DETERMINANTS OF SMALL AND MEDIUM ENTERPRISE (SME) FINANCING BY FINANCIAL INSTITUTIONS IN GHANA.

By

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DECLARATION

I hereby declare that this submission is my own work towards the CEMBA and that, to the best of my knowledge, it contains no material previously published by another person nor material which has been accepted for the award of any other degree of the University, except where due acknowledgment has been made in the text.

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DEDICATION

This work is dedicated to My Lord and my family, especially, Robert Ansah.

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ABSTRACT

This study investigated the definition of SME's as viewed by the financial institutions in Ghana. The study also investigated the SME loan eligibility criteria of the Ghanaian financial institutions. Data was collected through interviews of 10 bank and 5 non-bank financial institutions in Tema metropolis. The findings of the study indicate that there were some differences in the list of lending criteria of the bank and non-bank financial institutions.

However, the most important lending criteria for both bank and non-bank financial institutions is collateral. In addition although their relative level of importance differed the other common lending criteria were 'Audited account where applicable', 'Registered business and its documents'; 'Not less than six months accounts operation'. The definition of SMEs based on turnover was also found to be mainly two; annual turnover between GH¢1 and GH¢1,000,000; and annual turnover between GH¢5,000,000 and GH¢6.000, 000. Practical implications and future studies were discussed.

Bank financial institutions under this study were not having guarantor tax document and age of business as lending criteria for advancing credit to SME's. It was observed that low emphasis was placed on criteria such as business registration, credit history, and recommendation by risk managers.

The non-bank financial institutions are interested in major criteria such as collateral, guarantor, business registration documents, bank statement, audited account, recommendation by risk managers and credit history. The non-bank financial institutions place little premium on criteria such as tax documents and age of the business. The study therefore recommended that credit bureaus should be established to assess the peculiarities of SME's

Contents

LIST OF ABBREVIATIONS AND ACRONYMS

GH¢ - Ghana Cedis

GDP - Gross Domestic Product

IMF - International Monetary fund

NBFIs - Non-Bank Financial Institutions

SMEs - Small and Medium Enterprises

SSA - Sub Saharan Africa

CHAPTER ONE

INTRODUCTION

1.1 BACKGROUND OF THE STUDY

Small and medium-scale enterprise (SME) is defined as one which is independently owned and operated, and not dominant in its field of operation (Biryabarema, 1998). It can also be defined in terms of sales volume and by the number of employees in the business. Ownership and management is on family basis and as such has a small scale operation. While less than 5.5% of the formal work force is employed in SMEs in Azerbaijan, Belarus and Ukraine, this share is more than 80% in Chile, Greece, and Thailand and 31% in Nigeria (Ayyagari, Beck & Demirgue-Kunt, 2003). Similarly, the ratio of the informal economy relative to GDP varies from 9% in Switzerland to 71% in Thailand. In Ghana, available data from the Registrar General indicates that 90% 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 they are a major source of income and employment. It is estimated that SMEs employ 22% of the adult population in developing countries (Daniels, 1994; Daniels & Ngwira, 1992; Daniels& Fisseha, 1992; Fisseha, 1992; Fisseha & McPherson, 1991; Gallagher & Robson, 1995) and about 15.5% of the labour force in Ghana. The main financial challenge facing SMEs is access to affordable credit over a reasonable period. This is determined by the financing needs of SMEs and the action of banks. SME financing needs reflect their operational requirements, while the action of banks depends on their risk perception about the SME which is often influenced by several factors. Access to finance from banks remains a major challenge among SMEs in Ghana. According to the

World Bank discussion papers (1994) on supply and demand for finance of SMEs in Ghana, the success ratio for large firms applying for bank loans was 69 percent as against 45 percent for small-scale enterprises and 34 percent for micro-enterprises. Hence the data imply that the smaller the firm, the more important the constraint pertaining to the lack of access to finance.

Currently, there are 26 commercial banks, 136 rural banks, 53 non-banking financial institutions, and 157 microfinance institutions operating in Ghana to render various financial services to business which include loans and other forms of lending (Bank of Ghana). The client base of banks includes SMEs which forms the majority of businesses in Ghana.

Moreover, globalisation, mergers and acquisitions, and the emergence of new technologies have contributed dramatically to stiffer competition and pressures on profitability. In such a competitive marketplace, attracting profitable customers is a priority of all the financial institutions' (FI) managers especially banks. Banks are profit-seeking institutions that must provide acceptable returns to shareholders or go out of business. However, they operate under the objectives of profit maximisation through appropriate risk management strategy (Sinkey, 1998). This means that they must be prudent in the application of sound lending practices to assess the credit risk of the borrowers. It is reported that earnings from the lending activities account for more than 80 percent or more of the bank's profits (Wong, 1997). To estimate the borrowers' probability of default, Financial Institutions focus on the borrower's creditworthiness through gathering, processing and analysing timely and accurate information and small firms are no exception.

The availability of finance to SMEs is often determined by various factors ranging from the bank's ability raise funds to the firm or entrepreneurial characteristics of the SME. Firm characteristics include factors such as the age of the firm, the size of the firm and the availability of collateral and business information. Entrepreneurial characteristics are those traits or attributes that are specific to the owner of the firm which can impact on the performance of the firm negatively or positively. Entrepreneurial characteristics include the managerial competency of the owner of the firm, networking and gender.

Finance is provided in the context of information asymmetry on both sides (Fischer 1995) and can be resolved by demonstrating credit worthiness and project viability. Almost without exception, the financial institutions attempt to service SME clients with a package modified from their existing smaller "light" corporate clientele. As a result, there is strong emphasis on business documentation and financial reports. These are analysed basically in the same format as corporate applications, including time consuming cash flow analyses.

