whether they helped families of SMEs in solving family matters like decision in building a modern family house from business profit.

## 3.12 Ethical Consideration

Ethical refers to the standards of behavior that guide researchers' conduct in relation to the rights of those who become the subject of research, or are affected by it (Saunders, Lewis and Thornhill, 2007).In this study, the researcher ensured that there is confidentiality of the data provided by the respondents. In addition, researcher ensured anonymity of participant's identities. Before collecting the data, respondents were informed the purpose of the study and the way the results will be used for.

# CHAPTER FOUR

# 4.0 FINDINGS AND DISCUSSION

## 4.1 Overview

This chapter examines the data analysis, presentation, interpretation and the discussion of the findings. In addition, this chapter discusses the findings from the research questions that are an investigation on the effects of microfinance loans on performance of Small and Medium Enterprises (SMEs) in Tanzania; under the following objectives: To examine the effects of microfinance loans size on SME’s operational performance, to analyze the effects of microfinance loans processing time on social welfare of the borrowers and to explore the effects of collateral on loans on operational and social economic performance of SMEs and to explore challenges facing SMEs in obtaining loans from NMB.

The findings of this study were presented and analyzed by using statistical procedures such as mean, standard deviations, frequency tables, and percentages for easy analysis and interpretation of the findings.

## 4.2 Profile Information of the Respondents

This is the information obtained from data collected from the field study and it was used by the researcher in investigation of the problem from the sample of population selected in this study that is the NMB clients(borrowers). It was a demographic characteristics and features of the sample selected from the entire population in the area of the study, the selection was based on the gender of the respondents, age of respondents, academic qualification of the respondents, and duration of services and position of respondents in their business.

### 4.2.1 Presentation of the Descriptive Statistics of Profiles of Respondents

Table 4.1 shows the summary of the descriptive percentage of the respondent's demographic factors including (age, gender, academic qualifications and working experience). The study findings shows that majority of the respondents were aged between 31-40 years (45.3%) followed by those who aged between 41-50 years (34%) Others were aged between 21-30 years (15.7%) and those with ages above 61 years were 1.3%.This implies that age of the respondents can influence these demographic phenomena on the effects of microfinance loans on performance of Small and Medium Enterprises (SMEs) in Tanzania. The age between 21 up to 40 years old is the age of young entrepreneurs who strive for high growth of their businesses. Male respondents were more than female clients in the sampled population implying that the most beneficiaries of loans at NMB who are also the owners of many SMEs in Dar es Salaam are men.

Marital Status of respondents was categorized as married, not married and Widow and divorced. The researcher was interested to know how marital status is related with this small and medium enterprise business. The findings revealed that 83 (78.3%) of total respondents were married while 12(11.3%) were single. In addition, six (6) respondents (5.7%) were from the group of divorced while 4(3.8%) were widows/widower. Considering the educational background of respondents, the results show that the majority of respondents were educated. For example results found that 10 (9.5%) had Master Degree.

Eighteen (16.9%) respondents had bachelor degree, thirty one (29.2%) of respondents were having diploma and 45 (42.5%) were certificate holders. Only2 (1.96%) of the respondents were having PhD degree. In terms of length of service most of the respondents 72(67.9%) have worked as SME owners between 5-10 years followed by 15 (14.2%) respondents who have worked as SME owners for more than 15 years.

**Table 4.1: Respondent’s Biographical data**

|  |  |  |
| --- | --- | --- |
| **Description** | **N** | **Percentage** |
| **Age** |  |   |
| 21-30 | 15 | 15.7 |
| 31-40 | 48 | 45.3 |
| 41-50 | 36 | 34.0 |
| 51-60 | 5 | 4.7 |
| 61 and above | 2 | 1.3 |
| **Gender** |  |   |
| Male | 64 | 60.4 |
| Female  | 42 | 39.6 |
| **Marital status** |  |  |
| Single | 12 | 11.3 |
| Married | 83 | 78.3 |
| Divorced/Divorcee | 7 | 6.6 |
| Widow/Widower | 4 | 3.8 |
| **Academic qualifications** |  |  |
| Certificate | 45 | 42.5 |
| Diploma | 31 | 29.2 |
| Bachelor degree | 18 | 16.9 |
| Master degree | 10 | 9.5 |
| PhD degree | 2 | 1.9 |
| **Working experience** |  |  |
| Less than 5 years | 12 | 11.3 |
| 5-10 years | 72 | 67.9 |
| 11-15 years | 7 | 6.6 |
| Above 15 years | 15 | 14.2 |

**Source:** Field data (2017)

According to findings in Table 4.1, majority of the respondents were aged between 31-40 years(45.3) % followed by those who were aged between 41-50 years(34%). Others were aged between 21-30 years (14.2%) and those with ages above 61 years were 1.8%. This implies that age of the respondents can influence these demographic phenomena on the effects of microfinance loans on performance of Small and Medium Enterprises (SMEs) in Tanzania. The age between 31-40 years old is the age of young entrepreneurs who strive for high growth of their businesses. Status of respondents was categorized as married, not married and widow and divorced. The researcher was interested to know how marital status is related to small and medium enterprise business. The findings revealed that 83 (78.3%) of SME owners were married while 12(11.3%) were single. In addition, seven (7) SME owners (6.6%) were from the group of divorced while 4(3.8%) were widows/widower.

