Using Financial Statements to Analyze the Effects of Multiple Borrowings on SMEs Financial Performance in Tanzania

Chalu, H.★ & Lubawa, G. ★★

About the Authors

Henry Chalu★, University of Dar-es-Salaam School of Business (UDBS) -Tanzania
Galinoma Lubawa★★, Institute of Rural Development Planning (IRDP); Dodoma –Tanzania

Corresponding address: hchalu@gmail.com or galinoma@gmail.com

ABSTRACT

This study assessed the effects of multiple borrowing on entrepreneur's business performance in Iringa Municipality using financial statements collected from 102 SMEs. To analyse the data on the influence of multiple borrowing on financial performance, ratio analysis and paired sample t-test were used. The ratio analysis was divided into four categories: liquidity, profitability, efficiency and leverage. The empirical results indicate variations on the level of influence. In case of liquidity ratios, empirical results indicate that multiple borrowings have significant positive influence on current and quick ratios. For profitability, the multiple borrowings have significant positive influence on all three out of four (i.e. gross profit ratio, net profit ratio, and return on equity). Likewise, the empirical results show that multiple borrowings have significant positive influence on all indicators of efficiency and leverage ratios. The findings suggest that despite the challenges of multiple borrowings, the approach can used to improve financial performance of SMEs. However, for that to be achieved then it is necessary to control the risks of multiple borrowings through information sharing among MFIs, introduction of flexible financial services, financial education for microfinance clients, and introduction of friendly financial statement framework for SME.

1.0 INTRODUCTION

A number of empirical studies find that small and medium enterprises (SMEs) operators frequently choose to borrow from multiple lenders to finance their business investments. In this study, SMEs is defined based on capital investment to include all small and medium enterprises with capital investment of up to Tanzania shillings 200,000,000. Estimates of the incidence of multiple borrowing vary across countries. For example, based on survey involving microfinance clients in Iringa Municipality in Tanzania, Mpogole *et al.* (2012), Chalu and Lubawa (2014), reported that over 65 percent of the clients had at least two loans form Microfinance Institutions (MFIs) at the same time while 33 percent had three or more loans contracts with different MFIs at the same time. Examining microfinance markets in Nicaragua, Morocco and Bosnia-Herzegovina, Chen *et al.* (2010) report incidences of multiple borrowing between 20 and 40 percent of active borrowers. Boiwa (2014) found significant relationship between loan repayment and existence of multiple borrowing in Kenya. In Bangladesh, a study estimated that 15 percent of all MFIs borrowers took loans from more than one MFI back in 1990(de Aghion *et al.*, 2005). In Ghana, multiple borrowing has been mentioned as a source of over-indebtedness (ProCredit, 2009), while in Peru, over 20 percent of microfinance clients found to have loans from more than one institution (Copeme Microfinanzas, 2010). In India, Krishnaswamy (2007) estimates that in 17 MFIs operate, the incidence of multiple borrowing is about seven percent. These few studies suggest the existence of multiple borrowing in microfinance market. Schicks and Rosenberg (2011) point out that multiple borrowing is increasingly common, especially in more mature credit markets.

In practices, SMEs' operators tend to borrow from multiple credit suppliers or different relatives and friends concentrated in the same geographical business area or not. They tend to differentiate their allocation of borrowing in the sense that they do not obtain equivalent amount of credits from multiple lenders, but rather they systematically borrow more from some of the lenders being a MFI or relative or friend. Depending on data source, multiple borrowing refers to households that borrow from multiple MFIs or to households that borrow from MFIs as well as other sources like relatives, or friends (Mpogole *et al.*, 2012). SMEs are known to borrow from formal sources of credit like MFIs or other commercial banks as well as informal sources of credit like relatives, friends or neighbours. However, borrowing from informal sources of credits has got some challenges such as flexibility in loan repayment obligations and mostly no interest is charged. The amount of credit from these sources is usually not in SMEs books of accounts. Always data from these sources of credit are likely to provide limited information. Data from formal sources of credit, will obvious be available in the financial statements, and the size of loan and timing of repayment obligations are considered to be binding by SMEs.

However, for the purpose of this study, multiple borrowing refers to SMEs that borrow from multiple MFIs simultaneously and excluding other sources of credit. The prevalence of multiple borrowing in the microfinance industry is equivalent to assuming that the market cannot share information on customers they serve. The SMEs financing decision by acquiring multiple borrowing is not an amazing decision in business, rather it is a kind of innovation to boost the capital growth if the loans taken could be used solely for business purpose intended. The study is therefore guided by the major assumption that a well-planned multiple borrowing may increase debt financing and facilitate availability of funds for business opportunities arises. The study argues that therefore the presence of multiple borrowing to SMEs may improve the performance.

1.1 Causes and Consequences of Multiple Borrowing

The literature suggests a number of reasons, which have driven SMEs into multiple borrowings: first, a mismatch between the size of the loan and the business needs. In order to obtain the missing capital, SMEs operators might find it convenient to hide the real level of indebtedness and ask for additional loans at different MFIs (Jain, 2010; Diaz *et al.*, 2011; Mpogole *et al.*, 2012). A second potential cause is ex-post i.e. that is after the loan is taken and invested; some unexpected negative shocks can hurt borrowers and their businesses. This can make it impossible for them to repay the loan. Thus, borrowers might decide to take a second loan in order to repay the first loan. But this

consequently increase their level of indebtedness (McIntosh *et al.*, 2005; McIntosh and Wydick, 2005; de Janvry *et al.*, 2008). A third potential cause is in case of default, the client can take out a second loan to repay an earlier loan or simply start over after the first MFIs refuses to advance another loan due to a tarnished credit history. Interest rates may also vary across the sector, encouraging client to go to a second microfinance lender (Jain, 2010). This only occurs in the presence of information asymmetry about client indebtedness (Jain, 2010). According to Chijoriga and Cassimon (1999), information asymmetry is one of the major SMEs problems. Other possible explanations for multiple borrowing have more to do with limitations inherent to the banks which limit access of SMEs to bank loans or fail to offer loan according to SMEs requirements. Carletti *et al.* (2007) argues that if a bank is unable to achieve a satisfactory level of diversification for its loan portfolio, then the bank may deliberately decrease the size of its loans in order to issue a larger number of smaller sized loans. These loans are unsatisfactory, thus drive SMEs into multiple loans. Other studies from Uganda (McIntosh *et al.*, 2005) and India (Morduch *et al.*, 2003; Venkata and Yamini, 2010) show that continuity, convenience; flexibility and reliability of access to financial services are considered reasons that drive the poor into multiple borrowing.