Firm size is considered one of the most important determinants of access to finance. Even among the SMEs category, there is still a large variation in size and there are "small SMEs" and "large SMEs" in terms of number of employees and revenue and asset base. Numerous studies have discussed that SMEs are financially more constrained than large firms mainly due to the high risk involved because small firms have a high failure rate compared to large firms. Calomiris & Hubbard (1990) noted that when the company is smaller, the restrictions on credit are greater. In order to reduce the anticipated risk and moral hazard associated with lending, the banks use collateral as one of the instruments. The collateral is an assurance to the bank in case of default and it also ensures the borrowers commitment to the loan repayments. According to Berger and Udell (1995) smaller and younger firms are more likely to face higher cost of financing and they are required to offer collateral which is often a challenge because they often have a small asset base to used as collateral.

Banks also consider the age of the firm when deciding on lending. Financing constraints are particularly severe in start-up enterprises and relatively young firms (three years old or less) According to Aryeetey et al (1994) 10 percent of start-up firms in Ghana could obtain bank loans but medium size enterprises and older firms are provided with credit three times more often than their smaller counterparts.

The industry sector also can be stated as a factor affecting access to finance. The financial institutions may show bias towards industry sectors that are growing.

In Ghana, the requirements that SMEs need to meet to qualify for financing by financial institutions vary from bank to bank. Some of the requirements that are common to almost all financial institutions are collateral security, SME's financial performance, audited financial statements, entrepreneurial experience and age of firm (Field work 2012).

The financial services industry in Ghana is highly regulated by the Bank of Ghana, thus impacting on the loan disbursement practices adopted by financial institutions. Although the SME loan eligibility requirements may vary from one financial institution to the other, the principle remains the same; to ensure that the financial institution does not loss from the loan transaction.

In the light of the above, the research question in this study is to explore the determinants of access to credit among the SMEs in Ghana.

1.2 PROBLEM STATEMENT

SMEs are vital for economic growth and development because they encourage entrepreneurship, generate employment, and reduce poverty (Kayanula and Quartey, 2000; Mead and Liedholm, 1998; Fischer, 1995).

The capacity for Small and Medium sized Enterprises (SMEs) to fulfill their potential in an economy depends on the availability of finance (Cook, 2001; Whincop, 2001). Finance is especially important for SMEs, since they are unable to finance themselves through retained earnings or equity financing.

Despite efforts, several empirical studies (Boachie-Mensah and Marfo-Yiadom, 2006; Beck et al. 2002) have shown that venture owners access to funds continues to pose the biggest challenge to their firms' growth and survival. In Ghana, both private and public finance support institutions (Venture Capital Trust Fund, Micro-Finance and Small Loan Centre, Export Development and Investment Fund, Business Advisory Fund etc) have been established, yet a number of surveys (Poku and Frimpong, 2009; BoG Report, 2009; Mensah, 2004), still indicate that access to funding continue to pose a challenge to SMEs' operations in the country, Although Commercial Banks and other Non-Bank Financial Institutions advertise for SME loans, An informal interview with a section of SME owners in Tema indicates that, most SMEs owners have serious difficulty in accessing financing. It is in view of this that it is worthwhile to ascertain the determinants of SME financing by financial institutions.

1.3 OBJECTIVES OF THE STUDY

The study seeks:

1. to determine the determinants of SME financing of financial institutions in Ghana

2. To compare loan eligibility criteria of banks and Non-Banks Financial Institutions.

3. To identify definitions of SMEs of financial institutions in Ghana.

1.4 RESEARCH QUESTIONS

The research questions for this study are as follows:

1. What are the determinants of SME financing of financial institutions in Ghana?
2. What are the loan eligibility criteria of banks and Non-Bank Financial Institutions?
3. What are SME definitions among financial institutions in Ghana?

1.5 SIGNIFICANCE OF STUDY

SMEs form an integral part of the growth of Ghana's economy. However, accessing finance from financial institutions has been a challenge for most SMEs mainly because they are usually not able to meet the requirements of the financial institutions, which are often not known to them. This study will be of significance in a variety of ways. The findings of this study will provide an insight to SMEs on the forms of SME classification used by various financial institution and the determinants of finance by financial institutions in order to assist them improve on their eligibility to access financial support from financial institutions.

Further, this study will inform SMEs, financial institutions, government and all interested stakeholders about the factors that restrain the provision of finance to SMEs by financial institutions.

Finally, the study will add to the literature in this area of research that can generate by future research.

1.6 SCOPE AND LIMITATIONS OF THE STUDY

According to Yin (1994), restricting a research to a case study may not provide a representative sample. Hence, a study on the determinants of SME financing by Financial Institutions in Ghana using financial institutions and located within the Greater Accra Region of Ghana only, which is just one out of ten regions of Ghana, may seriously constrain the external validity and generalization of this study.

In this regard, it is necessary to state here that, the sample size of this study is too small and woefully inadequate. Nevertheless, every effort will be made to ensure that the samples of financial institutions selected will be as representative of SMEs and financial institutions in Ghana as possible. Since the Greater Accra Region is a cosmopolitan area and has the largest concentration of industries and financial institutions in Ghana, it can be taken as fairly representative of the ten regions of Ghana. This accounts for the selection of Accra-Tema Metropolitan Area as the research setting.

In addition, this study shall make use of a relatively small sample size due to time constraint and cost associated with surveys involving large sample sizes.