Considering the educational background of respondents, the results show that the majority of respondents had a certificate. The results found that 45 (42.5%) were certificate holders, 31(29.2%) had a qualification of diploma. Eighteen (16.9%) respondents were bachelor degree holders while ten (9.5%) of respondents were holders of master degree. Furthermore, the results show that only 2 (1.9%) respondents were PhD holders. These results signify that most of SMEs owners are certificate holders meaning that most of certificate holders were not absorbed in the formal employment; hence they decided to employ themselves through SMEs.

Table 4.1 shows the period of time which SME’s owners had been working as businessmen/women, the researcher was trying to assess the period undertaken by SMEs in doing such business. He also tried to assess the relationship of microfinance toward SMEs growth over a certain period of time. In terms of length of service most of the respondents 72 (67.9%) have worked as SME owners for a period of between 5-10 years followed by 15 (14.2%) respondents who have worked as SME owners for more than 15 years. Furthermore, the findings showed that 12 (11.3%) SME owners have work experience of less than 5 years while 7 (6.6%) have an experience of 11 to 15 years dealing with SMEs.The findings signify that the majority of SME owners have experience in borrowing and repayment of loans from NMB, hence this shows the duration of which SMEs have been enjoying the social and economic benefits obtained from borrowing from this financial institution (NMB).

### 4.2.2 Amount Applied

Researcher wanted to know the amount of loan applied and granted by NMB to their clients (SMEs).Table 4.2 show the findings.

Table 4.2: Amount of Loan Applied and Obtained from NMB

|  |  |  |
| --- | --- | --- |
| **Amount of loan** | **Frequency** | **Percent** |
| Below 500,000 | 17 | 16.0 |
| 500,000-1,000,000 | 29 | 27.4 |
| 1,000,001-2,000,000 | 50 | 47.2 |
| Above 2,000,000 | 10 | 9.4 |
| **Total** | **106** | **100** |

**Source:** Field data

According to the findings in table 4.2 of SMEs (47.2%) had applied and been granted amount of loan between Tshs1,000,001 and 2,000,000.Twenty nine (27.4%) of SMEsapplied for loan amounting to Tshs 500, 000 and 1,000,000. Seventeen (17) SMEs (16.0%) had secured a loan amounting to less than Tshs.500, 000 while small number of respondent 10 (9.4%) had applied and been granted more than Tshs.2, 000,000. This shows that most of SMEs borrows small amount which does not exceed Tsh.2, 000,000 which implies that SMEs are in small scale business which does not provide opportunity for SMEs to grow.

### 4.2.3 Sales Before Getting The Loan

One of questions in the questionnaire wanted respondents to express how much sales per month they got from their businesses before obtaining the loan from NMB.The question aimed at measuring operational performance using sales (variable).Table 4.3 shows the responses from this question.

**Table 4.3: Sales Before Getting The Loan**

|  |  |  |
| --- | --- | --- |
| **Tshs** | **Frequency** | **Percent** |
| Below 500,000 | 25 | 23.6  |
|  500,001-1000,000  | 30 | 28.3  |
|  1,000,001 – 2,000,000  |  22 | 20.8  |
|  2,000,001 – 3,000,000  | 13  | 12.3  |
|  3,000,001 – 4,000,000  | 10 |  9.4 |
| Above 4,000,000 | 6 |  5.7 |
| **Total** | **106** | **100** |

**Source**: Field data

According to the findings in table 4.3,about twenty eight (28.3) percent of SMEs received sales of between Tshs 500,001 and Tshs.2,000,000 per month before receiving the loan from NMB.This is followed by 23.6 percent of SMEs which receive the sales of below Tshs.500,000.Furthermore,the finding indicates that 12.3 percent of SMEs received the sales of between Tshs.2,000,001 and Tshs.3,000,000.The findings also observed 9.4 percent of SMEs receiving the sales of between Tshs.3,000,001 and 4,000,000 while only 5.7 percent of SMEs recorded sales of above tshs.4,000,000 per months. The significance of these findings is that SMEs experience the shortage of funds to boost their business.

### 4.2.4 Sales per Month After Getting The Loan from NMB

A question in a questionnaire wanted respondents to express how much sales per month they got from their businesses after employing loan obtained from NMB.The question aimed at measuring operational performance using sales (variable) in order to compare sales before and sales after utilizing loan from NMB.Table 4.4 shows the responses from this question.