Advocates of multiple borrowing have revealed that the tendency can have non-financial effects too as follows; *Borrowers are less dependent on single MFI*: It is believed that one of the underlying premises of microfinance is that borrowers repay their loans in order to sustain a relationship that allows them to get another, often larger, loans (Chen *et al.*, 2010). This delicate relationship between lender and borrower can gradually be undermined as ever-higher levels of multiple borrowing take hold in a crowded market. Borrower can default with one MFI whether by choice or out of sheer necessity and retain their borrowing relationship with other MFIs. *Borrowers can borrow larger total amounts than before:* With more choices, it is expected that borrowers will have the option to increase their total borrowings. Many MFIs, especially in group – based lending, keep their loan sizes small expecting that their borrowers will be able to meet their full borrowing needs from additional sources (Chen *et al.*, 2010). This tacit loan syndication lowers a MFIs exposure to any single borrower and means borrowers have access to additional liquidity from which to repay their various loans. In this way, multiple borrowing can be beneficial to borrowers and the overall market (Chen *et al.*, 2010).

However, while the existing literatures acknowledge the presence of multiple borrowing and explanatory factors, when it comes to the consequences the literature are mixed. For example, Krishnaswamy (2007) finds that there is no difference in performance between multiple borrowers and single borrowers in terms of repayment record. Mpogole *et al.* (2012) claims that multiple loans adversely affect the loan repayment and eventually its financial performance. On the other hand, Chaudhury and Matin (2002) suggest that households borrowing from more than one MFI are observed to have a higher likelihood of irregular payment. Chalu and Lubawa (2014) suggested that multiple borrowing could lead to entrepreneur's business performance if loans taken could have been used solely for intended purpose and invested in business opportunities. Lubawa and Louangrath(2016) suggested that multiple loans has contributed to the movement of firms migrant from the Altman's Z score "safe zone" to the "gray zone "financial health of SMEs firms in Tanzania. On the effects of multiple borrowing on income levels of clients, Boiwa (2014) noted that the MFIs clients with multiple borrowing were able to increase their income, which had positive impact on other factors of daily life. In Ghana, Alnaa (2013) finds that multiple loans have a positive impact on beneficiaries' household consumption expenditure and by extension poverty reduction.

Scanty literature basing on primary data, suggests the following effects of multiple borrowing; over-indebtedness (Maurer, Klaus & Justyna Pytkowska, 2010; Wisniwski, 2010; Engel *et al.*, 2014), poor loan repayment practices (Mpogole *et al.*, 2012; Afroze *et al.*, 2014), and consequently default on loans that might lead to financing cut-off and without access to funds, business will stop growing or even go bankrupt. Other studies have also found multiple borrowing may results into increase incidences of over-indebtedness and consequently default on loans, and collapse of the business (Gwendolyn, 2001; Vogelgesang, 2003). In general, these studies have

shown that lack of control and discipline in multiple borrowing can lead to over-indebtedness where a borrower takes more loans than she or he can repay. As a result, when loans are not paid as scheduled, financing is cut off and without access to funds, and SME will stop growing or even go bankrupt. Bartocha (2010) suggested that if not well managed, multiple borrowing could become a problematic to firm's financial performance and that reflect lack of financial discipline.

Iringa Municipality has many MFIs that give loans to borrowers. The majority of these MFIs were started when the government of Tanzania developed the National Microfinance Policy in line with the overall financial reforms initiated in 1991. Micro credits that started as a result of the microfinance policy include; Promotion of Rural Initiative and Development Enterprises Tanzania (PRIDE Tz), FINCA, Mama Bahati Foundation (MBF), Bayport, Building Resources Across Community – Tanzania (BRAC-Tanzania), Small Industries Development Organization (SIDO), and several Savings and Credit Cooperative Societies (SACCOS). In this case, clients have freedom to choose from among the many MFIs to apply for loans.

It is believed that the microfinance industry in Iringa Municipality recently has been growing at the unprecedented rates over the recent years (Mpogole *et al.*, 2012). This growth has been driven by increasing competent and confident MFIs with a social mission to increase outreach to the poor and the unbanked. It is also believed that the increment has caused a great competition among the MFIs available at Municipality (Mpogole *et al.*, 2012). Competition is increasingly a cause for concern in microcredit markets at Municipality. A growing number of institutions enter the market, motivated by goals spanning from poverty reduction to profit maximization. This competition is a positive phenomenon, because on the other hand has enabled microfinance clients to have a wider choice of services as from which MFIs they take a loan. Mpogole *et al.*, 2012 has shown that the prevalence of multiple borrowing at Iringa was very high, over 70% of the 250 microfinance, clients interviewed had at least two loans from different MFIs at the same time and consequence a borrower is associated with poor loan repayment schedules. Although these findings have obtained from different environments, but their important are also directly speak to Iringa environment too.

However, multiple borrowing should not be condemned or discouraged as a harmful behaviour. This is because there are yet others who managed multiple loans and make successfully of their businesses. Some evidence show that multiple borrowing may even is associated with better repayment rates in some environments (Krishnaswamy, 2007). Other benefits of multiple borrowing include; borrowers' less dependent on a single MFI and borrowing of larger amounts than before that lead to business growth (Chen *et al.*, 2010).

It is suggested that the tremendous growth of microfinance industry is expected to be one of the best alternative sources of capital to most SMEs operators and also as a means of improving their business performance. Yunus (1984) argued that the availability of credit to small business and low income households could greatly enhance their economic strength and eventually break the vicious circle of low income – low saving – low investment – low income. Growth of MFIs in Iringa has led to competition among existing credit suppliers (Mpogole *et al.*, 2012). As such make them reluctant to share information about the fundamentals of their debtors due to the lack of well-functioning credit information system (Chalu and Lubawa, 2014), and puts pressure on them to innovate credit prices and drive costs down, by considering that a customer is a foundation of a business and ensures its existence (Drucker, 1985).