Further, interview is often a frustrating process. There is the tendency of respondents providing unreliable information that could distort the outcome of the study. There is also the possibility of some banks not granting audience to researchers at all. Consequently, the possibility of some of the interviewee not responding interview cannot be ruled out.

CHAPTER TWO

LITERATURE REVIEW

2.1 INTRODUCTION

Despite the weight SMEs carry in local economies and the key role that they play as engines for economic development, SME access to financing in Sub Saharan Africa (SSA) is extremely limited. First, banking penetration rates are very low in SSA – the total amount of loans to the private sector only averages 18% of GDP (World Bank, 2006) – and second, it is mainly major corporate bodies that benefit from the bulk of financing. According to several studies (Africa practice, 2005; IMF, 2004; Aryeetey, 1998; World Bank, 2006), difficulties in gaining access to financing constitute the main stumbling block for SME development in SSA, far ahead of problems of corruption, deficient infrastructure and abusive taxation. These studies estimate that between 80 and 90% of SMEs experience important financial constraints. This can be easily understood in view of the reluctance of banks to grant credit to

SMEs in SSA, which can be clearly seen in their accessibility and eligibility criteria.

For many years Africa's formal banking system faced both high risk and high transaction costs in lending to small enterprises. Such impediments largely precluded their access to formal finance. For example, a survey which tracked bank borrowing by manufacturing firms in six African countries during the 1990s found that among those firms which wanted a loan, small firms had had substantially worse chances of getting one (Bigsten et al, 2003). The study controlled for many firm characteristics such as profitability and concluded that systematic bias by lenders was the most likely explanation. Indeed, banks in Africa did not need to develop the business of lending to small firms: they were operating profitably via the easier and safer role of lending to large firms, and by holding high-yielding government debt.

Enterprise surveys conducted by the World Bank reveal that close to 40 percent of small firms and 30 percent of medium-sized firms perceive access to finance as a major stumbling block to the growth of their operations (Peria, 2009). Data shows that bank financing to SMEs in Africa is less significant and more short-term than in other developing countries (Peria, 2009). This is particularly the case for small firm financing. In the large group of developing countries, bank loans devoted to financing small firms average 13.1 percent, while only 5.4 percent of loans are allocated to such firms by banks in Africa. Similarly, bank approvals for loan applications by small firms in non-African developing countries average 81.4 percent, whereas only 68.7 percent of such applications are approved by banks in Africa. Furthermore, while an average of 47 percent of small business loans are used to finance investments (as opposed to working capital)in non-African developing countries, the figure only reaches 28 percent in African countries. Importantly, all these differences are statistically significant (Peria, 2009)

Bank lending to SMEs in Africa is also more costly than in other developing countries. Fees charged on SME loans in Africa - an average of 1.97 percent of the loan value for small firms and 1.79 percent for medium-sized firms - are generally almost twice as high as in other developing economies. Interest rates on SME clients are also 5 to 6 percentage points higher on average in Africa than elsewhere in the developing world. For instance, banks in Africa charge on average close to 15.6 percent for loans to their best small firm borrowers, whereas interest rates in other developing countries hardly exceed 11 percent for these clients. At the same time, SME loans in the region appear to be riskier than those in other developing countries (Peria, 2009). This may be at the root of the higher interest rates observed in Africa. Indeed, the share of non-performing loans (NPLs) among small firm loans in Africa averages 14.5 percent compared to 5.5 percent in other developing countries. The NPL ratio for medium-sized firms is also higher in Africa (6.8 percent) than in other countries (5.1 percent), but the difference in means is not statistically significant (Peria, 2009).

The differences found in the scale, cost and riskiness of bank financing to SMEs in Africa compared to the rest of the world can be partly explained from banks’ responses to questions on the factors that drive and impede SME financing across countries is revealing. In non-African developing countries, more than three quarters of banks respond that the perceived profitability of the SME segment is a key driver for their involvement with SMEs, whereas only two thirds of African banks point to this factor as being important. At the same time, less than 40 percent of banks in non-African developing countries indicate that macroeconomic factors are significant obstacle to their involvement with SMEs, yet 60 percent of banks in Africa point to the state of the economy as constraining their involvement with these businesses. These responses suggest that policy-makers in Africa have a role to play - more so than elsewhere in the developing world - in helping to promote SME finance by adopting sound macroeconomic policies that reduce risks and increase profitability when doing business in Africa and financing firms in the region (Peria, 2009)

2.2 THEORETICAL FRAMEWORK

A theoretical debate in literature on SME accessibility to finance from banks has dominated the literature considerably. This debate focuses on two aspects of bank lending to SMEs. That is, informational asymmetries and reputational effects. The concept of Informational asymmetries suggests that there will be insufficient credit available for all sound or 'bankable' propositions (Stiglitz &Weiss, 1981). Asymmetric information means that there will be some proposals on which bank officers will not have 'perfect' information. For example, SMEs may have poor recordkeeping and obscure accounting. In some cases, entrepreneurs may be reluctant to provide full information about the opportunity they are taking advantage of because of concerns that disclosure may make it easier for others to exploit (Shane & Cable, 2002). There are also some categories of owners of SMEs that will face additional problems due to lack of security, such as young entrepreneurs or those from deprived areas. In addition, there may be asymmetries arising from location as well as sector. For example, owners of SMEs in rural environments may face difficulties with access to bank finance (OECD, 2008).

