

FACTORS AFFECTING LOAN ACCESSIBILITY TO SMALL AND MEDIUM ENTERPRISES: EVIDENCE FROM TANZANIA

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ABSTRACT

The study examined factors affecting loan accessibility to Small and Medium Enterprises(SMEs) from formal credit institutions basing on demand. Specifically the study examined terms and conditions of acquiring loan from institutions. Both primary and secondary data were collected. Primary data were collected from 60 respondents through interview, questionnaire from official member of credit institutions and individuals from small and medium enterprises. Secondary data were collected through documentary reviews.The findings revealed that Financial Institutions offer loans with stiff conditions and most of applicants fail to meet those conditions including interest rates, collateral, loan procedures, business plan, business registration and repayment schedule. However, others who are engaged in retail shop and carpentry are managing to meet loan requirement. It is therefore recommended that government and Non Government Organizations should set up policy option which will favour entrepreneur by regulating conditions for loan accessibility to enable growth of their business.

Key Words: Loan, Small and Medium Enterprises, Institution, Financial Institution, and Formal Credit

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INTRODUCTION

Small enterprises are undertakings engaging between 5 and 49 employees or with capital investment from Tshs. 5 million to Tshs. 200 million while Medium enterprises employ between 50 and 99 people or use capital investment from Tshs.200 million to Tshs.800 million, (URT, 2003). SMEs all over the world are known to play a major role in social economy development by contributing significantly to employment creation, income generation and stimulation of growth in both urban and rural areas (URT, 2003).

Given the great potential of small and medium sized enterprises to bring about social and economic development, it is of no surprise that the performance of SMEs is of huge concern to the government of different countries in the world. Small and medium sized enterprises in both developing and developed countries plays important roles in the process of industrialization and economic growth (Williams, 2006). Other study finds that the SME sector remains underdeveloped mainly due to inability to raise internal and external finance (Hutchinson, 2006).

Tanzania's economy is characterized by a relatively small and medium firms. Access to finance is one of the main barriers to the establishment and development of SME's (Olomi, 2009). The growth of SME's depends much on credit accessibility from Financial Institutions (Scheel, 2006).. However, access to credit has been found to be the biggest constraints for SMEs (Stephanou, 2005). According to the existing literature, the growth of SMEs encountered with many constrains which include management problems, labour skills, regulation and lack of access to finance (Bink et al, 1997). Lack of access to finance lead to inability of buying necessary inputs, delaying investment and closing down the firm due to liquidity problems. It is widely acknowledged that financing constraints limit the investment capacity of SMEs by hampering their growth (URT 2003).

Despite efforts of government and private sector in promoting accessibility of loan to small and medium enterprises, still there is inaccessibility to credit exist. These create bases for this study to examine factors affecting loan accessibility to SMEs from formal credit institutions basing on demand side.

Data and Methodology

The study involved a case study design. Both primary and secondary data were used. Primary data was obtained from officials of different credit institutions and businessmen by using Interviewer Administered Questionnaire. While secondary data was obtained from published, unpublished documents and relevant literature including reports, books, and internet. The Sample size comprised of 60 respondents whereby 58 respondents were from small and medium enterprises and 2 loan officers from CRDB and NMB.

The collected raw data were processed and analyzed through SPSS programme version 16. Descriptive statistics was mainly used to describe the problem under the study. A cross tabulation was used to understand the relation between SMEs and Financial Institutions.

Results and Discussion

With respect to activities performed by SMEs in Tanzania, It is estimated that third percentage of GDP originates from the Small and Medium Enterprises (SMEs) sector. Findings revealed that some of respondents (33.3%) are engaged into retail shop followed by carpentry (26.7%) compared to those dealing with food vending (13.3%) and those dealing with selling charcoal (5%). While saloon (13.3%), stationary (6.7%) and only 1.7% engaged on other business. This implied that majority of respondent are engaged with small and medium enterprises.

Table 1: Activities performed by SMEs in the study area

Activities	Frequency	Percent
Retail shop	20	33.3
Carpentry	16	26.7
Saloon	8	13.3
Selling charcoal	3	5.0
food vendors	8	13.3
Stationary	4	6.7
Others	1	1.7
Total	60	100.0

Source: Field data,2012.

Factors hindering SMEs to access loan from Financial Institution

The study revealed that credit awareness, Business skills and financial management skills as well as terms and condition for acquiring loan from Financial Institution are major factors hindering owners of SMEs to accesses loan.

(i) Credit Awareness

The credit awareness was found to influence individual chances to access credit from formal credit sources. Findings show that 48.3% of respondents were not aware on availability of credit while more than half of the interviewed respondents (51.7%) were conscious on credit accessibility from formal financial source (Table 2). This implied that, awareness on credit availability had a positive relationship with access to credit, implying that those who are aware on availability of credit services have better chances to access credit than those who are not aware.

