



# THE INFLUENCE OF MICROFINANCE SERVICES ON THE PERFORMANCE OF SMALL AND MEDIUM ENTERPRISE IN TANZANIA. A CASE OF IRINGA MUNICIPAL

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## ABSTRACT

The purpose of the study was to establish the influence of microfinance services on the performance of small and medium enterprises in Tanzania, specifically; to examine the influence of provision of microfinance services on the performance of SMEs; to determine the influence of micro insurance the performance of SMEs and to determine the influence of training on the performance of SMEs. The study employed descriptive design whereby quantitative research approach was used to gather data to answer the research problem and summarize the results. Data was analysed using descriptive statistical analysis. The targeted population was 210 SMEs stakeholders from Iringa municipalities where a sample size of 138 was drawn out of it. Simple random sampling technique was used for the selection of respondents for the sample in the study among participants. From the findings, the following results were obtained; it is important to provide microfinance services on the performance of small and medium enterprises, especially on microfinance services and training, because the change frequency of microfinance services and training has greater effects on performance of SMEs in comparison with micro insurance which have no contributions on influencing performance of SMEs in Iringa Municipality. The study concludes and acknowledges the importance of emphasizing insurance to the business of SMEs in Iringa Municipality was not a priority to microfinance institutions. Thus microfinance institutions have a big challenge on emphasizing the importance of insurance to the business of SMEs in Iringa Municipality. Therefore, the study recommends that microfinance institutions in Iringa Municipality should provide money transfer, deposit and consultancy to SMEs in order to support their business performances. Moreover, MFIs in Iringa Municipality should ensure openness on cost, reliability, stability, awareness and procedures of micro insurance to SMEs business and its importance of protecting the business when the risk is due. Additionally, MFIs in Iringa Municipality should provide chances for financial and business skills to SMEs in appropriateness because it has an impact on the performance of SMEs in Iringa municipality.

## INTRODUCTION

In recent years, both developed and developing countries support for SMEs development and growth has increased. This is because of the contribution of SMEs to the employment creation. Many countries in the world have shown great attention to create an enabling environment for promoting the growth of Small and Medium Enterprises (SME's) to grow their economy and reduce poverty. In November 2010, the OECD held a meeting in France on "Bologna +10" high-level meeting on SMEs and entrepreneurship" to design a roadmap to ensure that SMEs and entrepreneurship make their fullest contribution to the job creation needed now to help governments recover from the crisis and to secure sustainable growth over the longer term.

Small and Medium Enterprises in Pakistan face major problem in accessing finance (Khan & Khalique, 2014). There are several microfinance institutions but still they met a very little portion of the demand for access to finance (Asad, Shariff, & AlEkan, 2016). The demand for initial start-up capital and working capital is very high and the supply is limited (Thio, Megananda, & Maulana, 2016).

Small and medium enterprises (SMEs) have an important role to play in the development of the country. A strong SME sector contributes highly to the economy, contributing to the gross domestic product, by reducing the level of unemployment, reduction in poverty levels and promotion of entrepreneurship activity. In South Africa (SA), the growth of SMEs and prevalence of SMEs is signifi-

cantly low. A study was conducted to identify the internal and external factors affecting the performance of SMEs in KwaZulu-Natal, SA. It was a cross-sectional study conducted among 74 SMEs and results revealed technological advancement would improve the performance of the business (SharmileeSitharam and Muhammad (2016) Factors affecting the performance of small and medium enterprises in KwaZulu-Natal, South Africa).

According to Omondi and Jagongo (2018) Microfinance services significantly influence the financial performance of SMEs in Kisumu County, Kenya. The variables explained 95.1% of the changes in financial performance of the SMEs. A unit increase in access to credit by SMEs led to a 0.855 increase in financial performance of the SMEs, a unit increase in savings mobilization led to a 0.886 increase in financial performance of the enterprises, a unit increase in financial skills training transformed to a 0.965 increase in performance of the firms while a unit increase in role modelling for the SMEs led to a 0.960 increment in their financial performance. The access to credit as a microfinance service existed and was practiced to a greater extent by the MFIs for the SMEs followed by savings mobilizations, and financial skills trainings.