Reputational effects apply theoretically where SME owners are prevented by their own or others experiences from applying for debt finance. This provides a discouraged borrower effect (Kon and Storey, 2003; Fraser, 2005). That is, some small business owners may not access finance because at some stage they are discouraged from applying. For example women owners, who may be discouraged by perceived bureaucracy or financial requirements or are discouraged by a first refusal (Deakins, et al, 2005). Entrepreneurs may not seek finance if there are perceived issues .This could be either that they think they will be unsuccessful so there is little point in applying or a perception that they will not have the information and good credit history that they perceive as requirements of banks. It may occur where entrepreneurs from certain groups distrust bankers, as for example in the case of ethnic minority entrepreneurs since they may perceive institutional bias in banking institutions. Aspects of the literature have suggested that women seeking to start businesses may also form a category of discouraged borrowers (Roper and Scott, 2007).

According to Pandula (2011), credit rationing by banks and financial institutions exists due to adverse selection, moral hazard and contract enforcement problems. The adverse selection theory of credit markets originates with the paper by Stiglitz and Weiss (1981) in which they explained why the interest rate could not equate the supply and demand in the credit market. As discussed by Stiglitz and Weiss (1981), borrowers have inside information about the nature of the project they want financed and may reap substantial rewards from, talking up their projects. Moreover, while the lender gains if the loan is repaid with interest, it is not a beneficiary of any upside gain in the firm's performance; it is, however, a victim of any downside losses in the case of default. Lenders like banks therefore face difficulties in discriminating between good and bad credit risks and simply increasing the price of credit to all potential borrowers can lead to adverse selection. Rather than driving potential non payers out of the market, there may be systematic reasons why some of the highest risk firms are those willing to pay high interest rates (Pollard, 2003).

The other problem, moral hazard, can arise when lenders are unable to discern borrowers' actions that would affect the distribution of returns from an investment (Pandula, 2011). This means, after a lender has extended finance to a firm they are exposed to moral hazard, the risk that the firm will not perform in a manner sufficient to meet the contract. For example, once a loan has been secured, a borrower could use the proceeds of the loan for a higher risk purpose or a non income generating activity, necessitating costly ex post monitoring of the financial contract.

The third reason that causes credit rationing is the contract enforcement problems. Mushinski (1999) argued that credit market imperfections in developing countries derive not only from moral hazard and adverse selection problems but also from costly monitoring and contract enforcement. In contrast to countries characterized by well functioning legal systems, the problems are not as pronounced as in those where the mechanisms for enforcement of contracts, property verification and ownership are weak. Hence, the main reason for the contract enforcement problem is the poor development of property rights. Although this argument is not specifically drawn at SMEs, these problems are more associated with SMEs than large companies (Pandula, 2011).

Information and enforcement problems inherent in credit transactions can lead to imperfect credit markets (Pandula, 2011). It is also clear from the above arguments that the small firms' access to financing may either come from supply side market failure (rejection from the bank's side for reasons not connected with the viability of the proposal or high risk and costs associated with such loans) or demand side market failure such as insufficient information in the project proposal, high cost of bank credit etc.

2.3 EMPIRICAL STUDIES

Several factors have been noted as determinants for SMEs access to funds from banks and financial services (Pandula, 2011). These factors include firm size, age of firm, location and availability of good financial record keeping.

2.3.1 AGE OF THE FIRM AND ACCESS TO CREDIT

According to Pandula (2001), a number of studies have found that there is a correlation between firm age and access to credit. Being in the business for many years suggests that the firms are at least competitive on average. It can be argued that being an older firm means there is lower informational opacity. The reason is information required by the lenders to evaluate and process applications is readily available because these businesses have an established reputation or track record.

On the other hand, the new firms are not likely to meet the collateral requirements of the banks since they have not accumulated sufficient assets. Combined with the absence of information on their financial records, this makes difficult to lenders to assess lending proposals submitted by new firms. The studies conducted in the past have found that the financing constraints are particularly severe in startup enterprises and relatively young firms (three years old or less).For example, Aryeetey et al. (1994) conducted a survey of 133 firms, of which 76 had less than 10 workers, in various industries in Ghana in the early 1990s.They found that only 10 percent of startup firms in Ghana could obtain bank loans but medium size enterprises and older firms are provided with credit three times more often than their smaller counterparts. The similar survey was conducted by Levy (1993) in Sri Lanka and Tanzania and reported that 80 percent of firms with 16 or more workers and with 6 or more years in operation are able to access bank loans, compared to the success rate of around 55 percent in the case of smaller firms with 6-15 employees of similar age, and less than 10 percent for firms with 5 or fewer workers, regardless of age.

2.3.2 FIRM SIZE AND ACCESS TO CREDIT

Firm size is one of the most important variables in literature related to access to credit. This was true for both developed as well as developing countries. Numerous studies have discussed that small and medium enterprises are financially more constrained than large firms. For example, Calomiris & Hubbard (1990) noted that when the company is smaller, the restrictions on credit is greater. Previous studies have mentioned several reasons for small firms to have less access to credit. Firstly, the small firms face with information opacity such as unable to provide financial information (Binks & Ennew, 1996). When the firm is small, most of the time it is owned and operated by the entrepreneur and there is no such legal requirement to regularly report financial information and many firms do not maintain audited financial accounts.

In addition, smaller firms have lesser assets to offer as collateral. In order to reduce the anticipated risk and moral hazard associated with lending, the banks use collateral as one of the instruments. The collateral is an assurance to the bank in case of default and it also ensures the borrowers commitment to the loan repayments. Berger and Udell (1995) found smaller and younger firms are more likely to face higher cost of financing and they are required to offer collateral.