Empirical studies conducted in this area used different techniques for data analysis. For instance, Chalu and Lubawa (2014) used descriptive analysis to study the primary data on the perceptions of SMEs' operators on the effects of multiple borrowing on business performance. Mpogole *et al.* (2012) used descriptive and logistic regression analysis to study the primary data on the effects of multiple borrowing on loan repayment. The results for these studies are based on perceptions of SMEs owners. None of these studies has used financial records to arise that effect. As such apart from findings, this is the case, the extent literature conducted so far. The present study used ratio analysis and paired sample t-test to study secondary financial data to analyse the effects of multiple borrowing on SMEs financial performance by comparing when an SME had

single loan in previous financial year and then the same SME acquired multiple loans on the following financial year from multiple MFIs simultaneously. Basically the objective of this study is to assess whether financial statements data can help us to understand the effect of multiple borrowing on SMEs performance. This approach we consider to be more appropriate because SMEs becomes a unit of analysis.

This study therefore attempt to cover the that knowledge gap by focusing on the financial statement, which is likely to be used to compare the performance of a SME at different situation, hence being consistent with financial ratio analysis which is one approach of measuring and monitoring financial performance. According to Sørensen (2012), the ratio analysis drawn on the contents of the financial statements can be used to show how business venture earn money (profitability), meets short-term obligations (liquidity), productivity use of assets (efficiency) as well as manage long-term debt (leverage). To address, the main objectives for the study were; to assess the extent do multiple borrowings influence liquidity, profitability, efficiency and leverage of SMEs.

2.0 LITERATURE REVIEW AND HYPOTHESIS STATEMENTS
2.1 SMEs and Financial Performance Indicators
The study reviews the relationships between multiple borrowings and the SMEs financial performance. Performance measurements in SMEs is a subject which has been covered by a number of studies (Brouther and Nakos, 2004; Chong, 2008; Oweseni and Adeyeye, 2012; Phillips, Tan-Tsu and Shanka (2012), Torugsa, O'Donohue and Hecker, (2012). These studies have different perspectives on the performance measures. For example, Oweseni and Adeyeye (2012) consider SMEs performance as a degree of achievement of organizational goals. This perspective defines performance in broad aspect to include both financial and non-financial performance measures. The broad perspective is supported by Phillips *et al.* (2012), who argues that broad perspective of performance measures is necessary for effective strategic management. Phillips and others provide three types of measures which include; resource input measures (e.g. employee skills and organizational commitment); behavioural measures (e.g. operational process and compliance to procedures) as well as outcome measures (e.g. sales, profit, customer satisfaction and customer loyalty). Phillips and others as well as Oweseni and Adeyeye (2012) used both financial and non-financial performance measures and found that financial measures are used more than non-financial measures. This is contrary to Chong (2008) who found that owner-managers of SMEs tend to use combined approach by using both financial and non-financial performance measures. In this study, we use financial measures for three reasons. First, while non-financial performances are relevant, but they may be influenced more by other variables than multiple borrowings. Second, multiple borrowings has financial implications as such using financial measures can help us detect the financial impact of multiple borrowing. Lastly, financial measures are being accepted by various studies as good indicators of performance (Boardman and Vining, 1989; Commmander, Fan and Schaffer, 1996).

In accounting, financial performance of the organization is usually assessed through financial statement analysis (Palepu *et al.*,2013). As argued by Palepu *et al.* (2013), that financial statement summarizes economic consequences of business activities of the organization. These financial statements are constructed from entity's activities in accordance with generally accepted accounting principles (GAA), or international financial reporting standards (IFRS). In case of SMEs, there are special accounting standards for SMEs (IASC Foundation, 2009) which set out a stand- alone set of principles and disclosures for SMEs to meet the financial reporting needs and to maintain easy and accurate economic decision making by a broad range of resource providers and other users, such as non-manager owners, lenders, vendors, and other creditors, customers, and employees (Pacter, 2009).

These standards prescribe the financial statements which have to be produced by SMEs. Financial performance can be measured using return on equity, solvency, sales growth, liquidity and profitability (Piotroski, 2002; Sørensen, 2012). This approach will allow usage of complementary

measures to access financial performance because using only one approach may limit the differentiation between good performance and bad performance (Piotroski, 2002).

Developing and running the business requires cash for short-term obligations as well as long-term Sørensen (2012). It is therefore particularly important for the business developer to continually assess whether the growth of the business is maintained through earnings or if further external capital is required. If external capital is needed, should it be single loan or multiple loans. The question of source of the finance for SMEs or any business venture requires the financial plan (Sørensen, 2012). Therefore, it is expected that SME taking multiple loans is part of their financial plan, and expected to yield positive results. According to Saccurato (1994) and Chittenden (1998), SMEs in emerging markets tend to rely heavily on own financing, trade credit and short term bank loans to finance their operations. However, in practices, it is not commonly for SMEs operators to have formal finance plan (formalized and written out), their plans and records for daily activities and future activities sometimes went unrecorded. Even though SMEs are getting problem or there are difficulties facing SMEs to prepare financial statements, number of efforts have been done to help SMEs. For example, efforts by the international accounting standard board (IASB), with IFRS for SMEs, American Institute of Certified Public Accounts (AICPA), and so on have helped to provide accounting framework to enable SME prepare financial statements (AICPA, 2013; IASB, 2007; Stainbanh, 2008). These efforts recognized the need for financial reporting is there in SMEs and other companies. The differential reporting according to Stainbanh (2008) is justified by two reasons users' needs and cost/benefit constraints. The furi justification i.e. users' needs is the one which motivate this study, because users have to use and evaluate information contained in the financial statements to make decisions. Users' needs underscore the unpaid of financial statements in making predictions about future financial performance of the organizations. A number of studies have used financial statements to assess financial performance of different organizations (Piotroski, 2002). Ponikvar *et al.* (2009), for example used financial performance to determine managerial decision-making in a growing firm. Fagiolo and Luzzi (2006) determined the negative impact of liquidity ratios on the growth of Italian manufacturing firms. Beaver's (1966) examined the significance of financial ratios with reference to corporate bankruptcy. Thus, this study classified financial ratios to evaluate four aspects of operating performance and financial conditions which were liquidity, profitability, efficiency and leverage.

2.2 Liquidity for SMEs

Liquidity reflects the ability of a firm to satisfy its short-term obligations as they become due (Khan and Jain, 2012). Liquidity management in small firms can be defined as the planning and controlling of cash flow by owner-managers in order to meet their daily commitments (Collis and Jarvis, 2000). In this study the analysing involves examining the relationship between current assets and current liabilities to determine whether the SMEs' can fulfil its obligations for current liabilities in the short run before and after taking of multiple loans. To achieve that, three ratios; current ratios (CUR), quick ratios (QUR) and cash ratios (CAR) were used to assess the liquidity of SMEs.