Since Tanzania attained independence in 1961, considerable efforts have been directed towards the nation's industrial development. The initial efforts were government-led through the vehicle of small industry by establishing the small industry development organization (SIDO) in 1973. The objective of SIDO was to develop the small industry sector in Tanzania. It was expected to fulfil a very wide range of functions, from policy formulation to direct support to industries, to hands-on involvement in the establishment of Small and Medium Enterprises (SMEs) in both rural and urban areas. Following the introduction of microfinance institutions in Tanzania is seen as the best alternative source financial service for SMEs as a means to raise their income hence increased contribution to national income. According to Mpanju (2019) there is existence of a strong relationship between the extent of microfinance services and the performance of SMEs and that microfinance services influenced the performance of the SMEs in Tanzania.

Microfinance institutions have been defined as the provider of financial services and loans to the poor in which a sum of money lent out is repaid in small instalments over a certain period of time (Nkuah, Tanyeh and Gaeten, 2013). Small and Medium scaled Enterprises (SMEs) have the potential to fundamentally change all economies across the globe (Ocheni & Gemade, 2015; Quaye, et al., 2014).

Despite the recent development in the microfinance, most SMEs have little access to microfinance services from microfinance institutions (MFIs). In particular, this is a major handicap for their growth and survival. Various studies, including that of Makorere (2014); and Musomandera, Shukla, & Luvanda (2015) exhibit that this affects entrepreneurs' capacity to start or run their businesses profitably.

SME's are said to contribute immensely to the growth of economy of country (Kamugisha, 2016). This prompts countries to invent ways of encouraging the performance and growth of SME's. Data from Tanzania Investment Centre (TIC, 2018) shows that 18% of the SMEs collapse in the third year of establishment, while 20% remains dormant making little profits. Despite the recent development in the microfinance in Iringa Municipality, most SMEs have little access to microfinance services from microfinance institutions (MFIs). SMEs in Tanzania are being excluded from the targeted clientele of both the formal and semi-formal sectors (Ahmed, 1999). However, this is not a unique phenomenon particular to Tanzania. Survey was undertaken in 80 countries by Schiffer and Weder (2001) revealed that financing is the major obstacle for SMEs growth followed by taxes, regulation and inflation. Various factors are considered to be the obstacles for SMEs to be financed which includes lack of collateral, lack of fully registered business, and lack of transaction history. SME ventures in Tanzania depend on personal savings, family or other informal credit sources. A few of the established MFIs (Microfinance Institutions e.g. SACCOS) are scaling up to tap this market. In particular, this is a major handicap for their growth and survival. Failure of SMEs in Tanzania is highly contributed by the lack of capital for expansion and purchasing new technology which is efficient and more productive. Therefore, this raise the need for conducting a research on establishing the influence of microfinance services on the performance of small and medium enterprises in Tanzania, taking Iringa Municipality as a case.

## LITERATURE SURVEY

### The Influence of Provision of Microfinance Services on Performance of SME's

Small and medium enterprises are very essential in both economic and social sector due to their vital role in employment creation. Basing on their sizes, SMEs are controlled and managed by owners who are also the founders of such organizations. In recent years, Small and Medium Enterprises (SMEs) played an important role in employment creation and income generation in Tanzania. SMEs all over the world and in Tanzania in particular, can be easily established since their requirements in terms of capital, technology, management and utilities are not as demanding as establishing a large enterprise. These enterprises can also be established in rural settings and thus add value to the agro-products. SMEs development is associated with more equitable distribution of income and thus important as regards poverty alleviation. At the same time, SMEs serve as a training ground for emerging entrepreneur (SME Policy, 2002).