**Table 4.4: Sales per Month after Getting the Loan**

|  |  |  |
| --- | --- | --- |
| **Tshs** | **Frequency** | **Percent** |
| Below 1,000,000 | 6  | 5.7  |
| 1,000,001-3000,000  |  10 | 9.4  |
|  3,000,001 – 5,000,000  | 33 | 31.2  |
|  5,000,001 – 7,000,000  | 24   | 22.6  |
|  7,000,001 – 9,000,000  | 18 | 16.9  |
| Above 9,000,000 |  15 | 14.2  |
| **Total** | **106** | **100** |

**Source**: Field data

According to the findings in table 4.4,Thirty one point two (31.2) percent of SMEs received sales between Tshs 3,000,001 and Tshs.5,000,000 per month after utilizing the loan received from NMB.This is followed by 22.6 percent of SMEs which received the sales of between Tshs.5, 000,001 and 7,000,000 per month. Furthermore, the finding indicates that 16.9 percent of SMEs received the sales of between Tshs.7,000,001 and tshs.9,000,000.The findings also observed 15 percent of SMEs receiving the sales of more than 9 million while only 5.7 percent of SMEs received sales below Tshs.1,000,000 per months. These findings indicate that NMB loans boost both sales and profits of many SMEs and hence enhancing their growth.

### 4.2.5 Gross Profit Obtained Before Getting the Loan

In order to measure operational performance using profit/income variable, a question in the questionnaire wanted respondents to express how much profit per month they got from their businesses before getting the loan from NMB.Table 4.5 shows the responses from this question.

**Table 4.5: Gross Profit Obtained Before Getting the Loan**

|  |  |  |
| --- | --- | --- |
| **Tshs per month** | **Frequency** | **Percent** |
| Below 100,000 | 25 | 27.2 |
| 100,001-500,000 | 31 | 31.5 |
| 500,001 – 1,000,000 | 23 | 19.6 |
| 1,000,001 – 2,000,000 | 11 | 10.9 |
| 2,000,001 – 3,000,000 | 8 | 5.4 |
| 3,000,001 – 4,000,000 | 5 | 3.6 |
| Above 4,000,000 | 3 | 1.9 |
| **Total** | **106** | **100.0** |

**Source**: Field data

According to the findings in table 4.5, thirty one point five (31.5) percent of SMEs received gross profit between Tshs.100, 001 and Tshs.500, 000 per month before receiving the loan from NMB.This is followed by 27.2 percent of SMEs which received the gross profit below Tshs.100, 000.Furthermore; the findings indicate that 19.6 percent of SMEs attained the profit of between Tshs.500, 001 and Tshs.1, 000,000 per month. The findings also observed 10.9 percent of SMEs receiving the profit of between Tshs.1, 000,001 and 2,000,000 while 5.4 percent of SMEs attained gross profit between Tshs.2, 000,001 and Tshs.3, 000,000per months. In addition, the findings showed that 3.6 percent of SMEs attained the gross profit of between Tshs.3, 000,001 and Tshs. 4,000,000 per month while the small number of SMEs 1.9 percent attained the profit of above 4 million per month. The significance of these findings is that SMEs received small gross profit because of small capital they possess in their business; hence they need loan from financial institutions.

### 4.2.6 Gross Profit Obtained After Getting the Loan

In order to measure operational performance using profit/income variable a researcher asked respondents to express how much profit per month they got from their businesses after utilizing the loan received from NMB.Table 4.6 shows the responses of SMEs on this question.

Table 4.6: Gross Profit Obtained After Employing Loan From NMB in Business

|  |  |  |
| --- | --- | --- |
| **Tshs** | **Frequency** | **Percent** |
| Below 100,000 | 2 | 1.9 |
| 100,001-1000,000 | 10 | 9.4 |
| 1,000,001 – 2,000,000 | 12 | 11.3 |
| 2,000,001 – 3,000,000 | 22 | 20.8 |
| 3,000,001 – 4,000,000 | 24 | 22.6 |
| 4,000,001 – 5,000,000 | 30 | 28.3 |
| Above 5,000,000 | 6 | 5.7 |
| **Total** | **106** | **100** |

**Source:** Field data

The finding in table 4.6 shows that twenty eight point three (28.3) percent of SMEs received gross profit between Tshs.4, 000,001 and Tshs.5, 000,000 per month after employing the loan from NMB.This is followed by 22.6percent of SMEs which received the gross profit between Tshs.3, 000, 001 and Tshs.4, 000,000.Furthermore, the findings indicate that 20.8 percent of SMEs received the gross profit of between Tshs.2,000, 001 and Tshs.3, 000,000 per month. The findings also show that 11.3 percent of SMEs receiving the gross profit of between Tshs.1, 000,001 and 2,000,000 while 5.7 percent of SMEs recorded gross profit above Tshs.5, 000,000 per months. The significance of these findings is that the gross profit per month received by SMEs increased after the increment of sales attributed to loan obtained from NMB.The shows that after sales being boosted by loans received from NMB the SMEs’ performance improved than ever prior to obtaining the loan.

## 4.3 Microfinance Loans and Performance of SMEs

The general objective of the study was to examine the effects of microfinance loans on SME’s performance. To achieve this objective, multiple linear regressions were done on the components of loan which are profit/income, sales, investments explanatory variables of operational performance. Correlation is a term that refers to the strength of a relationship between two variables. Correlation coefficients -1.00 represent a perfect negative correlation while a value of +1.00 represents a perfect positive correlation. A value of 0.00 means no relationship between the variables under testing. Table 4-7 (below) describes the relationship between Loan received and Small and Medium Enterprise Operational performance variables. Pearson correlation was used given a two tail test (2-tailed).