The current ratio (CUR) is current assets divided by current liabilities (Friedlob and Schleifer, 2003). In this this study, research, the conversional rule of 2 to 1 is considered satisfactory assuming that there is no standard measure (Khan and Jain, 2012). However, one limitation of CUR is that it does not consider the degree of liquidity of each of the components of current assets. In other words, if the current assets of firms were mainly cash, they would be much more liquid than if comprised of mainly inventory. If the ratio is less than one, current liabilities exceed current assets, and then firm's liquidity is threatened. For a firm with multiple loans it is expected that current assets would be large enough to cover its current liabilities because will have enough fund for business operations, acquire inventory reducing the possibility that the level of stock will not fall below normal hence adequate cash and cash equivalents.

Quick ratio (QUR) is current assets minus inventories, divided by current liabilities (Friedlob and Schleifer, 2003). The QR also known as acid test ratio is the more rigorous test of short-term liquidity because it addresses the limitations of current ratio. It uses only the most liquid

current assets such as cash, short-term investments and accounts receivable. The conversional rule of 1 to 1 is considered optimal assuming that there is no standard measure (Khan and Jain, 2012). A firm needs to maintain a QUR that is neither too low nor too high. A ratio that is too high indicates inefficient use of resources while a ratio that is too low is a sign of possible cash shortages.

The cash ratio (CAR) is even stricter than the quick ratio and measure the ability of a firm to pay its current liabilities with the cash and investments it has on hand. The ratio of 1 to 1 is considered optimal in case there is no standard (Khan and Jain, 2012). The CAR is useful when the collectability of an enterpriser's accounts receivables is in doubt as practices revealed that small firms tends to feel powerless to late payments from their debtors (Drever,2005). As such the following hypothesis was tested: *Multiples borrowings are positively related to liquidity level of the SMEs.*

2.3 Profitability for SMEs

One of the most important issues for any business is maintaining profitability. As SMEs strive toward growth, the need for a profitable the need for external funding, which particularly affects profitability because interest paid reduces the net profitability and the surpluses available for distribution as shareholder dividends (Sánchez *et al.* 2011). The profitability of a firm can be measured by profitability ratios on the basis of either sales or investments (Khan and Jain, 2012). In this study, the gross profit margin(GPM), Net profit margin(NPM), net return on total assets(ROA), return on equity(ROE) were used to assess the profitability ratios of SMEs. The Gross profit margin (GPM) indicates how well the company can generate a return at the gross profit level. It is calculated by dividing the gross profit by sales. The higher GPM ratio, the better. The net profit margin (NPM) is widely used as measure of a firm's profitability; is calculated as the firm's net income after taxes divided by net sales. The higher NPM ratio is considered the better. The net return on total assets (ROA) is measured as the firm's net income divided by total assets. Here the study measured the return on investment in assets after SME had covered its operating expenses, interest costs, and tax obligations. The higher the ROA ratio, the better. The return on equity (ROE) measures the return that shareholders (SMEs' operators) earned on their equity invested in the firm. It indicated how well the firm had used the resources of owners. The return on equity is measured as the firm's net income divided by stockholders' equity.

The literature on profitability suggests positive relationship between profitability and debt. While some authors identified positive association between debt and profitability, others got a negative relationship between firm's profitability and capital structure. For instance; Taub (1975), found significant positive relationship between debt ratio and profitability. Nerlove (1968), Baker (1973), Petersen and Rajan (1994), Margaritis and Psillaki (2010), Aliakbar, Seyed and Pejman (2013), also identified positive association between debt and profitability. Ross (1977) and Heinkel (1982) suggest that increasing leverage, by acquiring debts should have positive implications for firm value and performance. The previous studies concluded that firms prefer debt financing because they anticipate higher returns. Abor (2005), investigated also the link between capital structure and profitability of firms listed in Ghana Stock Exchange by using regression analysis, he witnessed a significantly positive relation among return on equity(ROE) and the short-term debt and total debt, while a negative relationship with long-term debt.

It could be expected therefore that for a firm financed by multiple loans, and use the borrowed funds efficiently and effectively by capitalising on existing opportunities, then profitability can be guaranteed. It was therefore hypothesized in general that: *Multiple borrowings are positively related to profitability level of SMEs.*

2.4 Efficiency for SMEs

Efficiency ratios—for the most part, turnover ratios—can be used to evaluate the benefits produced by specific assets, such as inventory or accounts receivable, or to evaluate the benefits produced by the totality of the firm's assets (Fabozzi *et al.*, 2003). A low ratio could mean that SME was overcapitalized or carrying too much inventory. A high ratio could be deceptive. A firm with fully

depreciated older assets could have an artificially high ratio even though those assets were no longer operating efficiently. However, efficiency ratios are not independent of liquidity ratios (Karaduman *et al.*, 2010). Poor debtors or inventory turnover ratios limit the usefulness of the current and acid-test ratios (Khan and Jain, 2012). Therefore, efficiency ratios should be examined in conjunction with relevant liquidity ratios affecting efficiency ratios. Three efficiency ratios were considered for this study, which are inventory turnover (INT), Accounts Receivable Turnover (ART), and Total Assets Turnover (TAT).

The first measure of efficiency ratios is INT which indicates how quickly SME has used inventory to generate the goods and services that are sold, and how fast inventory is sold. A high ratio is good from the viewpoint of liquidity and vice versa. The second measure of efficiency is ART which measure how effectively a firm is using credit extended to customers to increase sales (Fabozzi *et al.*, 2009). The downside to extending credit is the possibility of default - customers may not pay according to their promise. The benefits obtained from extending credit is referred to as net credit sales (i.e. sales on credit less returns and refunds). The ratio indicates the number of times debtors turnover each year into cash. The third measure of efficiency is TAT which measure of how well assets are being used to produce revenue. A high TAT is beneficial for a firm.

