Asian Development Policy Review
ISSN(e): 2313-8343
ISSN(p): 2518-2544
DOI: 10.18488/journal.107/2016.4.2/107.2.51.64
Vol. 4, No. 2, 51-64

URL: www.aessweb.com

THE INTERACTIONS BETWEEN MICROFINANCE INSTITUTIONS AND SMALL AND MEDIUM SCALE ENTERPRISES IN THE SUNYANI MUNICIPALITY OF GHANA

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Article History
Received: 21 July 2016
Revised: 22 August 2016
Accepted: 19 September 2016
Published: 24 October 2016

Keywords
Development
Ghana
Growth
Loans
Micro-credit
Micro-finance
Microfinance Institutions
Savings
SMEs.

JEL Classification:

ABSTRACT

Small and Medium Scale Enterprises play a significant role in the global economy and hence, considered as the backbone of the private sector. SMEs play a vital role in economic, social and cultural development. Studies indicate that microfinance services and products over time have positive effects on SMEs. Conversely, other scholars have highlighted that microfinance has impacted negatively on SMEs, especially, those owned or operated by women. Thus, the study sought to establish the effects of microfinance on SMEs. The study adopted a case study approach. It examined the effects of microfinance services and products provided by Multi Credit Savings and Loans Limited on the performance of SMEs in the Sunyani Municipality of Ghana and also examined the problems encountered by both in dealing with each other. In all, questionnaires were administered to 152 customers of MCSL who were owners of SMEs. The study found that the main challenges faced by SMEs include short duration of loans repayment, high interest rates and request for collateral among others. Also, the study established that the effect of microfinance institutions on SMEs was positive. Revenue, profit and assets base of SMEs increased over time when they patronised the services of microfinance institutions. The study, therefore, recommended that microfinance institutions should make their products more SME friendly, institute more business advisory services, and ensure the proper application of loans contracted from them through effective monitoring systems. SMEs on the other hand, are to diligently keep record books for self-assessment and hire competent staff to improve their management capacities.

1. BACKGROUND OF THE STUDY

Small and Medium Scale Enterprises (SMEs) play a significant role in the global economy. It is considered as the backbone of the private sector. Apart from economic development, SMEs play vital roles in social, political and cultural development (Dixit and Pandey, 2011). In this regard, SMEs play a pivotal role in promoting grassroot economic growth and equitable sustainable development. Kachembere (2011) argues that SMEs' development is acknowledged as a key factor in promoting equitable and sustainable economic development. The SME sector has the potential to promote growth in employment as well as contribute to poverty reduction among urban and rural areas in most developing countries (Tombo *et al.*, 2008). Similar studies buttress this point that SMEs contribute immensely to job opportunities in Africa (Ayyagari *et al.*, 2007). SMEs contribute immensely to Gross Domestic

Product (GDP), economic growth, employment creation and increase government revenue through the payment of indirect taxes such as Value Added Tax (Dalberg Global Development Advisors, 2011).

Examining the contributions of SMEs to the economy, it becomes obvious that SMEs are tools for promoting equitable and sustainable economic development (Kachembere, 2011). However this can only be realised when Microfinance Institutions (MFIs) carry out their activities to meet the purpose for which they were established. Thus, the main purpose of MFIs is not just to offer credit to the productive poor but to provide non-financial services such as insurance, savings and money transfers which commercial banks are reluctant to provide because owners of SMEs are mostly unable to meet their collateral requirements. Studies indicate that microfinance services and products over time have positive effects on SMEs (Afrane, 2002; Roodman and Morduch, 2009; Idowu, 2010; Karikari, 2011). Conversely, other scholars have highlighted that microfinance has impacted negatively on SMEs especially women (Mayoux, 2005; Chowdhury, 2009; Duvendack *et al.*, 2011).

This shows why governments, particularly in Africa, have made tremendous efforts and instituted policies to enhance the growth of SMEs. For instance, the Nigerian government prohibits the importation of fully manufactured products from China and this policy has forced SMEs and other companies established in Nigeria to contribute to job creation and technology transfer (Consultancy Africa Intelligence, 2011). Similarly, the Moroccan government has totally exempted owners of SMEs set up in free zones from paying corporate taxes and income tax for the first five years of operation and applies a minimal corporate tax for the next ten years. In addition, Morocco has two state owned banks that offer micro loans and industrial modernisation programmes to SMEs (United Nation Economic Commission for Africa, 2008).

In Ghana, the private sector dominated with SMEs is considered as the engine of growth of the Ghanaian economy (Republic of Ghana, 2006). The SMEs in Ghana can be categorized into urban and rural enterprises. Kayanula and Quartey (2000) categorise the major activities within the Ghanaian SMEs sector as making soaps and detergents, weaving fabrics, designing clothing and tailoring, producing textiles and leather, village blacksmithing, firing ceramics, timber felling and mining, making bricks and cement, brewing beverages, food processing and baking, creating wooden furniture, assembling electronic products and mechanical activities.