Table 2: Awareness about access to credit

Awareness	Frequency	Percent
Aware	31	51.7
Not aware	28	48.3
Total	60	100.0

Source: Field data, 2012.

(ii) Business skills & financial management skills

Findings show that majority of respondents (70%) had no business skills, 7% had skills on record keeping, 6% had skills on business control while 5% had skills on financial management skills (Table 3). This implies that owners of SMEs in Sabasaba ward had poor skills to manage their business as a result they cannot control and manage proceeding from their business. These

results are similar with what World Bank report of 2000 reported that most of SMEs owner in Africa lacks business skills.

Table 3: Possession of business skills

Skills	Frequency	Percent
Record keeping	7	11.7
financial Management	5	8.3
Business control	6	10.0
No business skills	42	70.0
Total	60	100.0

Source: Field data,2012.

(iii) Terms and conditions of acquiring loan in financial institutions

Findings on terms and conditions of acquiring loan from financial Institutions by small business owner includes interest rate, loan procedure and transaction costs, business plan and cash flow, business registration and loan repayment schedule.

(a) Interest rate

Findings show that interest rate charged by financial institution differs from average interest rate of 15% to 20% per annum which is very high for small entrepreneurs to afford for the growth of his or her business (Table 4). Some of the respondents (30%) complained that they can't afford to access loan because of higher interest rates.

(b) Collateral

Collateral is an assurance to the bank in case of default. It ensures borrowers commitment to loan repayments. Findings show that 28.3% of the respondents were required to pledge asset as collateral for loan accessibility which was very difficult to them since they have less assets to offer as collateral (Table 4). This result is similar as suggested by (Berger, 1995) that smaller and younger firms are more likely to face higher cost of financing and they are required to offer collateral while most of firms cannot manage to offer the required collateral.

(c) Loan procedure and transaction costs

Findings on loan procedure and transaction costs revealed that 20% of interviewed respondents have encountered difficulties in accessing credit from commercial banks because of procedure given (Table 4). This signifies that low number of entrepreneurs is running their business with external financing. This result is similar as suggested by (Eshetu, 2000) that less than 20% of households have access to formal financial services.

(d) Business plan and cash flow

The result shows that some of respondents (25%) face hardship in accessing loan because of not having business plan whereby 11.7% is because of not having proper cashflow records of their business (Table 4). This signify that most of SMEs do not have business plan and records of business cash flow. These limits SMEs capacity to survive, access to credit, expand their markets and improve management to raise productivity and income (URT, 2003)

Table 4: Conditions for loan application

Conditions	Frequency	Percent
Interest rate	18	30
Collateral	17	28.3
Loan procedure	12	20
business plan	15	25
Business cash flow	7	11.7

Source: Field data,2012.

(e) Business registration

Findings revealed few number of respondents (46.7%) were registered and more than half (53%) of respondents were not registered (Table 5). This indicate that majority of entrepreneurs do not meet loan conditions in the study area.

Table 5: Business registration

Registration	Frequency	Percent
Registered	28	46.7
Not registered	32	53.3
Total	60	100.0

Source: Field data,2012.

(f) Loan repayment schedule

Business period is another thing considered in loan accessibility. Results indicate that loan repayment schedule for few interviewed respondents (8.3%) range from 1-10 months; (38.3%) were ranging from 1-5 years; (20%) ranging from 6-10years; (13.3%) were ranging from 11-15 years and (11.7%) above 15 years (Table 6).This signify that small bussines owner spent more than a year to repay their loan. However,it is also considered as a burden to low income earner.

Table 6: Loan repayment schedule

Period	Frequency	Percent
1 - 5months	5	8.3
6 - 10months	5	8.3
1 - 5years	23	38.3
6 - 10years	12	20.0
11 - 15years	8	13.3
Above 15years	7	11.7
Total	60	100.0

Source: Field data,2012.

Conclusion and Recommendations

The study aimed at examining factors affecting loan accessibility to small and medium enterprises. Both primary and secondary data were collected and processed using SPSS version 16. It is concluded that most of small business owner are involved in selling of food, charcoal, retail shop, carpentry, hair cutting saloon and stationary services. However, some of small business owners are faced with difficulties in generating enough income which leads to failure to repay given loan. At the same time majority of small business owners do not access loan because

of stringent condition given by Financial Institutions such as bringing fixed collateral, period of business, repayment schedule, business plan and long procedures.

It is recommended that Financial Institutions should regulate borrowing conditions to ensure majority of small business owners are easily accessing and borrow from financial institutions to raise up their capital. .

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