However, the INT and ART mentioned above reflects the benefits obtained from the use of specific assets (inventory and accounts receivable) (Fabozzi *et al.*, 2009). Because total assets include both tangible and intangible assets, these turnover indicates how efficiently all assets were used. If the liquidity is expected to have positive relationship with multiple borrowing, the same could be observed in efficiency ratios. It was therefore hypothesized in general that: *Multiple borrowings are positively related to efficiency level of SMEs.*

2.5 Financial Leverage for SMEs

Financial leverage, according to Gill and Mathur (2011), is defined as the degree to which a firm utilizes borrowed money. As such financial leverage or gearing is concerned with using borrowed fund to acquire assets. As put by Kumar and Rao (2015), the acquisition of assets is usually done based on the assumptions that these assets will generate revenues which are greater than costs of borrowing. This is consistent with the views of Modigliani and Miller (M&M) that firm can maximize their values by maximizing the use of debt financing (Lewellen & Mc Connell, 1978). According to Modigliani and Miller theorem in Corporate Finance of 1958, under certain assumption, the value of a firm is not affected by whether it is financed by equity or debt (borrowing money). According to Modigliani and Miller theorem in Corporate Finance of 1958, under certain assumption, the value of a firm is not affected by whether it is financed by equity or debt (borrowing money). Financial leverage therefore, is expected to allow SMEs to increase investment beyond what would be possible through their own funds. Likewise, financial leverage can increase return on investment to shareholders and provide tax advantages. As argued by Ghosh and Jain (2000), financial leverage may increase benefits to the shareholders through the tax deductibility of interest payments corporate dept. However on the issue of tax advantages, existing evidence from existing literature is still inconclusive (Ghosh & Join, 2000). It is expected that multiple borrowings can provide those advantages to SMEs. However, on the contrary, SMEs with multiple borrowings may increase risk of bankruptcy as per optimal capital structure theories (Ghosh & Jain, 2000; Kumar, 2008). As such the SMEs will be expected to balance between debt and equity financing. Three leverage ratios were considered namely; Debt to Total Asset (DT), Debt to Equity (DE) and Times interest Earned (TIE). It was therefore hypothesized in general that: *Multiple borrowings are positively related to leverage level of SMEs.*

3.0 METHODOLOGY

This research was carried out in Iringa Municipality, in, Tanzania. The location was purposively selected for major reason that prevalence of multiple borrowing is very high due to growing number of MFIs competing for microfinance services provision (Mpogole *et al.*, 2012, Chalu and Lubawa, 2014). The study was carried out between Junes to November 2012, and involved a survey covered 102 SMEs in Iringa Municipality. The design component of the study was undertaken under single blind condition to assure objectivity and minimize behavior modification by the subjects (Dubourg, 1852). The study adopted purposive sampling technique, where 102 SMEs were reached to get financial annual reports with their consent. The 102 firms included in the sample were the ones that had required specific characteristics required for this study. Sample size was estimated by using the following formula (Amin, 2002).

$$n = \frac{Z^2 \sigma^2}{E^2} \tag{1}$$

where n = sample size; σ = estimated population standard deviation; and E = standard error determine by $E = \sigma / \sqrt{n}$. Table 1 provides the distribution of the sample by industry.

Table 1. Industry distribution of the sample

Industry name	Number of firms
Flour and Mills	22
Cement and Construction materials	12
Manufacturing	18
Foods	20
Retail & Wholesale	30
Total	**102**

From this sample size of 102 SMEs 2010 and 2011 financial statements were collected. The financial statements collected were income statement, balance sheet and cash flow statement. In other words, the study utilized basic financial statements only. One justification for using basic financial statements, is that most SMEs are not sophisticated as far as accounting is concerned, as such most of them they just prepare basic financial statements. This perspective is also supported by the international accounting standard board (IASB) action of developing simplified version of IFRS applicable to SMEs only (IASC Foundation, 2009). Another justification is based on the previous one that majority of SMEs do not prepare financial statements for external uses. This implies that the financial statements prepared by SMEs since are not for external consumers, usually will not have in-depth disclosures. And in some cases, financial statements are prepared if the SMEs want to access loan particularly from MFIs. As argued by Epstein (2007), that financial statements should serve as an anchor between the credit suppliers and SMEs to predict the amount of the perceived risk.

The financial statements collected were divided into two categories before multiple borrowing (i.e. single borrowing) phase and after multiple borrowing phase. Average values were computed for each phase for every variable of financial performance (that is items/ratios of efficiency, liquidity, profitability and leverage).

The data collected were analysed by employing descriptive statistics, financial ratio analysis and paired samples t-test was used to test whether the difference between financial performance pre and post-acquisition of multiple loans were statistically different for liquidity, profitability, efficiency, and SMEs.

4.0 FINDINGS AND DISCUSSION

The results of this study are categorised into validity, reliability and descriptive statistics as well as inferential statistics. In case of reliability test, the results are presented in Table 2. According to

results in Table 2, Crobach's Alpha ranges between 0.602 (for efficiency variable) to 0.737 (for liquidity variable). Then results indicates that internal consistency has been achieved because the Cronbach's Alpha is greater than 0.6.

$$\alpha = \frac{K}{K=1}\left(1 - \left(\frac{\left(\sum_{i=1}^{k}\sigma_{Y_i}^2\right)}{\sigma_x^2}\right)\right) \qquad (2)$$

where σ_x^2 is the variance of the observed total, and $\sigma_{Y_i}^2$ is the score of the component i in the sample.

Table 2. Reliability Analysis Summary (Cronbach's Alpha)

Indicator	Number of Items	Cronbach's Alpha	Status
Liquidity	6	0.737	Reasonably reliable
Profitability	8	0.710	Reasonably reliable
Efficiency	6	0.602	Reasonably reliable
Leverage	5	0.619	Reasonably reliable

In case of content validity, a pilot study with SMEs owners was conducted to determine the relevance and representativeness of items such as individual questions in a questionnaire to the intended setting. Eby (1993) described content validity as validation concerned with the relevance and representativeness of items, such as individual questions in a questionnaire, to the intended setting. Therefore, for SME to be included in the study sample the following criteria were considered; the existance of financial records, annual reports for time frame under study for financial year 2010 and 2011, amount of capital, multiple borrowings records/history, and loan contracts were the information asked during the pilot study with SMEs owners' to make assurance that the study designed to intended sample and ascertain respondents' knowledge. Our sample is carefully chosen in order to minimise selection-based endogeneity probability. We exclude those firms that do not keep financial records, do not prepare annual financial reports, no loan contracts and all SMEs that do not have multiple loan comparative financial information. The methodology adopted is supported by literature reviews and documentary evidence.