The Ghana Statistical Service (GSS) estimates that SMEs make up 70 percent of all industrial establishments that contribute about 70 percent of Gross Domestic Product (GDP) as well as absorb more than 60 percent of the labour force and account for about 92 percent of businesses in Ghana (Ghana Statistical Service, 2012). This makes SMEs a very important sector of the economy. Government, realising the socio economic importance of SMEs, established the National Board for Small Scale Industries (NBSSI) by an Act of Parliament (Act 434) to promote the activities of SMEs aimed at reducing unemployment rate and to boost economic growth. As part of the government's vision to promote SMEs, it established the Microfinance and Small Scale Loan Centre (MASLOC) in 2004 to assist SMEs in income generating ventures and to reduce poverty (Abaane, 2008).

With regards to the foregoing debate, this study sought to examine the effects of microfinance products and services on SMEs over time in the Sunyani Municipality of Ghana, taking clients of Multi Credit Savings and Loans Limited (MCSL) as case study. The main objective of this study is to assess the ways in which microfinance services and products over time affect the activities of SMEs with focus on the Sunyani Municipality of Ghana. The key question driving the study is how microfinance services and products provided by MCSL affect the performance of SMEs in the Sunyani Municipality? In answering the question above, the study unpacked the interactions between MFIs and SMEs, especially, on how MFIs enhance the access to credits and productive services by SMEs for sustainable growth. The study concludes by identifying the challenges confronting such interactions and offers remedies to reduce these challenges.

2. SMALL AND MEDIUM-SCALE ENTERPRISES AND MICROFINANCE IN THE DEVELOPING WORLD

Microfinance is a concept in development and business literature dating to the 1970s. The concept, however, caught on early as Robinson (2001) states that the 1980s represented a turning point in the history of microfinance in that Microfinance Institutions (MFIs) such as Grameen Bank began to show that they could provide small loans and savings services profitably on a large scale. It was now clear for the first time that microcredit could provide large-scale outreach profitably. During the 1980s, MFIs received no continuing subsidies, were commercially funded and fully sustainable, and could attain wide outreach to clients (Robinson, 2001). It was also at this time that the term "microcredit" came to prominence in development studies. According to a World Bank (2012) report, an estimated 22 percent of the population of the developing countries live below $1.25 a day. Most people in the developing world barely have enough to spend and save towards the creation and sustainability of a business venture. This makes it difficult for many individuals with entrepreneurial skills to fund and grow their businesses no matter how small. Microfinance has been identified as a desirable measure to support such individuals and their initiatives (Duvendack, 2011).

Conversely, the notion of SME and entrepreneurship development was introduced into the growth and development landscape as early as the late 1940's with the introduction of targeted policies such as grants, subsidised credits, special tax treatment, and the establishment of small business or SME support agencies by governments (Organisation for Economic Cooperation and Development, 2004). Researchers in different disciplines have varied conceptions of what may be described as Small and Medium Scale enterprise (Elaian, 1996; Mensah, 2004). Storey (1994) argues that the definition of SMEs varies because the classification of firms by size varies. Again, while some use capital assets for the classification of SMEs, others use skill of labour and turnover level. In the developing world, according to Elaian (1996) SMEs are classified as:

- Large - firms with 100 or more workers;
- Medium - firms with 20-99 workers;
- Small - firms with 5-19 workers;
- Micro - firms with less than 5 workers.

Quaye (2011) opines that Small and Medium Enterprises (SMEs) have similarities that aid their classification. They usually have limited access to deposits, credit facilities and other financial support services made available by Formal Financial Institutions (FFIs). This is because SMEs cannot provide the necessary collateral security requested by formal institutions and usually the banks have challenges recovering the high cost involved in dealing with small firms. In Ghana, available data from the Registrar General's Department indicates that 90 percent of companies registered are micro, small and medium enterprises (Mensah, 2004). This target group has been identified as the catalyst for the economic growth of the country as it is a major source of income to the government and creates employment. It is estimated that the Ghanaian private sector consists of approximately 80 000 registered limited companies and 220 000 registered partnerships.

Small and Medium Scale Enterprises (SMEs) have a long history of development efforts. Throughout the 1980s and up to the late 1990s, they were perceived as a synthetic construction mainly of "social and political" importance. Although domestic SMEs and the informal sector constituted most of what could be and what are still deemed as 'private business activity', in most developing countries, private sector development strategies advocated for and implemented in these countries were directed towards the needs of large-scale businesses, including foreign invested ones. This type of policy advice was subtly informed and motivated by the rather disappointing outcome from the extensive SME support systems operated in developed countries since the 1970s (OECD, 2004). Given that most SMEs are one-person businesses; the largest employment category is working proprietors. This group, Abor and Quartey (2010) argue, makes up more than half of the small and medium enterprises workforce in most developing countries; their families, who tend to be unpaid but active in the enterprise, make up roughly another quarter. The remaining portion of the workforce is split between hired workers and trainees or apprentices. Another perspective (Abor and Biekpe, 2006) to SMEs in Ghana is that majority of the SMEs owned by females are home based enterprises compared to SMEs owned by men.