The results summarized in a Pearson correlation matrix indicate that the correlation coefficient between Loan given and operational performance of SMEs is positive with 0.833. The probability Value (P-value) is 0.000 less than the significance level which is 0.05. Loan received and SME operational performance move together in the same direction

### 4.3.1 The Mean Distribution of the Responses from the Impact of Micro Finance on the Performance of SMEs Questionnaire Statements

In order to answer the research questions, first distribution of the responses to main statements on the impact of microfinance loan on the performance of SMEs questionnaire were computed. Table 4.7, which shows the mean distribution of the responses to main statements on the impact of microfinance loan on the performance of SMEs questionnaire, gives an insight into the general perception of the respondents on each variable. i.e. three dimensions of SME operational performance (Profit/Income, sales and Investment) and social performance (Education ,Health care and Family affairs).

The mean of the responses to some statements that relate to Profit or Income generation (statements 1, 2, 3 & 4) are high i.e. above 3.5 marks. Findings show that, majority of the respondents show willingness to ask for a loan in order to increase the profit so as to contribute to the growth of the SME. Furthermore, majority of respondents were proud to look for a micro loan and thinks that the choice to borrow from NMB was right because they perceive that loan obtained help to increases income generating activities. This suggests that customers of NMB are to some extent concerned about the performance of the SMEs. Moreover, statement "decision making in family increases as the income generated increase confidence” had the lowest average (3.17). In addition, the mean of the responses to some statements that relate to Investment in SMEs are also high i.e. above 3.5 marks. These responses to the statements that relate to the intention to start new business or expand the existing one. However, the mean of the responses to some statements that relate sales or revenue are below 3.5 marks. These responses show that some SME owners are uncertain about continuing borrowing from NMB.

**Table 4.7: The Mean Distribution of the Responses from impact of micro finance on the performance of SMEs Questionnaire Statements**

|  |  |  |
| --- | --- | --- |
| **QN** | **Questionnaire statements** | **Mean** |
|  | **Profit** |  |
| 1 | Loan obtained increased profit | 3.50 |
| 2 | Loan obtained help to increases income generating activities | 3.52 |
| 3 | Helps improving Business | 3.61 |
| 4 | Loan increase level of business income for SMEs | 4.38 |
|  | **Sales** |  |
| 5 | Loan obtained increased sales | 3.98 |
| 6 | Loan help in controlling over savings account  | 3.12 |
| 7 | Loan employed causes the increase in sales volume and rate of stock turnover | 4.83 |
|  | **Investment** |  |
| 8 | Loan obtained helps in starting a new business | 3.85 |
| 9 | Profit obtained after employing loan helps in expanding the existing business | 3.68 |
| 10 | Profit obtained after employing loan helps in acquisition of assets | 3.79 |
| 11 | Loans Creates Employment potential when used wisely | 3.89 |
| 12 | Profit obtained after employing loan helps in building modern family house | 3.65 |
|  | **Education** |  |
| 13 | Improved social services like education for children | 3.79 |
| 14 | Loan can increase self-efficacy when used wisely | 3.48 |
|  | **Health care** |  |
| 15 | Profit obtained after employing loan helps in obtaining medical expenses for the family | 4.29 |
| 16 | Profit obtained after employing loan helps in joining health service schemes like NHIF | 3.64 |
| 17 | Profit obtained after employing loan helps in joining health insurance services | 3.43 |
|  | **Family affairs** |  |
| 18 | One of the few serious consequences of not borrowing from NMB would be the scarcity of available alternatives | 3.12 |
| 19 | One of the major reasons I continue to borrow from NMB is that leaving would require considerable personal sacrifice (another Bank may not match the overall benefit I have here). | 2.98 |
| 20 | Profit obtained after employing loan helps in obtaining family needs  | 3.16 |
| 21 | Decision making in family increases as the income generated increase confidence | 3.17 |
| 22 | Loan obtained improves borrowers living standards  | 4.40 |
| 23 | Create awareness to borrowing and resettlement  | 4.40 |
| 24 | Promote respect and social dignity  | 4.67 |
|  | **Loan size/amount** |  |
| 25 | The amount of loan received is sufficient | 3.23 |
|  | **Loan processing time** |  |
| 26 | Loan processing time is very short | 3.56 |
| 27 | Loan processing time is moderate | 3.57 |
| 28 | Long processing time is very long | 4.00 |
|  |

**Source:** Field data (2017)

### 4.3.2 Descriptive Statistics for Impact of Microfinance Loan on SMEs Performance

Table 4.7 above represents the mean value for overall Impact of microloan on SME operational performance in three dimensions (Income or profit, sales and investment) and SME social-economical performance (educational, health care and family affairs). Since the average level of operational performance is represented by (mean =3.71, SD = 1.002) it is evident that large number of owners of SMEs believes in the values benefit obtained from the microloan obtained from NMB. Increase in Sales revenue (mean =3.68 and SD =0.774) gives evidence that a large number of SMEs portrayed beyond average level of operational performance.