For smaller firms, there is high risk involved because small firms have high failure rate compared to large firms. For example, Schiffer and Weder (2001) sampled firms across a number of countries and found that there was a negative relationship between the size of a business and the risk it might pose for a lender. In contrast, Lopez- Gracia and Aybar Arias (2000) came up with a different explanation stating that the smaller firms may themselves limit their financial structure with the aim of avoiding the need to share control of the business with others.

2.3.3 OWNERSHIP TYPE AND ACCESS TO CREDIT

Entrepreneurs choose ownership structures in large part to ensure adequate financing and because of the selection effect whereby finance goes to firms with conducive ownership structure (Pandula, 2011). Ownership structures in the firms can influence the ability to have access to finance. For example, previous research has found that listed firms and foreign owned firms face lesser financial constraints (Beck et al, 2006). Storey (1994), found that legal status influence the bank lending. He further states that corporate status at start up appears to be associated with a greater likelihood of bank lending.

2.3.4 INDUSTRY SECTOR AND ACCESS TO CREDIT

Industry sector also can be stated as a factor affecting access to finance. The lending banks may show preference for industry sectors that are growing (Pandula, 2011). Some industries are more likely to depend on external financing than others, depending upon project scale, and cash flows (Pandula, 2011). Firms in certain sectors will require more credit to invest in equipment, machinery, buildings, labour and raw materials than firms in other industry sectors. For instance, the industries with more capital requirements may face proportionately greater constraints (Kumar & Francisco, 2005).

Silva and Carreira (2010) argue that, for most services, the main input is human and not physical capital and therefore service sector firms find it hard to use this physical capital as collateral when resorting to external finance. Previous research has also found that the survival rates of small businesses vary between sectors (Storey & Wynarczyk, 1996).

2.3.5 LOCATION AND ACCESS TO CREDIT

According to Pandula (2011), it can be argued that spatial variations exist in both the cost and availability of finance, especially for small firms. There are a variety of factors which may contribute to spatial variations in the availability of bank finance for small firms in rural areas. Firstly, there may be an absence of financial institutions in these rural areas. Sometimes, there may be a single bank branch available to the location, which may enjoy a monopoly power in the area, and small firms may not have much financing alternatives available. Due to this, they may end up paying high interest on bank loans or may have to adhere to restricted covenants such as collateral and other conditions (Pandula, 2011).

Secondly, the bank branch managers assigned in these rural bank branches may have limited delegation of authority. As a result, there may be delays in approving loans requested by rural firms or high amount of loan rejections, as the bank loans are processed and approved by the head office officials who have no personal knowledge of customers or projects based in rural locations.

Thirdly, banks may be reluctant to lend to small firms located in rural areas, as the assets offered as collateral by these firms may have less market value, and in case of default, they may find it difficult to realize these assets (Pandula, 2011).

However, the previous studies done in this topic have contradictory views. Keeble (1990) investigated the constraints to growth experienced by urban and rural firms in the UK and suggest that the problems facing firms in urban and rural areas are broadly similar except finance. They reported that the only significant difference is that rural firms feel themselves more constrained in terms of finance compared to the urban firms. O'Farrell (1990) suggests on the basis of research in Nova Scotia, Canada that banks appear to be more reluctant to lend to small firms in rural areas, because if the firm fails, the bank considers that it will be more difficult to sell the assets. Kumar & Francisco (2005), also found that there is a large variation in branch density across different regions in Brazil and argued that well branched regions in Brazil would be expected to ease physical access and also lower information asymmetry problems as a consequence of greater ratios of banks per firm and they argued that the firms located in these regions have easy access to credit.

However, Perry (1988) found no clear evidence that small firms in a rural region of New Zealand are disadvantaged in the search for debt finance. Tucker and Lean (2001) also examined the relationship between firm location and success in obtaining external finance, by dividing the firms into two groups, the first containing firms located in the north of England and the second containing firms in the south, found that no significant variations exist, although there is some indication that firms in the south of England are more successful in obtaining term loans guaranteed under the Small Business Loan Guarantee Scheme.

However, a difference of opinion was found by (Rand, 2007).According to him, probability of accessing credit is higher in rural than in urban areas. He further states that "most of government bank credit is allocated towards rural areas confirming that local governments often are distinctly protective of firms in rural areas, which are more oriented towards serving local markets and therefore tend to escape from some of the credit barriers inherent in larger, possibly more outward oriented markets (Rand, 2007, p.10). Another contradictory argument of some researchers is that the distance between lenders and borrowers has no influence on financing small businesses is the development of new.

2.3.6 HAVING AUDITED FINANCIAL STATEMENTS AND ACCESS TO BANK CREDIT

Bass & Schrooten (2005) concluded that the lack of reliable information leads to comparably high interest rates even if a long term relationship between borrower and bank exists. In a situation like this, having audited financial statements play a major role.

In a study by Tagoe, *Anuwa-Amarh* and *Nyarko (2008),* the relationship between information management practices of small and medium size enterprises (SMEs) and their access to bank finance was examined. Data were collected with a researcher-administered questionnaire and analyzed using non-parametric correlation tests. It was found that SMEs that keep records and present certain types of information improve their access to bank finance.

Audited financial statements are very useful in accessing credit from financial institutions. Often, banks require audited financial statements before granting credit. For example, Berry et al (1993) found that lenders in the UK pay much attention to accounting information in order to deal with the loan applications of small firms. Given the reduced information risk arising from audited financial statements, potential lending institutions may offer low interest rates as well. In other words, audited financial statements improve borrower’s credibility and therefore reduce risk for lenders.