MSMEs in Ghana can be categorised into urban and rural enterprises (Abor and Quartey, 2010). Urban enterprises can be further divided into organised and unorganized. Organized SMEs have mostly paid employees with a registered office, whereas the non-organised are made up of artisans who work in the open spaces, temporary wooden sheds or at home. Their workers are few and in some cases, no salaries are paid. Apprentices and family members make up their main staff (Kayanula and Quartey, 2000). Rural enterprises are largely made up of family groups, individual artisans and women engaged in food production from local crops. The major activities within this sector include soap and detergents, fabrics, clothing and tailoring, textile and leather, village blacksmiths, tin smiting, ceramics, timber and mining, bricks and cement, beverages, food processing, bakeries, wood furniture, electronic assembly, agro processing, chemical-based products and mechanics (Abor and Quartey, 2010).

SMEs have the potential to grow into large corporations when the right conditions are put in place. Ghana, like other developing cronies, has a plethora of policies and strategies that relate to the private sector (Addaney *et al.*, 2016). These strategies are crafted and presented in the forms of private sector development, trade and investment policies among others. The responsibility for implementing these various national policies/strategies and programmes are carried through the public sector institutions, (Ministry of Finance) where both capacities and authority to coordinate are weak. This was the case during the Economic Recovery Programme (ERP) of the 1980s in Ghana (Mensah, 2004).

This notwithstanding, government of Ghana has in the past, either alone or with the support of donor agencies, tried to implement a number of direct lending schemes to SMEs. These are referred to as official SME credit schemes. Managed in most cases by the Ministry of Finance, these facilities were often obtained under the ERP and the Structural Adjustment Programme (SAP). According to Mensah (2004) the results of the direct lending schemes operated by government have been mixed. For instance, under the Austrian Import Programme of 1990, 20 companies of varying sizes benefited from the scheme. Beneficiaries were given six (6) years made up of a one-year moratorium and a five-year repayment period. Since the loans were disbursed in 1990, the borrowers should have completely liquidated their loans by the end of 1996. However as at December 2001, only 1 out of 20 beneficiaries had fully paid. Other direct interventions such as the Business Assistance Fund (BUSAC), Ghana Investment Fund and the Export Development and Investment Fund (EDIF) have also been tried out but with mixed results. Regarding funding from financial sources such as banks, SMEs have become attractive clientele as banks and other financial institutions seek to broaden their loan portfolio (Addaney *et al.*, 2016). Suffice to say, these institutions lend to SMEs with a heavy heart due to their undisputed high default rates (Ahinful, 2012).

Akorsu and Agyapong (2012) aver that only few SMEs are financed from commercial bank loans, government assistant programmes or other informal sources. The main methods to access funds for SMEs are basically through debt or equity sources or both. Equity usually may be by the business owner relying on personal savings from previous work, gift from friends or family members or even remittance from abroad. However, SMEs are beginning to receive a lot of financial support from microfinance institutions than from other formal financial institutions (Duvendack *et al.*, 2011). It can be inferred from literature that financing remains a major challenge for SMEs. In the light of this, there have been a number of state interventions and assistance from other well-meaning international organisations to financially support the growth of SMEs. The results of these interventions have however been mixed and the cause of this can be traced to administrative lapses, poor implementation and other inefficient financial management practices on the part of SME owners. These notwithstanding, microfinance institutions represent the new hope for SME financing in the developing world especially in Ghana.

Microfinance encompasses the provision of financial services and the management of small amounts of money through a range of products and a system of intermediary functions that are targeted at low income clients.

Microcredit is thus one of the critical dimensions of the broad range of financial tools for the poor, and its increasing role in development and business cannot be underestimated (Morduch, 2000). Through microfinance, financial services are made available to relatively poor households and microenterprises in small transactions suited to their conditions. Micro-finance companies present a decent opportunity of aiding the poor in society out of poverty and supporting micro-enterprises to grow. In the light of this, the number of microfinance organisations in the country is on the surge. These organisations have sprung up in many parts of the country with products mostly aimed at making finance available to individuals and small scale businesses (Dzisi and Obeng, 2013). The Microfinance concept as it is practiced now had a lot of support from the international community and other donors following the success story of the Grameen exercise by Professor Muhammed Yunus. In addition to a business model explanation, Jain and Moore (2003) give a political economy explanation for the success of the microfinance movement. According to them, microfinance campaigners successfully projected the image of the movement, such as empowerment of women, which resonates well with the donor community.

Another reason for the early success of microfinance has been attributed to the birth of the movement which roughly coincided with the rise of neo-liberal ideas in the United States of America and the United Kingdom, and within the Bretton Woods Institutions in the late 1970s and early 1980s. Thus, the notion that microfinance programmes are primarily engaged in the promotion of small scale enterprises appealed to major donors. While donors had concerns about subsidised credit through state-owned specialised financial institutions, they were quite pleased to subsidise microfinance institutions as they appeared to promote a market economy, and more importantly, they helped to diminish the role of the government (Jain and Moore, 2003). To date, Quaye (2011) and Boss and Milestone (2012) still trace the development of microfinance to the success of the Grameen Bank in Bangladesh. The Grameen Bank (GB) reversed conventional banking practice by removing the need for collateral and created a banking system based on mutual trust, accountability, participation and creativity. It has been argued that if financial resources can be made available to the poor people on terms and conditions that are appropriate and reasonable, these millions of people with their small pursuits can add up to create the biggest development wonder (Morduch, 2000).