In addition, investment (mean = 3.26, SD = 0.726) shows that SMEs uses the loan obtained to expand their investments. However, mean values for children education, health care and family matters were 3.98, 3.96 and 4.07 respectively. The aggregate mean value indicates that SMEs perform high in operational and social economical performance.Standard deviations for both variables are close to 1 which is at an acceptable level.

**Table 4. 8: Descriptive Statistics**

|  |  |  |
| --- | --- | --- |
|  | **Mean** | **Std. Deviation** |
| **Statistic** | **Std. Error** |
| PI | 3.71 | .097 | 1.002 |
| SA | 3.68 | .075 | .774 |
| INV | 3.26 | .071 | .726 |
| ED | 3.98 | .064 | .656 |
| HC | 3.96 | .083 | .850 |
| FA | 4.07 | .071 | .724 |

**Source:** Field data (2017)

### 4.3.3 Results of Correlation between Impact of Microfinance Loan and SME performance

The focus of this study is examining the relationship between microfinance loan and SME performance. Pearson Correlation Analysis conducted to verify the existence of relationship between the independent variables: loan size/amount, time of processing loan, collateral security and the dependent variable profit/income, children education, health care as shown in Table 4.9. Results revealed that the Pearson Correlation Coefficient matrix for the relationship between loan characteristics on SMEs Performance for two-tailed test were significant and positive related, (r = 0.387\*\* p <0.01 and 0.436\*\* p <0.00) respectively. However, result shows that relationship between collateral securities with SMEs performance (profit/income) is not significant. (r =0.187).This result indicates that there is a relationship which is significant and positive between loan characteristics and SMEs performance.

**Table 4.9: Pearson Correlation Matrix**

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  |  **LS** |  **LT** | **COL** | **PI** | **ED** | **HC** |
| LS | Pearson Correlation | 1 |  |  |  |  |  |
| Sig. (2-tailed) |  |  |  |  |  |  |
| N | 106 |  |  |  |  |  |
| LT | Pearson Correlation | .251\*\* | 1 |  |  |  |  |
| Sig. (2-tailed) | .000 |  |  |  |  |  |
| N | 106 | 106 |  |  |  |  |
| COL | Pearson Correlation | .472\*\* | .565\*\* | 1 |  |  |  |
| Sig. (2-tailed) | .000 | .000 |  |  |  |  |
| N | 106 | 106 | 106 |  |  |  |
| PI | Pearson Correlation | .387\*\* | .436\*\* | .187 | 1 |  |  |
| Sig. (2-tailed) | .001 | .000 | .020 |  |  |  |
| N | 106 | 106 | 106 | 106 |  |  |
| ED | Pearson Correlation | .288\*\* | .286\*\* | .065 | .741\*\* | 1 |  |
| Sig. (2-tailed) | .002 | .002 | .506 | .000 |  |  |
| N | 106 | 106 | 106 | 106 | 106 |  |
| HC | Pearson Correlation | .366\*\* | .275\*\* | .118 | .718\*\* | .797\*\* | 1 |
| Sig. (2-tailed) | .001 | .002 | .230 | .000 | .000 |  |
| N | 106 | 106 | 106 | 106 | 106 | 106 |

**Source: Field data (2017)**

**\*\* Correlation is significant at 0.01 levels (2-tailed test)**

## Furthermore correlation analysis found slightly significant impact on Loan size and loan time with SMEs performance in terms of education for children (r = 0.288\*\* p <0.02 and r = .286\*\* p < 0.02) respectively. Results found no significant relationship between collateral with SME performance (r = .065). In additional, results shows strong relationship between Loan size with SME performance (r = .366\*\* p <0.01) and slightly significant relationship between Loan processing time with SME performance in terms of health care (r .275\*\* p <0.02). Furthermore there was no relationship found between collateral with SME performance in terms of health care (r = .118).

**Table 4.10: Model Summary**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | **R** | **R Square** | **Adjusted R Square** | **Std. Error of the Estimate** |
| 1 | .462a | .213 | .209 | .152 |

**Source:** Field data

Results from Table 4.11. indicates that the value of Adjusted R squire is 0.209, which shows that Small and Medium Enterprise Performance has 20% influences on loan size, loan processing time and collateral security. Results show that SME performance (both operational and socio economical) has a significant relationship on loan size and loan processing time (β =.283, p=0.002) and (β = 0.269, p= 0.003) respectively. SME performance has no significant impact to collateral security compared to loan size and loan processing time (β =.212, p=0.010). These findings show that SME performance has a significant and positive relationship on two dimensions of loan (loan size and loan processing time).