The term SMEs in Tanzania is used to mean micro, small and medium enterprises. It is sometimes referred to as micro, small and medium enterprises (MSMEs). The SMEs cover 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. The commonly used yardsticks are total number of employees, total investment and sales turnover. In the context of Tanzania, micro enterprises 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 micro enterprises fall under the informal sector. Small enterprises are mostly formalised undertakings engaging between 5 and 49 employees or with capital investment from Tshs.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.

Ahmed (1999) conducted a study on Report on Support the Growth of SMEs in Developing Countries in Morogoro. The study was a case study research design and 138 SMEs were sampled. Data were analysed using descriptive statistics and correlation analysis. The study found out that SMEs in Tanzania are being excluded from the targeted clientele of both the formal and semi-formal sectors. However, this is not a unique phenomenon particular to Tanzania. Survey was undertaken in 80 countries by Schiffer and Weder (2001) on a survey of the Demand for financial Services in Tanzania. A case study research design was employed and 75 SMEs were sampled. Data were analysed using descriptive statistics and regression analysis. The study revealed that financing is the major obstacle for SMEs growth followed by taxes, regulation and inflation. Various factors are considered to be the obstacles for SMEs to be financed which includes lack of collateral, lack of fully registered business, and lack of transaction history. SME ventures in Tanzania depend on personal savings, family or other informal credit sources. A few of the established MFIs (Microfinance Institutions e.g. SACCOS) are scaling up to tap this market. Banks that are actively involved in microfinance services delivery include the Mkombozi commercial bank, National Microfinance Bank (NMB), CRDB bank, Akiba Commercial Bank (ACB) and a few Communities which include Dar es Salaam Community Bank, and Kilimanjaro Cooperative Bank.

Through provision of variety of microfinance services to small and medium enterprises, it has influence their growth and expansion in recent years that led to increase in employment and poverty alleviation.

#### The Influence of Micro Insurance on Performance of SME's

Allen and Overy (2012) conducted a study on competitiveness through increased added value to SMEs in Kenya. A case study research design was employed and 150 SMEs were involved. Data were analysed using correlation analysis. The study found out that micro insurance typically refers to insurance services offered primarily to clients with low income and limited access to mainstream insurance services and other means of effectively coping with risk. More precisely, micro insurance is a means of protecting low-income people against specific risks in exchange for a regular payment of premiums whose amount is proportional to the likelihood and cost of the relevant risk. The principal distinction from traditional insurance is in the targeting of low-income people, which leads to distinct characteristics and objectives, including addressing the particular risks of low-income people, affordability and inclusivity, simplicity and clarity in documentation, accessible processes, and building trust among target clients.

Churchill (2006) studied on the models for business performance: Kareen Wiley and Sons, Ltd, Chichester, England. A descriptive research design was adopted whereby simple random sampling technique was used to select a sample of 170 respondents. Data were analysed using descriptive statistics and regression analysis. The study found out that micro insurance is recognized as a useful tool in economic development. As many low-income people do not have access to adequate risk-management tools, they are vulnerable to fall back into poverty in times of hardship, for example when the breadwinner of the family dies, or when high hospital bills force families to take out loans with high interest rates. Furthermore, micro insurance makes it possible for people to take more risks.

#### The Influence of Training on Performance of SME's

If the MFIs train their credit officers on what kind of investment opportunities are viable for SMEs. The credit officers not only give out credit, but also advise borrowers on profitable projects. Mbithe (2010) conducted a study on the effect of micro finance services on the growth of SMEs in Machakos County, the stochastic model of firm growth was employed, also a quantitative descriptive design was used with a moderate multiple regression analysis was applied to determine the relative importance of each of the three variables; microcredit, micro insurance and training, with respect to the effects of microfinance services on the growth of SMEs, the findings were that microcredit and trainings had a positive effect or contribution to the growth of SMEs.

Temu et al., (2010) conducted a study on the impact of Training on performance of micro and small enterprises served by micro-finance institutions in Tanzania. The researcher used a descriptive survey design, where 50 SMEs were involved. Data were analysed using descriptive and regression analysis. Primary data were collected through questionnaire, while secondary data were collected through documentary review. An independent t-test was used to compare the groups which were the SMEs which received trainings and the SMEs which did not receive trainings from MFIs. The implications from the study was that training in business skills for Tanzania micro and small entrepreneurs is vital for firms performance, growth and improved owners living standards in addition to credit access.