In Ghana, though SMEs play an important role in the development of the economy, their level of development is often hampered by the limited access to finance (Abor and Biekpe, 2006). This lack of access is often associated with financial policies and bank practices that make it difficult for banks to cover the high costs and risks involved in lending to small firms (Addaney *et al.*, 2016). SMEs depending on their developmental stage require particular kinds of credit. For small traditional micro businesses, personal savings equity in residential property and soft loans are good sources of credit. High potential, possibly, export businesses require a different kind of finance; angel finance, venture capital or asset backed finance from banks (National Credit Regulator, 2011). SME's lack of finance is a common phenomenon in developing countries (Anane *et al.*, 2013). The cause of this is traceable to the relatively underdeveloped financial sector in most of these countries with low levels of intermediation, lack of institutional and legal structures that facilitate the management of SME lending risk and also the high cost of borrowing and rigidities of interest rates.

However, owing to the persistent financing gap, many interventions have been launched by governments and development partners to improve the flow of financing to SMEs to offer more options and financing alternatives to what is available from existing private sector financial institutions. The many interventions that have been instituted in the past as well as the currently existing ones can be harmonised under two categories; official credit schemes and financing provided by financial institutions (Mensah, 2004). Access to finance from banks is a major difficulty for most SMEs in Ghana. The access to affordable credit over a reasonable period is the main financial difficulty SMEs face. Adomako-Ansah (2012) however opines that this is because of the financing needs of SMEs and the action of banks. SME financing schemes have to reflect their operational requirements. Meanwhile, this is usually not the case because the actions of banks depend on their risk perception about the SME which is often influenced by several factors ranging from the bank's ability to raise funds to the characteristics of the SME or the features of the entrepreneur (Adomako-Ansah, 2012).

Mensah (2004) contends that the interventions for SMEs to access credit have not been altogether very effective. The ineffectiveness of these interventions and SMEs difficulty in accessing credit can be explained in two fold; from the supply and demand sides. From the supply side, financial institutions are still skeptical about lending money to SMEs. This is because of the moral hazard that the financial institutions have to bear. In the absence of opportunities for monitoring borrower actions and for verifying the information provided by borrowers, there might be situations where lending institutions either withdraw from the market or impose borrowing conditions which are difficult for most borrowers to comply. This partly accounts for the high interest rates that some financial institutions heap on loans for SMEs (Quaye, 2011). From the demand side, SMEs also do not observe sound financial management practices. The majority of SMEs do not prepare business plans and cash flow statements at all. The few that do only prepare business plans when applying for bank loans (Ahinful, 2012). The book keeping practice of most SMEs is also poor and discourages banks and other financial institutions from lending to them due to the high risk of default.

In addition, some SMEs who have received credit facilities tend to default as a result of poor financial management practices, inadequate monitoring and diverting of loans to unproductive areas (Quaye, 2011). In the same vein, some financial institutions also institute cumbersome loan application procedures including the request for collaterals which often pose challenges to SME financing (Asiama and Osei, 2007). The challenges of SMEs in accessing credit are enormous and multidimensional. These challenges, whether from the demand side (SMEs side) or the supply side, (credit provider) limit the amount of credit that is available to SME owners for the sustainable growth and development of their business.

3. STUDY SETTING AND METHODOLOGY

The study was conducted in the Sunyani Municipality in the Brong Ahafo region of Ghana. And the population for the study was made up of all the SMEs that have benefited from the credit facilities of MCSL and are registered with the Sunyani Branch. In order to select the unit of analysis, multi-stage sampling technique was adopted. Firstly, purposive sampling was used to get the credit officers of the case study organisation while simple random sampling was used to select 152 respondents to constitute a sample size for the study. The research involved a combination of quantitative and qualitative research approaches with the simple random sampling technique used. This is a type of sampling technique in which the units to be observed are selected not on any specific basis (Babbie, 2007; Yates *et al.*, 2008). Questionnaires and interviews were used as the means of gathering primary data. Secondary data, that is data that have been collected for another purpose and exist elsewhere (Saunders *et al.*, 2009) were also analysed. Descriptive statistics was used in analysing the data.

4. RESULTS AND DISCUSSIONS

This section deals with the analysis and interpretation of the responses from the interviews and offers detailed information and explanation of the textual data collected and the results obtained from the field.

4.1. Educational Background of Respondents

Regarding the highest education of the respondents, it was revealed that 48 (32%) had Higher National Diploma (HND), 25 (17%) had WASSCE/ GSE, 31(20%) had BECE/ MSLC, 37 (24%) had bachelor's degree while 11 (7%) had some other qualifications. There has been the perception that most SME owners are illiterate, that is, they have little or no formal education but the study revealed that majority of SME owners in the Sunyani Municipality had some considerable level of education. The results are shown in Table 4.1.

Table-4.1. Educational background of Respondents

Educational status/Variable	Frequency	Percentage (%)
JHS/MSLC	31	20
SHS/GCE	25	17
HND	48	32
Degree	37	24
Others	11	7
Total	152	100

Source: Field Survey, 2015

4.2. Profile of Small and Medium Scale Enterprises

Regarding the registration of business by respondents, the study revealed that 99 (65%) of respondents had not registered their business while 53 (35%) had registered. All the respondents who had not registered attributed it to *inter alia* their ignorance of the registration process and high registration fees. This reveals that most SMEs in the Sunyani Municipality are not registered.