**Table 4.11: Coefficientsa**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Model** | **Unstandardized Coefficients** | **Standardized Coefficients** | **t** | **Sig.** |
| **B** | **Std. Error** | **Beta** |
| 1 | (Constant) | 3.126 | .376 |   | 8.308 | .000 |
| LS | .270 | .292 | .353 | 7.827 | .001 |
| LT | .202 | .205 | .347 | 7.615 | .002 |
| COL | .154 | .133 | .310 | 5.185 | .007 |
| **a. Dependent Variable: SMEOP** |

|  |
| --- |
| **Model Summary** |
| **Model** | **R** | **R Square** | **Adjusted R Square** | **Std. Error of the Estimate** |
| 1 | .382a | .461 | .430 | .289 |

**Source: Field data**

Table 4.12 shows that SME Operational Performance has 43% impact on loan characteristics (loan size, loan processing time and collateral security). Results show that SME Operational Performance has a strong and significant relationship on loan size (β = .353, p= 0.001).Loan processing time has significant relationship with SME Operational Performance (β =.347, p=0.002). Collateral security has very slightly significant impact to SME Operational performance (β =.310, p=0.007). These findings show that SME Operational performance has a significant and positive relationship on loan size and loan processing time but has no significant relationship with collateral security.

**Table 4.12: Coefficientsa**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Model** | **Unstandardized Coefficients** | **Standardized Coefficients** | **t** | **Sig.** |
| **B** | **Std. Error** | **Beta** |
| 1 | (Constant) | 2.806 | .447 |   | 6.276 | .000 |
| LS | 2.668 | .409 | .416 | 6.058 | .001 |
| LT | 1.421 | .304 | .394 | 5.976 | .003 |
| COL | .953 | .936 | .913 | 5.109 | .005 |
| **a. Dependent Variable: SMESP**  |
| **Model Summary** |
| **Model** | **R** | **R Square** | **Adjusted R Square** | **Std. Error of the Estimate** |
| 1 | .583a | .340 | .319 | .125 |

Table 4.13 shows that loan characteristics (loan size, loan processing time and collateral security) has 31% impact on SME social-economical performance. Results shows that loan size and loan processing time has strong and significant relationship on SME social economic performance (β = 0.416, p= 0.001) and (β =.394, p=0.003) respectively. In addition, collateral security has moderate significant relationship on SME social performance compared to loan size and loan processing time, (β =.223, p=0.007). Findings show that SME social performance has a slightly significant relationship with loan characteristics.

## 4.4 Discussion of the Findings

The present study examines the effects of Microfinance loans on performance of Small and Medium Enterprises (SMEs) in Tanzania, taking a study of Kinondoni SMEs in Dar es salaam. The findings show that most of the respondents feel that the loans obtained from NMB helps SMEs operationally and socially. In line with research question 1 about the effects of microfinance loans size on SME’s operational performance result found high performance to the most of SMEs who obtained loans from NMB in terms increased gross profit, increase in sales volume (stock turnover) meaning that there is enjoyment of economies of scale. In line with research question 2 on effects of microfinance loans processing time on social welfare of the borrowers, the findings show positive and significant relationship between loan processing time and social welfare of the borrowers.

These findings are in line with previous empirical works of Veselin *et al*, (2012) and Waithanji (2014) who affirmed that SMEs operational performance dimensions; profit/income, sales and investment have positive and significant relationship with operational performance. However, the results are contrary to the findings of Zavatta, (2008) who studied the relationship of sales and investment with operational performance. He found no relationship existed between sales and investment and operational performance of SMEs. Both sales and investment were found un-related to operational performance of SMEs.

In line with research question 3 to explore the effects of collateral of loans from NMB on performance of SMEs the findings confirmed that collateral and operational performance were positively related to low degree of significance. This implies that SMEs who does not have collateral do not satisfy the requirement of NMB to receive a loan. In so doing, no collateral, no loan and hence operational performance becomes low. The findings support study conducted by (Quianoo, 2014) who revealed that SMEs performance increases as the level of collateral needed by financial institutions decreases. However, study conducted by Sabrahmanya (2010) found that there is no significant relationship between collateral and organizational performance.

#

# CHAPTER FIVE

# 5.0 CONCLUSION AND RECOMMENDATIONS

## 5.1 Overview

This chapter presents conclusion, recommendations and areas for further study.

## 5. 2 Conclusion

The effects of microfinance loans on performance of SMEs in Kinondoni districts in terms of operational and social performance have been investigated. Results from the study indicated that there were significant increases in the average monthly gross profit of SMEs after employing loan obtained from NMB over time. In order to sustain microfinance loans impact on clients, it was observed from the study that, there is a need to increase the amount/size of the loan offered to SMEs so as to enhance the performance and financial sustainability of these SMEs. Furthermore, the findings have indicated that, the contribution of microfinance loans in the growth of SMEs as indicated by the field results that showed the following highly positive ratings: creation of employment with 3.89 mean, increase in level of business income with 4.38 mean, asset accumulation with 3.79 mean, improve borrowers living standards with 4.40 mean, create awareness to borrowing and resettlement with 4.40 mean, and promote respect and social dignity with 4.67 mean of the total sample responses.

In addition, micro-loan facilities have enormous outcomes to borrowers at the household level in urban communities in Dar es Salaam. Borrowing and using micro-loan has increased the capacity of the poor to overcome financial vulnerability. Many credit users have met household and business needs like medical, education and expansion of their businesses hence improvement in their standards of living. Micro-loans have boosted businesses and many micro-entrepreneurs owe success to borrowing and using micro-loans. People of different socio-economic status, knowledge, experience, exposure and geographical location; from urban settings have different success stories concerning micro-loan usage.