Mwewa et al., (2014) conducted a study on effects of micro-credit, micro-savings and training on the growth of small and medium enterprises in Kenya. The purpose of this study was to find out the effects of micro-credit, micro-savings and training on the growth of SMEs in Machakos County. The stochastic model of firm growth was employed and a survey research design was applied to study types of business categories in Machakos County. Structured questionnaire was used to collect data. Multiple regression analysis was used to determine the relationships between micro-credit, micro-savings, training and growth of SMEs. The results showed that micro-credit, micro-savings and training jointly contribute positively to SMEs growth. However, the effect of training is not statistically significant.

Quaye, et al., (2014) conducted a study to find the effects of MFIs on the growth of SMEs. The study employed a case study design and convenience sampling technique was used in the selection of 100 sample size. Data were analysed using descriptive statistics and inferential statistics. The study revealed that MFIs have a positive effect on the growth of SMEs, the findings of the study also show that MFIs also significance influence to the growth of SMEs through the provision of non-financial service such as Business, Financial and Managerial trainings.

## METHODOLOGY

This was conducted at Iringa Region specifically in the Municipality. The study was descriptive design whereby the researcher employed quantitative research approach to gather data and answer the research problem and summarize the results. The study popu-

lation included SMEs in Iringa Municipality whereby a sample size of 138 observations was taken. Simple random sampling technique was used for the selection of respondents for the sample in the study among participants. Data was analysed using descriptive statistical analysis.

## RESULTS & DISCUSSION

### The Influence of Provision of Microfinance Services on the Performance of SMEs in Iringa Municipality

The study intended to examine the influence of provision of microfinance services on the performance of SMEs in Iringa municipality. To answer this objective of the study, five statements were given to the respondents to rate using Likert scale of agreement. The response to these statements is indicated in the Table 1. Where SD= Strong Disagree, D= Disagree, N= Neutral, A= Agree, SA= Strong Agree.

Table 1: Provision of Microfinance Services and the Performance of SMEs

Statement	SD		D		N		A		SA		Total
	F	%	F	%	F	%	F	%	F	%	F
The use of service facilities from MFIs has slightly improved my business performance	11	8.0	28	20.3	33	23.9	33	23.9	33	23.9	138
Access of credit facilities from MFIs has increased the assets my business possesses					22	15.9	11	8.0	105	76.1	138
Microloans from MFIs are always available whenever the need for loans consultancy arises	11	8.0	11	8.0	33	23.9	61	44.2	22	15.9	138

Table 1 shows that of 138 respondents, 66 (57.8%) of the respondents agreed that the use of service facilities from MFIs has slightly improved their business performance, 39 (28.3%) disagreed with the statement, while 33 (23.9%) were neutral. One hundred and five (76.1%) of respondents agreed that, access of credit facilities from MFIs has increased the assets their business possesses, 22 (15.9%) disagreed with the statement while 11 (8.0%) remained neutral. Eighty three (60.1%) of respondents agreed with the statement that, microloans from MFIs are always available whenever the need for loans consultancy arises, while 33 (23.9%) of the respondents were neutral with the statement, the remaining 22 (16%) disagreed to the statement.

This implies that provision of microfinance services to SMEs enhances their business performance in Iringa municipality. The availability of microfinance services helps to enhance SMEs on financing their business and expanding it, hence increases their business market share. Also the access of credit facilities from MFIs has increased assets on their business possesses especially when they borrow from micro finance institutions to expand their business. Moreover, microloans from MFIs are available whenever the need for loans consultancy arises to SMEs. In addition, they are advising small business holders or entrepreneurs to use microloans to improve their businesses. This will help SMEs to improve business performance of SMEs.