However, most of the SMEs in the South Asia have difficulty in getting credit from the formal financial institutions because they lack proper financial records. Most of the businesses in these countries often keep multiple sets of books and do not have audited financial statements based on reliable accounting standards. On the other hand, these firms end up getting loans at higher interest rates because banks considered them as high risk borrowers. According to the discussion above, it is clear that when an SME is audited by an external organization, this indicates that its financial status is healthier than those not audited.

Most SMEs evolve in the informal sector and are therefore not in a position to give banks the minimum information they generally require (contact details, legal documents, financial statements…). In addition, for SMEs evolving in the formal sector, the absence of accounting standards – or, on the contrary, the excessive level of accounting information required by the Organization for the Harmonization of Business Law in Africa (OHADA) standards in the case of West and Central Africa – as well as the lack of independent, competent and credible accounting firms, have an impact on the quality of financial information transmitted to banks (Kauffmann, 2005; IMF, 2006). Moreover, it may be in the interest of entrepreneurs to disseminate extremely limited or even erroneous information in order to evade taxes. Finally, there is usually no tools that would allow banks to learn about the payment behaviours of their new clients. Credit bureaus either do not exist or are ineffective. In this context, informal communication between banks and entrepreneurs must make up for this deficiency in classic communication channels.

2.3.7 ASSET TANGIBILITY

Previous researchers suggest that bank financing will depend upon whether the lending can be secured by collateral (Storey, 1994; Berger and Udell, 1998). Johnsen and McMahon

(2005) also stated that other factors held constant, firms with more intangible assets need to borrow less, compared with firms with more tangible assets, because of collateral factor.

SMEs have fewer acceptable collateral assets than large firms. This may partly relate to the stage of growth the firm belongs to. In the earlier stages of the firm, it may have lower retained profits which may hinder them to purchase fixed assets compared to the larger firms which has a longer history. Another reason for small firms to have a smaller proportion of fixed assets is the capital constraints faced by them. Because of the need to raise large amounts of capital, it finds difficult for them to acquire a large number of fixed assets. Hence a positive association between an acceptable collateral assets and having access to credit can be expected.

2.3.8 FIRM PERFORMANCE AND ACCESS TO CREDIT

Although it is difficult to construct the measures for firm performance in the SME sector, many studies have attempted to do this and found that greater sales and profits are associated with greater access to credit (Topalova, 2004). In addition, firms with increasing sales and increasing sales turnover ratios would be expected to have less credit constraints (Pandula, 2011).

2.3.9 EDUCATIONAL BACKGROUND OF ENTREPRENEUR AND ACCESS TO CREDIT

Past research found a positive relationship between higher educational qualifications and business growth (Kozan, Oksoy, & Ozsoy, 2006). Education affects entrepreneurs' motivation (Smallbone & Wyer, 2000). Furthermore, education helps to enhance the exploratory skills, improves communication abilities and foresight (Dobbs & Hamilton, 2007).These enhanced skills are positively related to present a plausible case for a loan to a banker at the time of preparing a loan proposal and then convincing the banker during the client interview.

Previous research, in particular has explored how managerial education affects the access to credit. For example, Kumar & Fransico (2005), found a strong education effect in explaining access to financial services in Brazil.

The study of 600 SMEs in Britain, France and West Germany (Watkins and Morton, 1982) interviewed the participants from the financial institutions as part of their main study and found that they were much less concerned about the difficulty in compliance with new laws and regulations and much more concerned with the managerial capability of the owner, which was given first rank in France, and second rank in Britain and West Germany.

In contrast, Han (2008) found that entrepreneurs with undergraduate degrees are more likely to be financially constrained than those without formal education background. Han (2008) believes the reason to be that better educated entrepreneurs normally own and manage large businesses which are more likely to be constrained by finance.

The other opposing argument is that educated individuals are more likely to discard the traditional concept of a loan as risky, and thus would have a higher probability to borrow from formal financial institutions.

It can be also assumed that educated entrepreneurs are likely to have better managerial skills and are better equipped to go through difficult administrative procedures in the credit system, increasing their standing in lenders eyes.

2.3.10 ENTREPRENEUR'S EXPERIENCE AND ACCESS TO CREDIT

Previous researchers have found positive relationships between previous management experience and business growth (Dahlquist, Davidsson, & Wiklund, 1999). Furthermore, Storey (1994) explained this was due to the desire of owner managers to exceed the wage level they sacrificed in becoming self-employed. Dobbs and Hamilton (2007) emphasized the positive effect of past experience on small business growth by proposing that owner-managers with previous experience are more likely to avoid costly mistakes than those with no prior experience.

In another study by Okurut, Olalekan, & Mangadi, (2009), they investigated the factors that influence the credit rationing behaviour of banks towards SMEs using 2007 Informal Sector

Survey data collected by Central Statistics Office and supplemented by our survey of SMEs from the major cities/towns in Botswana on the demand side, and key informant discussions with the banks on the supply side. Heckman Probit Model with sample selection was used to estimate the determinants of the probability of SMEs being credit rationed by banks. The study findings suggest that the experience of SMEs reduces their probability of being credit rationed by banks. From the bank perspective the experience of SMEs is determined from their ability to keep proper financial statements, the performance of their bank accounts with the banks, and their ability to make profits. From the SMEs perspective, there is need for banks to improve their efficiency in terms of reduction of loan processing time and cost of borrowing (i.e. interest rate). This will improve access to bank credit by the SMEs and promote their growth thereby stimulating economic diversification, employment creation opportunities, increased household incomes.