Moreover, the researcher concludes also that a micro-credit facility is, no doubt, a good innovation for developing low income earners of our society, as it enhances the productive capacity of the SMEs to participate in income generating activities. For a long period of time commercial banks neglected the poor members of our society who lack conventional collateral security like land ownership document; building ownership document, equipment and third part guarantee on realizing this gap, Microfinance Institutions (MFIs) came in to extend affordable and easily payable loans to SMEs through micro-loan schemes. Micro-loans, as a result, enable low income earners, in Dar es Salaam, to expand and develop their income generating activities, enhancing their bargaining power and interests within the household and support payment of household necessities like medical care and education among others, thereby contributing to the welfare of their household.

## 5.3 Recommendations

The Government is called upon to undertake the preparation of an appropriate way for credit lending institutions to further penetrate and reach out even to the poorest of the poor in both rural and urban areas since the study has found out that micro-credits greatly improve the wellbeing of entrepreneurs at urban areas. There is also a need for the Government to appreciate the socio-economic conditions, knowledge, attitudes, perceptions, cultural beliefs and practices of credit borrowers and a critical consideration of these issues will have a high impact in enabling lending institutions to tailor their financial services to the needs of the clients and low income earners in developing communities. It has also been apparent that micro-credit institutions provide important services for clients neglected by the formal banking sector.

This study also calls for immediate measures to revamp micro-credit policies in the country (Tanzania). It is also recommended that micro-credits, in their present form, should not only be considered for their alleged poverty alleviating qualities, but also as subsidies in support of an alternative small-scale banking sector. As long as social development funds are directed to microfinance institutions, qualitative and quantitative indicators of social progress achieved through micro-credit lending should be among the basis of assessment of growth and social development. A core issue in this respect is the working conditions of micro-entrepreneurs and their employees.

It is not enough to know that loans have been repaid; micro-credit institutions should also account for the social and economic impact their programs have on their clients. For the case of Micro-loan providers, they should be able to expand their loan facilities to reach out the vast majority of the poor population in the country, both in rural and urban areas. As it has been pointed out earlier, for a long period of time commercial banks neglected the poor members of our society who lack conventional collateral security like land title. In realizing this gap, Microfinance Institutions (MFIs) should come in full force to capture this niche and extend affordable and easily payable loans to the poor people through micro-loan schemes. Micro-loans, as a result, will enable low income earners, to expand and develop their income generating activities, enhancing their bargaining power within the household and be able to support payment of household necessities like medical care and education among others, thereby contributing to the welfare of the household and, finally, to the economy of the country as a whole.

## 5.4 Limitations

The researcher came across some limitations in collecting data. Some of respondents were not ready to disclose some information pertaining to the amount of loan obtained from NMB, income and expenditure. This is because they associated the questionnaire with enquiry from Tanzania Revenue Authority (TRA).

## 5.5 Delimitations

The researcher insisted that the information required were for academic purposes only, showing letter of introduction from OUT Management and assuring them anonymity the respondents accepted to respond to questions in the questionnaires.

## 5.6 Areas for Future Research

The study assessed the effects of Microfinance loans on performance of Small and Medium Enterprises (SMEs) in Tanzania, taking a study of Kinondoni district SMEs in Dar es salaam.Suggestions for future studies are provided accordingly. Other researchers should consider investigating effects of Microfinance loans on performance of Small and Medium Enterprises (SMEs) in Tanzania in other geographical areas in Tanzania for the purpose of making comparative study on the findings.Future research may further study and analyse the relationship between loan financing using intermediate variable to get a clear picture of the antecedents and consequences of loans on performance.

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# APPENDICES

Dear Respondent,

My name is **Geofrey L.Nyamwihula,** I am pursuing Master of Business Administration programme in Finance at Open University of Tanzania. I am conducting a study, “The effects of Microfinance loans on performance of Small and Medium Enterprises (SMEs) in Tanzania.” Will you please assist my study by filling and answering the questionnaire. I assure you that your answers will be kept confidential and your names shall not be disclosed except for this study.

Please tick the appropriate answers or fill the space provided. Thank you in advance for your response.

**PART ONE: Personal Information**

**Section A: Background Information of the Respondents**

1. Profile of respondents

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Sex** | **Age** | **Marital Status** | **Educational Level** | **Experience** |
| 1).Male2).Female | 1) 21 – 30 years2) 31 - 40 years3) 41 – 50 years4) 51 - 60 years5) 61 and above | 1). Single2).Married3).Divorced/Divorcee4).Widow/widower | 1) Certificate2)Diploma2).Bachelor degree3).Master degree4).PhD | 1).Less than 5 years2).5 – 10 years3).11 – 15 years4) Above 15 years |

2. How much money you applied for at NMB?

|  |  |
| --- | --- |
| **Amount of loan** | **Put a tick where applicable** |
| Below 500,000 |  |
| 500,000-1,000,000 |  |
| 1,000,001-2,000,000 |  |
| Above 2,000,000 |  |