The results are supported by Schiffer and Weder (2001) on their study who revealed that access of credit is the major obstacle for SMEs growth followed by taxes, regulation and inflation. Various factors are considered to be the obstacles for SMEs to be financed which includes lack of collateral, lack of fully registered business, and lack of transaction history. Although, SME ventures depend on personal savings, family or other informal credit sources.

Therefore, performance of SMEs depends on the provision of microfinance services. In Iringa municipality; microfinance institutions should provide a useful microfinance services to SMEs so that to enhance their business performances.

### The Influence of Micro Insurance on the Performance of SMEs in Iringa Municipality

The researcher wanted to determine the influence of micro insurance on the performance of SMEs in Iringa municipality. To answer this objective of the study, five statements were given to the respondents to rate using Likert scale of agreement. The response to these statements is indicated in the Table 2. Where SD= Strong Disagree, D= Disagree, N= Neutral, A= Agree, SA= Strong Agree.

Table 2: Micro Insurance and Money Transfer on the Performance of SMEs

Statement	SD		D		N		A		SA		Total
	F	%	F	%	F	%	F	%	F	%	F
I am aware of having insurance to cover my business	22	15.9	22	15.9	22	15.9	72	52.2			138
The insurance is reliable and it covers all the aspect of my business	22	15.9	61	44.2	22	15.9	33	23.9			138
The cost of insurance is minimum and help me to generate profit to my business	33	23.9	28	20.3	33	23.9	11	8.0	33	23.9	138
Insurance is stable provided by MFIs to SMEs	22	15.9	39	28.3	44	31.9	33	23.9			138
The conditions and procedures of getting microloans insurance are very easy	33	23.9	39	28.3	33	23.9	33	23.9			138

Table 2 shows that of 138 respondents, "I am aware of having insurance to cover my business", 72 (52.2%) of respondents disagreed with this statement while 44 (31.8%) disagreed and 22 (15.9%) were neutral. The second statement was, "The insurance is reliable and it covers all the aspect of my business", 83 (60.1%) of respondents disagreed with this statement while 33 (23.9%)

agreed and 22 (15.9%) were neutral. The third objective was, "The cost of insurance is minimum and help me to generate profit to my business", 61 (44.2%) of respondents disagreed, 44 (31.9%) agreed and 33 (23.9%) were neutral. On the fourth statement; "Insurance is stable provided by MFIs to SMEs", 61 (44.2%) of respondents disagreed with this statement while 44 (31.9%) were neutral with this statement and 33 (23.9%) agreed. The fifth statement was on; "The conditions and procedures of getting microloans insurance are very easy", 72 (52.2%) disagreed, 33 (23.9%) agreed and 33 (23.9%) were neutral.

From the findings, this implies that, large numbers of respondents were disagreed that they are aware of having insurance to cover their business; this means majority of respondents are not aware of the importance of having insurance to cover their business. Moreover, majority of respondents disagreed that the insurance is reliable and it covers all the aspect of the business, so lack of awareness of the importance of insurance has been an obstacle to the majority of SMEs on their business performance. In addition, majority of respondents disagreed that insurance is not stable provided by MFIs to SMEs whereas the conditions and procedures of getting microloans insurance are not very easy.

This is inconsistent with the study conducted by Allen & Overy, (2012) in their study who found that micro insurance is a means of protecting low-income people against specific risks in exchange for a regular payment of premiums whose amount is proportional to the likelihood and cost of the relevant risk. The principal distinction from traditional insurance is in the targeting of low-income people, which leads to distinct characteristics and objectives, including addressing the particular risks of low-income people, affordability and inclusivity, simplicity and clarity in documentation, accessible processes, and building trust among target clients.

Generally, the researcher observed that majority of the respondents was not aware on the importance of insurance in relation to their business performance. Additionally, cost of insurance and its procedures were not taken into consideration as the influencing variables of microfinance services on SMEs performances. Furthermore the researcher observed that emphasizing the importance of insurance to the business of SMEs in Iringa Municipality was not a priority to microfinance institutions.