In terms of the nature of SMEs, the study discovered that 75 (49%) were into trading, 26 (17%) were into services provision whilst 30 (20%) and 21 (14%) were into manufacturing and agriculture respectively. This revealed that SME who were into trading dominated, followed by service provision, especially, hair dressing and tailoring. The outcome confirms that of the World Bank (2008) that owners of SMEs are mostly self-employed, household vendors who are into small retail shops, street selling, small manufacturing and service provision who are neglected by the traditional banks in developing countries.

With respect to years in operation, the study revealed that 67 (44%) of SME had been operating between 6 to 10 years, 41 (27%) had operated for less than 5 years, 20 (13%) had been in business for 16 to 20 years whilst 15 and 9 representing 10% and 6% had operated for 11 to 15 years and above 21 years respectively. This indicates that the entire respondents had some level of experience in the management of SMEs.

4.3. SME Oriented Micro-Credit Services Provided by Multi Credit Savings Loans Limited

Products and services offered by microfinance institutions according to Ledgerwood (1999) are generally classified under the four broad categories: financial intermediation, social intermediation, enterprise or business development, and the social services. However, this study was limited to the financial intermediation and business development services since it applied directly to services offered by MCSL to their SME clients. The study revealed that 73 (48%) of SME owners who dealt with MCSL have accessed loan facilities, 25 and 12 representing 16% and 8% accessed savings and deposit services respectively. Regarding the extent of services offered by Multi Credit Savings and Loans Limited, 146 (96%) of the respondents stated that MCSL offered loan advice while 6 (4%) contended that MCSL does not offer loan advice at all. On whether MCSL offered SME advisory services to SME owners, majority (92%) of the respondents indicated that MCSL offered SME advisory services while 8% stated that MCSL did not offer any SME advisory services at all. Regarding loan insurance services offered, 97 (64%) of the respondents indicated that MSCL does not offer loan insurance services while 55 (36%) indicated that MCSL offered loan insurance services.

Majority (93%) of the respondents opined that MCSL offered financial advice. Minority (7%) of the respondents indicated that MCSL does not offer financial advisory services at all. On short term loans offered by MCSL, majority (90%) of respondents stated MCSL offered short term loans while 10% stated that MCSL does not offer the service. This indicates that the microfinance studied basically provides financial intermediation, which involves the provision of financial assistance to small business groups in a form of credit which assists SMEs to invest in their existing business or set up a new business venture. In addition, MCSL provides enterprise development services which are non-financial services that provide knowledge and information services to SME entrepreneurs to assist them raise human capacity and organization capabilities. They include skills development, basic business training, book keeping, marketing and technology services and subsector analysis.

These responses corroborate Ledgerwood (1999) observation that products or services are clearly targeted but microfinance providers may choose to provide a combination of these services. However, as it is, many microfinance institutions are more comfortable providing the financial intermediation without necessarily considering the welfare of the fund recipients or equipping them with enterprise skills. This is a major shortfall in the provision of piece-meal microfinance because financial intermediation without the requisite skills might lead to financial mismanagement and its attendant problems which may further worsen the plight of some of these SMEs. Non - traditional products and services offered by MCSL are presented in Table 4.3.

Table-4.3. Non-Traditional Products and Services offered by MCSL

Variable/Responses	Yes		No (Not at all)	
	Frequency	Percentage	Frequency	Percentage
Loan Advice	146	96	6	4
SME Advice	140	92	12	8
Loan Insurance	55	36	97	64
Financial Advice	142	93	10	7
Short Term Loans	137	90	15	10
Business Insurance	137	90	15	10
Pension Scheme	58	38	94	62
Interest of savings	128	74	40	26

Source: Field Survey, 2015

Regarding the quality of service, majority (63%) of the respondents graded it as excellent, 25% said that the services were very good and 12% said the services were good. Based on this, majority of the respondents perceived the services as excellent. This confirms the assertion of Lewis and Mitchell (1990) that quality of service is the extent to which a service meets customer's needs and expectations. The MFI under study met the expectations of its customers and in some cases exceeded them.

4.4. The goal of SME and Microfinance institutions interactions

As in many human institutions both customers and service providers have various reasons why they deal with each other and it is based on these that customers switch or remain loyal to service providers. According to Binks *et al.* (1996) the perception of SMEs and their banks was virtually identical across banks. His conclusion was that the bank/ SME relationship was insufficiently close to enable anything other than a capital gearing based loan decision rather than any form of prospects based on income gearing approach. Though MFIs were supposed to fill the gap between banks and SMEs and provide solutions that suit the conditions within which SMEs operate, the volatility of SMEs does not provide enough security for the provision of some services by MFIs especially the provision of credit facilities. SMEs are required by the MFIs to meet some criteria to be able to access credit from them. Therefore, the study attempted to identify the reasons why SMEs patronise the services of microfinance institutions and it was found that 137 (90%) of the respondents work with MCSL because they can secure loans, 72 (47%) stated they deal with the institution because they are able to save to improve their businesses while 53 (35%) stated that they obtain business advice but 16 (11%) stated that they are able to save for personal projects.