For the descriptive analysis, the results are presented on Table 3. Profitability ratios offer several different measures of the firm's ability to generate profits. According to table 3, the mean values of GPM, NPM, ROA and ROE show that there are statistical differences in using assets to generate revenues pre and post-multiple loans acquisitions. The standard deviations values of profitability indicators were found to be higher after multiple loans acquired. The mean variation is an indication of multiple loans higher profitability level.

In case of liquidity, the descriptive results indicates that with exception to CAR which generally deteriorated after multiple borrowing acquisitions, the mean values of CUR, QUR are in satisfactory level though there was slightly decrease at post-multiple loans acquisitions. However, the liquidity general trend shows good short term financial strength of the SMEs at post–multiple loans acquisitions. The mean differences is an indication that multiple loans decreases liquidity level.

In case of efficiency ratios, the descriptive statistics indicates that the mean for INT and TAT decrease after multiple loans acquisitions while ART show an increase in efficiency. This is an indication that after acquiring multiple loans there is fluctuation in efficiency variables. In case of

leverage, the mean values of DTA, and DE, were expected to increases as debt proportion tends to increase as results of multiple loans. The mean for TIE tremendously decreases at post – multiple loans acquisitions.

Table 3. Descriptive Statistics Summary

| Variable | Item | Mean | | Standard Deviation | | Sample |
		Before	After	Before	After	(N)
Profitability	Gross Profit Margin	23.7216	12.3125	4.75983	27.89010	102
	Net Profit Margin	17.5704	8.6057	2.74831	25.23936	102
	Return on Assets	20.5745	20.8716	5.21830	6.32492	102
	Return on Equity	24.8049	29.1020	5.78346	7.87985	102
Liquidity	Current ratio	4.6267	2.1529	11.29757	0.88601	102
	Quick ratio	1.4339	1.0075	1.91355	0.49525	102
	Cash ratio	1.0638	0.8203	1.65292	0.40308	102
Efficiency	Inventory Turnover	6.0048	4.3541	4.01956	3.12805	102
	Accounts Receivable Turnover	37.8137	44.0910	26.28520	29.14015	102
	Total Asset Turnover	1.2954	1.1224	0.50654	0.43317	102
Leverage	Debt to Total Assets	9.2176	30.8892	5.44332	6.06396	102
	Debt to Equity	6.2371	30.2588	5.63222	18.25895	102
	Times interest Earned	86.0088	1.1922E2	70.46391	83.80546	102

To analyze the relationship between multiple loans and financial performance of SMEs, paired sample T-tests were performed to determine whether there is significant relationship between multiple loans and SMEs' financial performance in terms of on liquidity, profitability, efficiency and leverage. These results therefore are presented in the following sections.

(i) Multiple borrowing and liquidity of the SMEs
In this first variable, it was hypothesized, multiple borrowing are positively related to liquidity of SMEs. Three items current ratio, quick ratio and cash ratio were used to access the financial performance difference of SMEs between before and after multiple borrowings. The results for the first hypotheses are presented in Table 4. According to Table 4, two items (current and quick ratio) show significance difference between before and after multiple borrowings. Current ratio with T = 2.246 and pValue = 0.027 and quick ratio (T = 2.019 and pValue = 0.046) were tending to be significant at 5%. However, a cash ratio (T = 1.358 and pValue = 0.178) was found to be not significant. As such the H₁ is partially supported by two items, namely current and quick ratios only.

Table 4. Paired Sample Test for Liquidity

| | | Paired Differences | | | | | | | |
| | | | | | 95% Confidence Interval of the Difference | | | | |
		Mean	SD	SE Mean	Lower	Upper	T	df	Sig. (2-tailed)
Pair 1	Current Ratios Before Multiple Borrowings - Current Ratios After Multiple Borrowings	2.47	11.12	1.10	0.29	4.66	2.25	101	0.027

		Mean	SD	SE Mean	Lower	Upper	T	df	Sig. (2-tailed)
Pair 2	Quick Ratios Before Multiple Borrowings – Quick Ratios After Multiple Borrowings	0.43	2.13	0.21	0.01	0.85	2.02	101	0.046
Pair 3	Cash Ratios Before Multiple Borrowings – Cash Ratios After Multiple Borrowings	0.24	1.81	0.18	-0.11	0.60	1.36	101	0.178

(ii) Multiple borrowings and profitability of SMEs

The second variable for financial performance is profitability. In this study it was hypothesized (H$_2$) that multiple borrowings are positively related with profitability of SMEs. Four items: GPM ratio, NPM ratio, ROA ratio and ROE ratio were used. The results presented on Table 5, indicate that three items GPM (with T = 4.252, pValue = 0.000); NPM (T = 3.552, pValue = 0.001) and ROE (T = 7.339, pValue = 0.000) were found to be significant at 1% significance level. On the other hand ROA (T = 0.722, pValue = 0.472) was found not to be significant. As such out of four items of profitability, three (3) items indicate that multiple borrowings have improved financial performance.

Table 5. Paired Sample Test for Profitability

| | | Paired Differences | | | 95% Confidence Interval of the Difference | | | | |
		Mean	SD	SE Mean	Lower	Upper	T	df	Sig. (2-tailed)
Pair 1	Gross Profit Margin Ratios Before Multiple Borrowings-Gross Profit Margin Ratios After Multiple Borrowings	1.141	27.10	2.68	6.08643	16.73	4.25	101	0.000
Pair 2	Net Profit Margin Ratios Before Multiple Borrowings-Net Profit Margin Ratios After Multiple Borrowings	8.97	25.51	2.53	3.96	13.98	3.55	101	0.001
Pair 3	Return on Assets Ratios Before Multiple Borrowings-Return on Assets Ratios After Multiple Borrowings	-.297	4.16	0.41	-1.11	0.52	0.72	101	0.472
Pair 4	Return on Equity Ratios Before Multiple Borrowings-Return on Equity Ratios After Multiple Borrowings	-4.30	5.91	0.59	-5.46	-3.14	7.34	101	0.000

(iii) Multiple borrowings and Efficiency of SMEs

The third variable used to test financial performance is efficiency. It was hypothesized that "multiple borrowings are positively related to efficiency of SMEs". Three ratios were involved namely; Inventory turnover, accounts receivable turnover and total assets turnover. The results for the third hypotheses are presented in Table 6. According to Table 6, all three indicators inventory turnover (T=13.090 and pValue =.000), accounts receivable turnover (T = -2.934 and pValue = 0.004) and total assets turnover (T = 5.147 and pValue = 0.000) show significant difference before and after acquisition of multiple loans.