2.3.11 NETWORKING AND ACCESS TO CREDIT

Previous researchers have emphasized that networks can be used as the solutions to overcome the problems of access to limited resources and markets. For example, Curran et al (1993) argue that networks help to provide advice, information and capital to small firms. Applying this idea in the context of banking, it can be also argued that, having associated with a professional, trade or social associations such as Chambers of Commerce, Clubs and Societies may also lead to having access to bank loans. For example, some associations like Chamber of Commerce conduct seminars, workshops and industry visits to develop various skills and knowledge of the members. At times, the workshops are conducted on preparing project proposals for banks and managing finances in the business. In some occasions, one prominent and established member in an association may introduce another member to his or local bank managers and loan officers, and that referral may be used as a best screening method for the bank loan officers to get some idea of the character of the borrower. Further, the members of these associations are also been given information on various credit schemes available in the banks etc. There could be instances where one members act as a guarantor for another member at the time of obtaining a loan from a bank.

Talavera, Xiong and Xiong (2010) investigated the impact of social capital on financial obstacles faced by entrepreneurs using a pooled data of about 270 small companies. This is the only study we have found in the literature which investigated this issue. The researchers concluded that membership in business associations increase the probability of having a loan by 14.8 percent.

Levitt & March (1988) have acknowledged that networking sometimes called external relations, of firms among industry, trade associations and other forms of association create learning by facilitating the sharing of knowledge, providing a means for organizations to learn from the experience of others in the industry. It is therefore clear that small business owner managers use networking to obtain key information, learning opportunities and problems and to gain access to, or enhance understanding of sources of finance. Thus, it is logical to assume that businesses with networks are more likely to have easy access to bank credit compared to those who do not have such networks.

Banks' over cautiousness towards SMEs can be explained by several factors: the volume effect which leads to high unit costs, the risks on these counterparties, banks' lack of long-term resources, information asymmetry between entrepreneurs and bankers, (Lefilleur, 2008). While most of the other obstacles are structural to SSA markets and may therefore be difficult to overcome, risks stemming from information asymmetry and securitization difficulties could be minimized by the development of financial systems that are more adapted to local environments. Several factors, that are specific to the SSA context, are at the root of this information asymmetry between entrepreneurs and bankers.

2.3.12 SME LENDING CRITERIA

According to studies by Beck, Demirguc-Kunt and Martínez Pería (2009), while the financial assessment is the most important approval criterion across countries, a firm's credit history and owner characteristics are important in developing countries, while loan size is the second important criterion in developed countries. For small business lending, 50% of banks in developed countries and 49% of banks in the developing countries indicate that the financial assessment of the business is the most important criteria (Beck, Demirguc-Kunt & Martínez Pería, 2009). Banks in developing countries, a film's credit history with the bank is considered the second most important criteria, followed by the firm's owner characteristics and collateral. Although the collateral is not a decisive criterion for lending, in developing country banks, about 87% of banks require it for lending.

CHAPTER THREE

METHODOLOGY

3.1 RESEARCH DESIGN

In this chapter, an overview of the analytical framework of the study is discussed. This study primarily seeks to determine the major determinants of SME financing by banks and Non-Bank Financial Institutions in Ghana. It compares the lending criteria of selected banks to those of Non-Bank Financial Institutions in the Tema Metropolis.

The research design and methodology adopted for the data collection, including the questionnaire administered during the study are all discussed in this chapter. The chapter forms the basis for the data analyses and interpretation of findings from the study in the successive chapters of this study

3.2 SOURCES OF DATA

The data used for the study is a primary data obtained through structured interviews .The population of the study comprised ten Commercial Banks and five Non-Bank Financial Institutions (NBFIs) in Ghana. More specifically, the study concentrated on commercial banks and NBFIs in Tema Metropolis. Tema was chosen for the study due to the existence of an ample number of financial institutions providing each bank with an equal opportunity of been represented and also due to the limited nature of time and resources available to the researcher.

Secondary data was collected from the banks in relation to their policy regarding SME financing and criteria for assessment of loans. This provided the researcher with information from the perspective of the loan agents. To obtain information to determine the determinants of SME financing in Ghana, the study used a self-completion questionnaire that had close questions to gather primary data. The questions were straightforward and easy to answer. Bryman and Bell (2003) indicate that closed questions have some merits as they are easy to process, enhance comparability of answers and facilitate the demonstration of the relationship among variables.

The questionnaire comprised two parts. The first part focused on individual characteristics with questions on respondents gender and age. The second part consisted of all the ten determinants of SME financing identified in the literature. Several items on each construct were developed and adapted from relevant literature. All of the items were measured using a five-point Likert-type scale anchored at 5 for strongly agree and 1 for strongly disagree respectively.

3.3 SAMPLING AND SAMPLING TECHNIQUES

All Banks and Non-Bank financial institutions in the Tema Metropolis were used for the study based on a population of 24 banks and 56 Non-Bank Financial Institutions in Ghana (a total of 80). It would have been prudent to use over 40-55% to account for non-response (Salkind, 1997). However, in this case where all the institutions in the study are used there was no need to use a sampling technique. In the case of identifying the determinants of SME financing in Ghana, 200 questionnaires were administered based on a simple random sampling of SME entrepreneurs within the Tema Metropolis.