Regarding the requirements that qualify SMEs for micro financing services, the study found that for 90 (59 %) of SMEs, the major requirement that qualifies one to access some services at MCSL is ones' savings, 20 (13%) indicated that guarantors were required before they could access some services especially credit. Also, 18 (12%) stated that they collateralised their land as a requirement, 15 (10%) indicated their business assets and finally 9 (6%) stated that they collateralised their cars as a requirement. The staff of MCSL stated that they require the business registration documents and business address of SME when they request to access credit from them. They also assess their movable and non-movable assets of the applying SME owner. This, the loan officers stated, is to provide security against the high rate of default among SMEs.

The above corroborate Kaufmann *et al.* (2005) argument that formal finance is poor because of the high risk of default among SMEs. This, they indicated, required securities to ensure that banks or MFIs do not accumulate bad debt. The outcome of the results further confirms the observation of Asiama and Osei (2007) that financial institutions including MFIs adopt cumbersome loan application procedures including the request for collateral which often pose challenge to SME financing.

4.5. Challenges Encountered by Both MFIs and SMEs in Dealing with Each Other

Challenges faced by the MFI and SMEs in dealing with each other generally entail the major factors that prevent smooth transactions. These major challenges include short durations of loan repayment, high interest rates, demand for collateral securities, no knowledge on interest rate, mode of payment and denial of auxiliary services among others. Table 4.5 illustrates some of challenges.

Table-4.5. Challenges faced by SMEs in dealing with MFIs

Challenges	High		Normal		Low	
	Frequency	Percentage	Frequency	Percentage	Frequency	Percentage
Short duration of loan repayment	115	76	27	18	10	6
High Interest Rate	124	82	20	13	8	5
Collateral	128	84	15	10	9	6
Ignorance Interest Rate	22	14	59	39	71	47
Mode of Payment	12	74	31	20	9	6
Denial of Auxiliary	29	19	21	14	102	67

Source: Field Survey, 2015

The challenges indicated above affect SMEs in various ways. The respondents largely agreed that the general effects of the challenges were that the high interest rate increases the cost of the debt. They also indicated that, pressure due to the short duration of loans affect the performance of their businesses. The daily repayment leads them to borrow money to repay loans, which leads to an increase of debts. The lack of knowledge of interest rates on loans makes it difficult for SME owners to plan with the loan and the inability to provide collateral means getting less than the amount demanded. The outcome of the results confirms the assertions of Mensah (2004) that the major problems facing SMEs is the lack of access to credit. As indicated in Table 4.14, the major challenges SMEs faced when assessing finance from MFIs included short duration of loan repayment, high interest rate and demand for collateral security from SMEs.

Mensah (2004) argues that the challenges faced by SMEs are traceable to the relatively underdeveloped financial sector in most of these countries with low levels of intermediation, lack of institutional and legal structures that facilitate the management of SME lending risk and also the high cost of borrowing and rigidities of interest rates. Mensah (2004) however asserts that SMEs access to finances cannot be solely solved with micro finances, owing to the persistent financing gap; many interventions have been launched by governments and development partners to improve the flow of financing to SMEs to offer more options and financing alternatives to what is available from existing private sector financial institutions. The many interventions that have been instituted in the past and the existing ones can be harmonized under two categories; official credit schemes and financing provided by financial institutions.

In terms of the effects of products and services on revenue, profits, asset base and business expansion, 65% of the respondents indicated that their revenue were low, 20 (13 %) stated their revenue were normal while 30 (20%) stated their revenue were uncertain and 3 (2%) stated that their revenue were high but after accessing the products of MCSL over time, 120 (79%) stated their revenue were now high, 28 (18%) indicated their revenue were normal, 1(1%) stated their revenue were still low while 3 (2%) stated that their revenue were still uncertain as presented in Figure 1.