Table 6. Paired Sample Test for Efficiency

| | | Paired Differences | | | | | | | |
| | | Mean | SD | SE Mean | 95% Confidence Interval of the Difference | | T | df | Sig. (2-tailed) |
					Lower	Upper			
Pair 1	Inventory Turnover ratios Before Multiple Borrowings – Inventory Turnover ratios After Multiple Borrowings	1.65	1.27	0.13	1.40	1.90	13.09	101	0.000
Pair 2	Accounts Receivable Turnover ratios Before Multiple Borrowings – Accounts Receivable Turnover Ratios After Multiple Borrowings	-6.28	21.61	2.14	-10.52	-2.03	-2.93	101	0.004
Pair 3	Total Assets Turnover Ratios Before Multiple Borrowings – Total Assets Turnover Ratios After Multiple Borrowings	.173	0.34	0.034	0.11	0.24	5.15	101	0.000

(iv) Multiple borrowings and Leverage of SMEs

The fourth variable used to test financial performance is leverage. It was hypothesized that "multiple borrowings are positively related to leverage of SMEs". Three ratios were involved namely; debt to total assets ratio, Debt to Equity ratio and Times Interest Earned. The results for the third hypotheses are presented in Table 7. According to Table 7, all three indicators debt to total assets ratio (T= -30.943 and pValue =.000), debt to equity ratio (T = -13.536 and pValue = 0.000) and times interest earned (T = -12.520 and pValue = 0.000) show significant difference before and after acquisition of multiple loans.

Table 7. Paired Sample Test for Leverage

| | | Paired Differences | | | | | | | |
| | | Mean | Std. Deviation | Std. Error Mean | 95% Confidence Interval of the Difference | | T | df | Sig. (2-tailed) |
					Lower	Upper			

Pair 1	Debt to Total Assets Ratios Before Multiple Borrowings Debt to Total Assets Ratios After Multiple Borrowings	-2.16	7.07	0.70	-23.06	-20.28	-30.94	101	0.000
Pair 2	Debt to Equity Before Multiple Borrowings – Debt to Equity Ratios After Multiple Borrowings	-2.40	17.92	1.77	-27.54	-20.50	-13.53	101	0.000
Pair 3	Times Interest Earned Before Multiple Borrowings – Time Interest Earned Ratios After Multiple Borrowings	-3.32	26.78	2.65	-38.46	-27.94	-12.52	101	0.000

This study assessed the effects of multiple borrowings on SME's business performance by using financial statements where financial variables; liquidity, profitability, efficiency and leverage ratios were used. The results indicate that current ratios, liquid ratios, gross profit margin, net profit margin, return on equity, inventory turnover, accounts receivable turnover, total assets turnover, debt to total assets ratios, debt to equity ratios and times interest earned of SMEs – were statistically positively related to multiple borrowings. These variables show that multiple borrowings have effects on SMEs' financial performance. As it observed from practices, it make valuable for SMEs to undertake multiple loans as most of them are poor cash.

4.2 The Influence of Multiple Borrowings on SMEs Liquidity
The analysis has revealed that firms' liquidity was in good ratios both before and after multiple borrowings. However, liquidity ratios magnitudes were decreases post – multiple loans. It is expected that this decrease would affect the cash management of SMEs as confirmed by downsized cash ratio that went below minimum (i.e.1:1) after multiple loans. The good performance in other areas such current and quick ratios actually expected to have indirect impact to cash management. This is an indicative that after acquisition of multiple loans, cash management did not disrupt the SMEs and lead to insolvency as the firms are still in operations. It can be argued that SMEs have done enough to manage the liquidity position, as justified by the MFIs decision to provide additional loans, though there were slight decreases in liquidity ratios.

The study also suggests that cash liquidity observed might have been influenced by the ability of SMEs to settle for multiple loans. Mpogole *et al.* (2012) claims that multiple loans adversely affects loan repayment. The problem here is how can SMEs manage current assets, current liabilities, cash conversion cycle and still balance its risk and return so as to ensure sustainable profits under influence of multiple loans.

As observed in really practices in Tanzania, most SMEs operators accepted the preparation of financial reports by their lenders just to support their loans applications. However, there is doubt if the SMEs operators are using the financial statements information contents to regulate their business as most of them are not good at working capital management (Atrill, 2006). Experience shows that most of SMEs in Tanzania operates without credit control department, no proper debt collection procedures, and poor methods of records keeping. Therefore, it can be argued that, multiple borrowing supported with good working capital management practices, will let the SMEs sector be improved significantly. It should be also noted that most of SMEs' assets are in form of current assets and they depend heavily on current liabilities as main sources of external financing against long-term capital markets (Petersen and Rajan, 1997). Thus it could be argued that effective liquidity management is indicative of overall SME management.

4.3 The Influence of Multiple Borrowings on SMEs Profitability

The results also show that there were improvements in firm's profitability. With exceptional to ROE, the results of this study showed signs consistent with theoretical predictions that profitability(GPM,NPM,ROA) is assumed to have a positive relationship with multiple borrowings. The relationship between profitability and multiple borrowings implies that access to multiple loans tended to improve sales, profitability and hence internal financing, if at all the loans taken were whole and exclusive employed in the intended businesses as planned and in new profitable business opportunities emerged.

However, practical experience shows that most SMEs have no debt collection procedures, and even credit policy. This casts doubt on the effect that delaying debts collection from debtors and payments to suppliers may have on SMEs profitability. Therefore, it can be argued that, good performance on profitability may have influenced by good performance on liquidity as evidenced by the findings. Diacogiannis (1994) confirmed the direct relation between profitability and working capital management. Therefore, it can be argued that despite of all managerial deficiency SMEs are facing, multiple loans are manageable to them and enhance room for profits.

4.4 The Influence of Multiple Borrowings on SMEs Efficiency

The results confirmed that efficiency ratios were in good position to most of SMEs after multiple borrowings. Although inventory ratios showed slight, decreases but this did not endanger the performance of most firms. Being in good liquidity position after multiple borrowing is an indication the SMEs are selling fast and goods do not stay in shelves.

However, the slightly decrease in inventory ratios, might have been caused by the possibility that SMEs operators were busy coping with increased operational activity that they did not have time to control its inventory position or due poor working management. The effect of this is obvious that the average payment period to suppliers and other stakeholders might have been decreased but not to the extent that affected the profitability and liquidity position of firms. The decrease in inventory ratio would adversely increase storage and inventory management costs and increase the risk of inventory obsolescence, eventually affect the SME profitability.