#### The Influence of Training on the Performance of SMEs in Iringa Municipality

The researcher wanted to determine the influence of training on the performance of SMEs in Iringa Municipality. To answer this objective of the study, five statements were given to the respondents to rate using Likert scale of agreement. The response to these statements is indicated in Table 3. Where SD= Strong Disagree, D= Disagree, N= Neutral, A= Agree, SA= Strong Agree.

Table 3: Staff Development and Performance of SME's

Statement	SD		D		N		A		SA		Total
	F	%	F	%	F	%	F	%	F	%	F
Trainings provided by MFIs is appropriate to my business	19	13.8	11	8.0	11	8.0	49	35.4	48	34.8	138
There is great impact on my business through the MFIs trainings	19	13.8	11	8.0	11	8.0	54	39.0	43	31.8	138

Table 3 shows that of 138 respondents, 97 (70.2%) of the respondents agreed that trainings provided by MFIs is appropriate to their business, 30 (21.8%) of respondents disagreed, and 11 (8%) of respondent were remaining neutral to the statement. In the second statement the 97 (70.2%) of respondents agreed to the statement that there is great impact on their business through the MFIs trainings, 30 (21.8%) disagreed and 11 (8%) were neutral.

This implies that microfinance institutions provides training programs to SMEs in Iringa Municipality, that is why the majority of respondents agreed that training and development on business skills has an impact on their business performances. Majority of respondents agreed that trainings provided by MFIs is appropriate to their business because there is great impact on their business through the MFIs trainings. This helps most of SMEs in expanding their business hence improving their business performances in Iringa municipality.

The results are supported by Temu et al., (2010) conducted a study on the impact of training and development on performance of micro and small enterprises served by microfinance institutions in Tanzania an independent t-test was used to compare the groups which were the SMEs which received trainings and the SMEs which did not receive trainings from MFIs implications from the study was that training in business skills for Tanzania micro and small entrepreneurs is vital for firms performance, growth and improved owners living standards in addition to credit access.

Therefore, performances of SMEs might be increased because of training and development given to SMEs from microfinance institutions in Iringa Municipality. Thus microfinance institutions should provide financial trainings to SMEs in Iringa municipality in order to influence SMEs business performances.

## CONCLUSION

The study acknowledges the importance of microfinance services on the performance of small and medium enterprises in Iringa municipality, as it requires SMEs to seek microfinance services from micro finance institutions in order to increase their business performance. Microfinance services and training has a high and positive significant relationship on the performance of small and medium enterprises in Iringa municipality. Financial institutions are required to offer financial services to SMEs in order improve and expand their business through access to loan and financial skills. Moreover, emphasizing the importance of insurance to the business of SMEs in Iringa Municipality was not a priority to microfinance institutions. Thus microfinance institutions have a big challenge on emphasizing the importance of insurance to the business of SMEs in Iringa Municipality.

## RECOMMENDATIONS

### Recommendations for Action

The findings indicate that microfinance services influences the performance of SMEs in Iringa municipality; therefore, microfinance institutions in Iringa Municipality should provide saving facilities, credit facilities and consultancy to SMEs in order to support their business performances.

Moreover, the findings indicate that micro insurance has no influence of the performance of SMEs in Iringa municipality; therefore, the researcher recommends that microfinance institutions in Iringa municipality should ensure openness on cost, reliability, stability, awareness and procedures of micro insurance to SMEs business and its importance of protecting the business when the risk is due.

Furthermore, the findings indicate that training influences the performance of SMEs in Iringa municipality; therefore, the researcher recommends that microfinance institutions in Iringa Municipal should provide chances for financial and business skills to SMEs in appropriateness because it has an impact on the performance of SMEs in Iringa municipality.

### Recommendations for Further Studies

Qualitative study studies should be done to examine the influence of micro insurance on the performance of SMEs.

Further studies should be conducted to examine to why micro insurance is not an influence variable on improving the performance of SMEs, and what are the other influencing factors of microfinance services on the performance of small and medium enterprises in Tanzania.

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