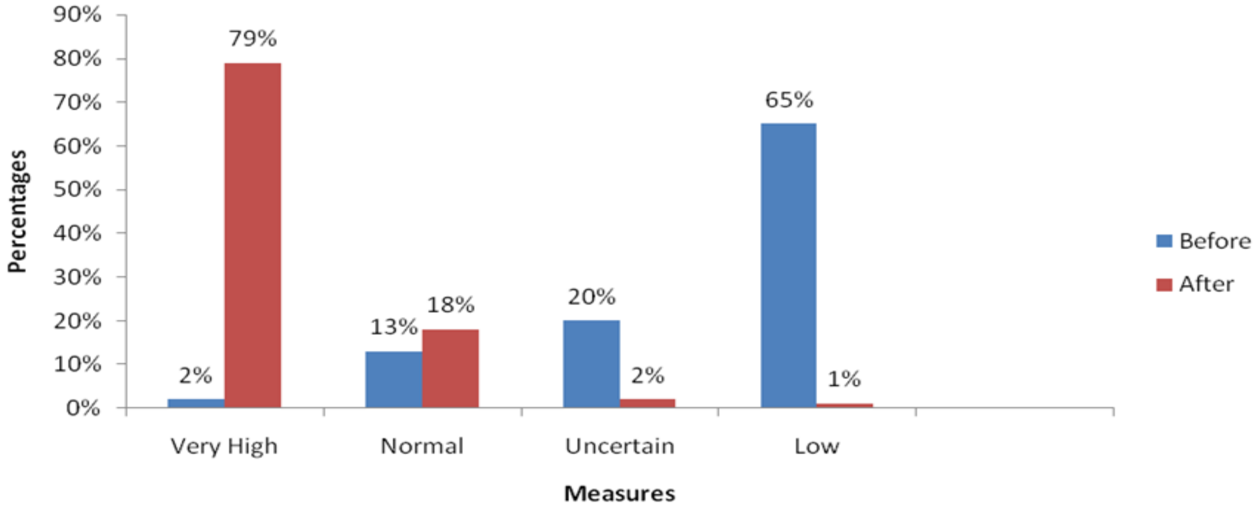

Figure-1. Revenues before and after accessing Microfinance products and services

Source: Field Survey, 2015

Respondents indicated that before they became customers of MCSL, 87 (57%) recorded low profits, 35 (23%) were uncertain, 25 (17%) recorded normal profits and 5 (3%) recorded very high profits. After becoming customers of MCSL over a period of time, 111 (73%) recorded very high profits, 29 (19%) normal profits, 10 (7%) were uncertain while 2 (1%) recorded low profits as presented in Figure 2.

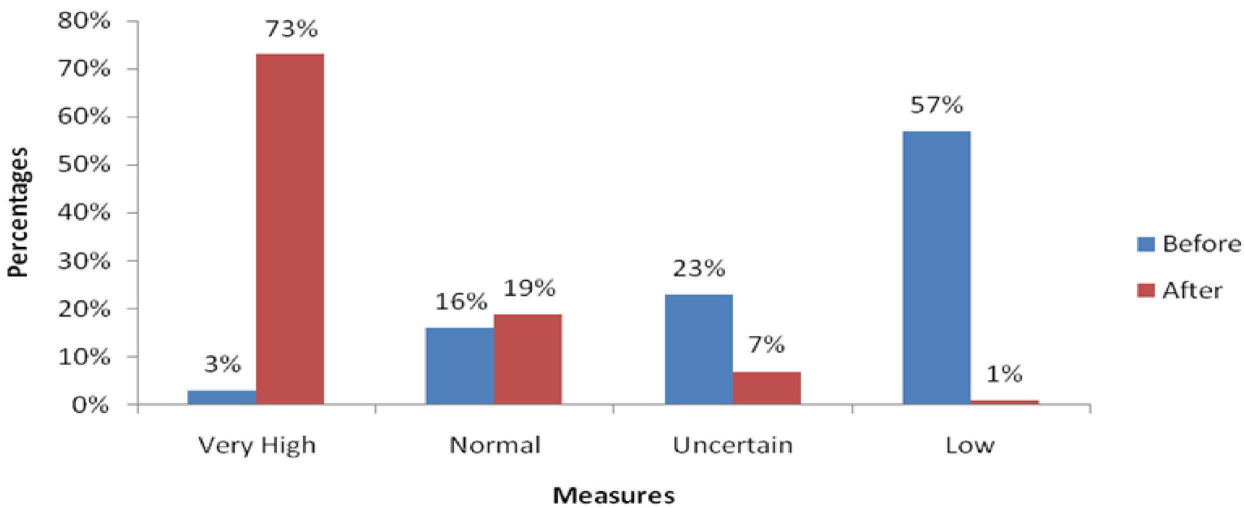

Figure-2. Profits before and after accessing Microfinance products and services

Source: Field Survey, 2015

On assets base, before accessing the products of microfinance institution, 78 (51%) stated their assets base were low, 42(28%) were uncertain while 22 (14%) indicated their assets base were normal and 10 (7%) stated that their assets base were high. However, after they assessed microfinance products over a period of time, 107 (71%) stated that their assets base were very high, 26 (17%) stated it was normal while 5 (3%) and 14 (9%) stated that their assets were low and uncertain respectively. The study found that the majority of SME owners acquired more assets as identified by Roodman and Morduch (2009).

On the ability to open new branches, before the assessment of products, 104 (68%) stated their ability to open branches was low, 36 (24%) were uncertain while 2 (1%) indicated their ability to open new branches was very high and 10 (7%) stated that it was normal. However after they assessed micro finance products, 98 (64%) stated that their ability to open new branches was now very high, 27 (18%) stated it was normal while 10 (7%) and 17 (11%) stated that their ability to open new branches was low and uncertain respectively as presented in Figure 3.