Despite the facts that SMEs tend to work manual, without proper debts collection procedures, however, the analysis revealed that the Accounts receivable turnover (ART) of the firms had been improving position for the period under review from 2009/2010 to 2010/2011. It indicated a shorter time between making a sale and collecting the cash. This may have been influenced by the acquiring of multiple loans and hence forced many firms to speed up cash collections so that they could pay multiple loan interests as they become due to avoid financial risk.

For total assets turnover, findings revealed that firms were less successful in keeping active the firm's assets after had been acquiring multiple loans in the year 2010/2011, due to decreased turnover of inventory. Despite these downtrends in turnover, majority of the SMEs operated under normal profits, confirming a significant relation between SME's profitability and number of days of accounts receivable and of inventory turnover. Results revealed by efficiency ratios, confirmed theoretical predictions, that working capital management is important to small and medium-sized enterprises because most of these firms' assets are in form of current assets., current liabilities are also one of their main sources of external finance. The findings comply with results of Peel and Wilson (1996), who noted the same that "efficient working capital management is particularly important for smaller companies. In this context, the efficiency ratios have provided empirical evidence about the efficiency of SMEs operators' on managing the business toward performance under multiple borrowings. However, it can be argued that, the good picture provided by the efficiency should be taken with highly consideration as it might be contributed by nature of business environment, which heavily depend on individual retailers as traditionally do business on cash basis to avoid defaults on payments.

4.5 The Influence of Multiple Borrowings on SMEs Leverage

On leverage ratios, the analysis revealed, Debt-total assets ratios of the firms had been increasing for the period under review from 2009/2010 to 2010/2011. The higher ratio is not a good indication as it imply that more assets have been financed by outside funds (multiple loans). The low ratios are desirable from the point of credit suppliers as it is an indicative of sufficient margin of safety. This increase does not mean that more assets were acquired by addition of second loan, rather might have been contributed by other factors. For instance, most of SMEs' assets are in form of current assets (Pedro Juan *et al.*, 2007). Large portion of current assets were consisting of larger amount of accounts receivable, thus decreased or increased in accounts receivable would actually tend to decrease or increase total assets of these firms and affect the debt to total assets ratios. Current liabilities are also one of their main sources of external finance to these firms (Pedro Juan *et al.*, 2007) and thus increase or decrease in current liabilities would actually tend to increase or decrease total debt and affected the debt-total assets ratios. An increase in debt to total assets ratio is not a good sign as business heavily depend on external financing. This is imply that the large portion of profit generated is spent on debt repayment.

In case of Debt-Equity ratios, the analysis revealed that the Debt-Equity ratios had been increasing position for the period under review from 2009/2010 to 2010/2011. This increment meant that creditors (MFIs) have put more funds in the SMEs than the owners themselves. Khan and Jain, (2012) suggests that a high proportional in the capital structure would lead to inflexibility in the operations of the firm as creditors would exercise pressure and interfere in management.

It should be noted also that, any time SMEs use debt financing, they are running the risk of bankruptcy and the more debt financing they use, the higher the risk of bankruptcy. The danger of this is that SMEs owners may behave irresponsibly and indulge in speculative activity (Khan and Jain, 2012). However, the results of this study have shown that in the presence of multiple loans, Debt-Equity-mix has a significant influence on the performance of SME. The results indicate that multiple borrowings positively affect return on equity (ROE) of SMEs. The findings comply with other studies such as by Ross (1977), Heinkel (1982) and Noe (1988) who suggested that increasing leverage, by acquiring debt should, have positive implications for firm value and performance. It also complies with the Modigliani and Miller Capital theory (1963) who studied on incorporating tax benefits as determinant of the firm's' capital structure choice. They argue that SMEs are able to maximize their value by employing more debt because of tax-shield benefits associated with debt use. Interest on debt is considered as a tax-allowable expense. However, the access to external finance should not go beyond its payment ability so as to avoid financial risk, as acquiring more loans is not a positive sign to the SMEs. Abor (2007) argued that employing excessive debts for SMEs is likely to result in high bankruptcy cost which affects firm's performance.

On the times-interest earned, the analysis revealed that the ratios had been increasing percentage wise for the period under review from 2009/2010 to 2010/2011. However, the increase may imply unused debt capacity. However, low ratios is a danger signal the SMEs are using excessive debt and does not have the ability to offer assured payment of interest to lenders. In general debt ratio have shown positive relationship with the performance of the SMEs. The debt ratios findings comply with other studies from several countries. For instance, Taub (1975) found significant positive relationship between debt ratio and measures of profitability. Hadlock and James (2002) also concluded that companies prefer debt financing because they anticipate higher returns (Khan and Jain, 2012).

5.0 CONCLUSION AND IMPLICATIONS

The results provide evidence that by using financial ratios there are financial performances differences between prior and post multiple loans of SMEs. The empirical results are indicative that multiple loans have significant influence on liquidity, profitability, efficiency and leverage of SMEs' especially for those who properly used the additional loans and invested on the existed opportunities. The results suggest that if well managed, multiple loans are not detrimental to financial status of SMEs, and in long run may lead to more productive operations. It therefore

recommend to a need of establishing an effective and efficient information sharing system (a credit Bureau) to prevent unnecessary over-borrowing among microfinance borrowers.

The findings contribute to the assessment of financial management practices in SMEs, and how these should be improved, as most existing literature tended to be based solely on the standards and practices used by large companies or those adopted by professionals such as accountants, consultants, banks, etc., with relatively little attention being paid to the practices actually used by owner-managers themselves. Nayak and Greenfield (1994) argue that owner-managers in their survey of 200 SMEs in the West Midlands did not use financial management techniques very effectively. Yet, these techniques are those designed for large companies and consequently the process of financial management and associated decision-making in SMEs remains something of "a black box" (Deakins *et al.*, 2000).

LIMITATIONS OF THE STUDY

This research study was mainly based on financial data derived from the SMEs' financial statements (annual reports). The reliability and the finding are contingent upon the data published in financial statements. Accounting ratios have its own limitation, which also applied to the study. The study is limited to one year before multiple loans acquisitions and the subsequent year with multiple loans, in order to be more certain, it is suggested study period to be extended.

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