3 How much sales have you been getting before obtaining the loan from NMB?

|  |  |
| --- | --- |
| **Tshs** | **Put a tick where applicable** |
| Below 500,000 |  |
|  500,001-1000,000  |  |
|  1,000,001 – 2,000,000  |  |
|  2,000,001 – 3,000,000  |  |
|  3,000,001 – 4,000,000  |  |
| Above 4,000,000 |  |

4 How much sales have you been getting after employing the loan from NMB?

|  |  |
| --- | --- |
| **Tshs** | **Put a tick where applicable** |
| Below 1,000,000 |  |
|  1,000,001-3,000,000  |  |
|  3,000,001 – 5,000,000  |  |
|  5,000,001 – 7,000,000  |  |
|  7,000,001 – 9,000,000  |  |
| Above 9,000,000 |  |

5. How much gross profit have you been getting before getting the loan from NMB?

|  |  |
| --- | --- |
| **Tshs per month** | **Put a tick where applicable** |
| Below 100,000 |  |
| 100,001-500,000 |  |
| 500,001 – 1,000,000 |  |
| 1,000,001 – 2,000,000 |  |
| 2,000,001 – 3,000,000 |  |
| 3,000,001 – 4,000,000 |  |
| Above 4,000,000 |  |

6 How much gross profit you are gettingafter employing the loan from NMB?

|  |  |
| --- | --- |
| **Tshs per month** | **Put a tick where applicable** |
| Below 100,000 |  |
| 100,001-500,000 |  |
| 500,001 – 1,000,000 |  |
| 1,000,001 – 2,000,000 |  |
| 2,000,001 – 3,000,000 |  |
| 3,000,001 – 4,000,000 |  |
| Above 4,000,000 |  |

**PART II: Statements relating to impact of micro finance loan on the performance of SMEs**

7. Give your opinion on these statements regarding the benefits accruing from the loan obtained from NMB.

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **QN** | **Questionnaire statements** | **Strongly agree** | **agree** | **Not sure** | **disagree** | **Strongly disagree** |
|  | **Profit** |  |  |  |  |  |
| 1 | Loan obtained increased profit |  |  |  |  |  |
| 2 | Loan obtained helped to increase income generating activities |  |  |  |  |  |
| 3 | Helped Business growth |  |  |  |  |  |
| 4 | Loan increased level of business income for SMEs (same as 1 above) |  |  |  |  |  |
|  | **Sales** |  |  |  |  |  |
| 5 | Loan obtained increased sales |  |  |  |  |  |
| 6 | Loan help in controlling savings account  |  |  |  |  |  |
| 7 | Loan employed causes the creation of employment in SMEs |  |  |  |  |  |
|  | **Investment** |  |  |  |  |  |
| 8 | Loan obtained helps in starting a new business |  |  |  |  |  |
| 9 | Profit obtained after employing loan helps in expanding the existing business |  |  |  |  |  |
| 10 | Profit obtained after employing loan helps in acquisition of assets |  |  |  |  |  |
| 11 | Loans Creates Employment potential when used wisely |  |  |  |  |  |
| 12 | Profit obtained after employing loan helped in building modern family house for  |  |  |  |  |  |
|  | **Education** |  |  |  |  |  |
| 11 | Improved social services like education for children |  |  |  |  |  |
| 13 | Loan obtained increased my self-efficacy  |  |  |  |  |  |
|  | **Health care** |  |  |  |  |  |
| 14 | Profit obtained after employing loan assisted to increase ability to pay medical expenses for the family |  |  |  |  |  |
| 15 | Profit obtained after employing loan enabled me to join health service schemes like NHIF |  |  |  |  |  |
| 16 | Profit obtained after employing loan helps in joining health insurance services |  |  |  |  |  |
|  | **Family affairs** |  |  |  |  |  |
| 17 | One of the few serious consequences of not borrowing from NMB would be the scarcity of available alternatives |  |  |  |  |  |
| 19 | One of the major reasons I continue to borrow from NMB is that leaving would require considerable personal sacrifice (another Bank may not match the overall benefit I have here). |  |  |  |  |  |
| 20 | Profit obtained after employing loan helped me in obtaining family needs  |  |  |  |  |  |
| 21 | Decision making in family increased as the income generated increased my confidence |  |  |  |  |  |
| 22 | Loan obtained improved SMEs/ borrowers living standards  |  |  |  |  |  |
| 23 | Increased income created awareness to borrowing and resettlement  |  |  |  |  |  |
| 24 | Promote respect and social dignity  |  |  |  |  |  |
|  | **Loan size/amount** |  |  |  |  |  |
| 25 | The amount of loan received is sufficient |  |  |  |  |  |
|  | **Loan processing time** |  |  |  |  |  |
| 26 | Loan processing time is very short |  |  |  |  |  |
| 27 | Loan processing time is moderate |  |  |  |  |  |
| 28 | Loan processing time is very long |  |  |  |  |  |

THANK YOU FOR YOUR COOPERATION