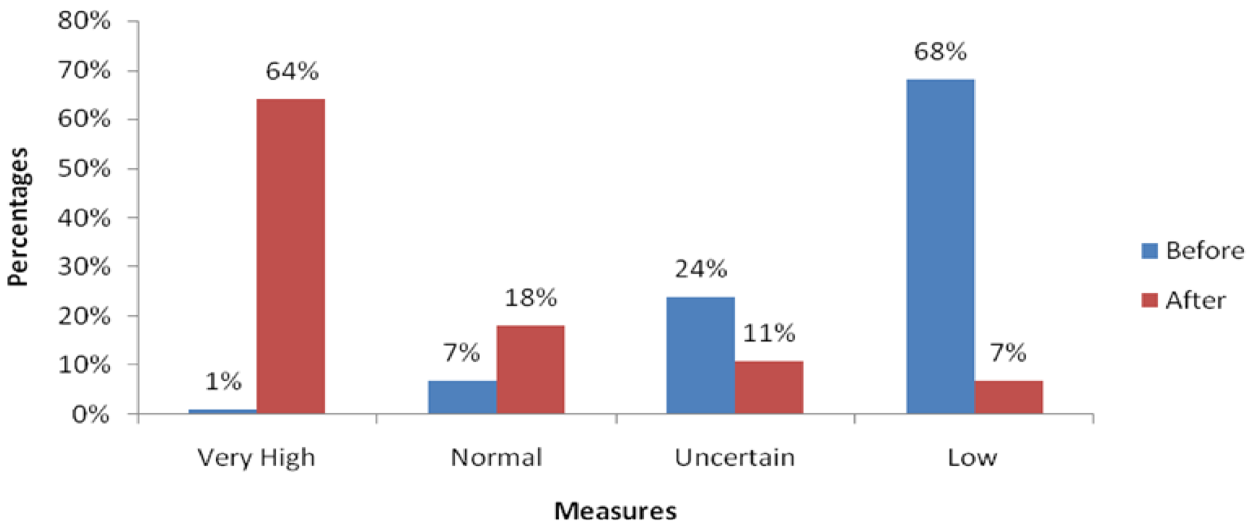

Figure-3. The ability of SME owners to expand their businesses before and after accessing Microfinance products and services.
Source: Field Survey, 2015

The above indicates that microfinance products and services have major effects on SMEs. The results above indicate that microfinance products and services over time are able to impact the revenues and profits of SMEs. The increase in revenues implies that SMEs generate enough capital in-house to expand and employ more people as corroborated by Idowu (2010) who established that there was a positive and significant relationship over time between MFI products and services and SMEs performance. He further states that there was a positive contribution of MFIs towards promoting SMEs' market share, production efficiencies and competitiveness. Advani (1997) praises the positive influence of microfinance products and services on SMEs as laudable because, the performance of SMEs is important for both economic and social development of developing countries. From the economic perspective, SMEs provide a number of benefits (Advani, 1997). Furthermore, the outcome of the study affirms the assertion of Afrane (2002) and Karikari (2011) that microfinance has the potential to make significant contribution to increase income and savings of SMEs to cope with challenges in everyday life.

5. CONCLUSION AND RECOMMENDATIONS

The study sought to establish the effects of the interactions between SMEs and microfinance institutions as well as outline the challenges that hinder smooth transactions between the two. The study revealed that though micro-credit has improved the business status of its clients in the form of increased revenue, increased profit, acquired more business assets and opened more branches than before microfinance intervention. Nevertheless, there are still some challenges that SMEs face. Notable among them include short duration for loan repayment, high interest rates, high loan processing fees and insufficient loan amounts. The paper therefore argues that for microfinance to improve the performance of SMEs, interest rates need to reduce, loan processing fees must be minimal, loan repayment period must be extended, loan process must be simplified and capacity building training for SMEs intensified.

Based on these findings, Microfinance institutions should repackage their products to make them conform to their main purposes, that is, to alleviate poverty and empower women. This involves reducing the requirement of collateral and revising the mode loan repayment. Many SMEs in Ghana are in the informal sector; therefore, microfinance institutions need to intensify their non-financial services and products to ensure that SMEs that come to them have the capacity to handle whatever capital inflow for efficient use. MFIs need to ensure the proper use of loans for the purposes intended as that facilitates business growth and development. This can be achieved by making credits or loans client-oriented and not product-oriented. Also, MFIs need to take appropriate and widespread monitoring activities for clients who are granted loans to sustain MFI operations and enhance the growth of SMEs. Micro Finance Institutions need to research into very profitable business lines and grant loans to clients who have the capacity to capitalize such business lines in order to reduce default rates.

Finally, SMEs should keep record books and update them regularly to ease the process of self-assessment before assessing any product or service from a microfinance company or other financial institutions, especially, if it is credit. SMEs also need to hire competent staff to improve efficiency and productivity. Proper structures need to be put in place to ensure proper checks and balances, especially, in finance. SMEs need to register their businesses to open them up for government intervention and also assist them to get access to micro loans from microfinance institutions and other formal financial institutions. They need to also pay their loans on time so that MFIs can offer credit to prospective customers.

In conclusion, the Government of Ghana should provide attractive environment for the establishment of vibrant micro finance institutions such as tax relief and seed capital which would bring about competition in the sector. When this happens, the high interest rates that SMEs are paying would automatically reduce so that varieties of micro finance packages can now be obtained at lower interest rates.

Funding: This study received no specific financial support.

Competing Interests: The authors declare that they have no competing interests.

Contributors/Acknowledgement: All authors contributed equally to the conception and design of the study.

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