3.4 PROCEDURE

Research techniques are step-by-step procedures which you can follow in order to gather data, and analyze them for the information they contain (Jankowicz, 2000). Credit Officers, Credit Managers and Relationship Managers within the various financial institutions were provided by the management of the respective banks. The purpose of the study was explained to them and they responded appropriately to the questions posed. Ten to fifteen minutes each was allocated to each interview. They were assured of the confidentiality of the information they were going to provide and were assured that it will not affect their employment status in the organisation nor the organisation in any way. Also, they were assured that the information they provided was to be used for research purposes and the information was not going to be disclosed to a third party without their consent and their response was going to be treated as a unit during the analysis. The study also used questionnaires to collect primary data from SME owners in connection with the ascertaining the determinants of SME financing in Ghana.

3.5 DATA ANALYSIS

The field data was processed to allow for analysis. All of the items under each of the 10 constructs were measured by using a five-point Likert-type response scale, assigning numerals to question responses with 5 coded for strongly agree, 4 for agree, 3 for neutral, 2 for disagree and 1 for strongly disagree. Responses for demographic questions were also coded.

The response categories in Likert scales have a rank order and therefore could be referred as ordinal because ordinal scale of measurement is one that conveys order (Jamieson, 2004).

There are many tools and techniques appropriate for analyzing ordinal data. In this study, the research chose the software SPSS for Windows to do analysis.

CHAPTER FOUR

RESULTS AND DISCUSSION

4.0 INTRODUCTION

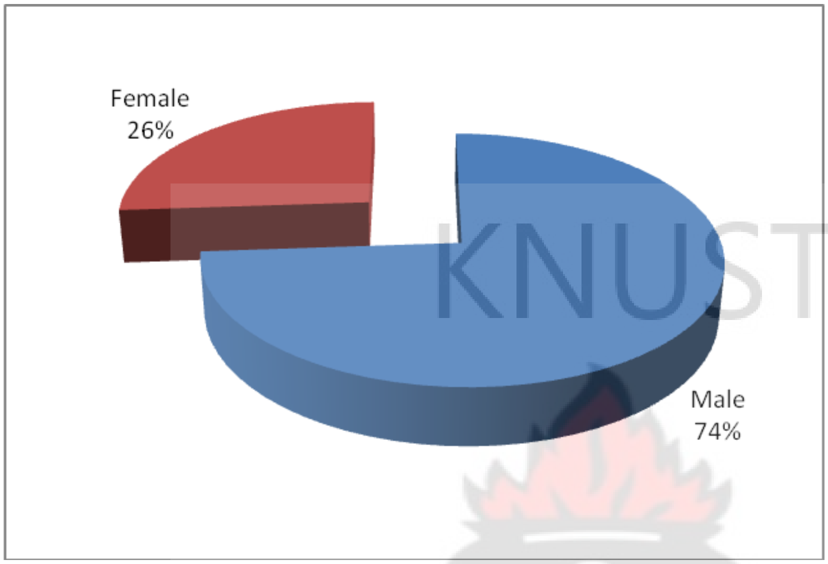
The chapter presents the data gathered from the field and the result of data analysis performed on the data. It also discusses the result obtained relating it to literature that exist in the area, and recommendation are made to industry players based on the findings. Included on the list of information and data generated are frequency tables representing the distribution of responses to each of the questions contained in the research questionnaire.

4.1 ANALYSES OF STRUCTURED INTERVIEW

The following are analysis of data obtained from fifteen respondents from 10 banks and 5 Non-Bank Financial Institutions following the interviews. Figure 1 shows the summary of the gender composition of the employees from the banking and non-banking financial institution who took part in the study.

4.1.1 SUMMARY OF GENDER OF THE RESPONDENTS

Fig 1: Summary of Gender of the respondents

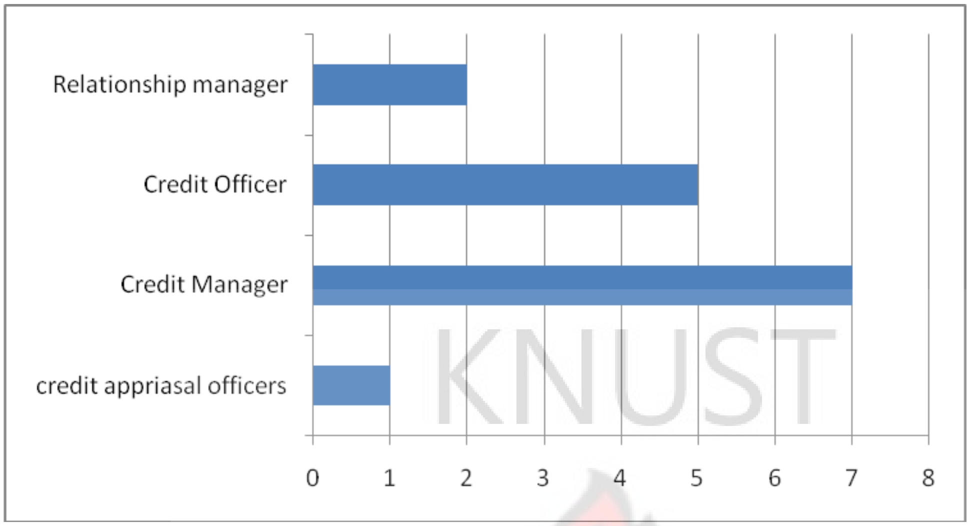


The majority, (74%) of the respondents, were males whilst 26% of the respondents were females, details are shown in figure 1.

4.1.2 RESPONDENTS' POSITIONS IN ORGANIZATIONS

Figure 2 illustrates the positions held by the respondents who were interviewed at their respective institutions.

Fig. 2: Summary of respondents positions in Organisation

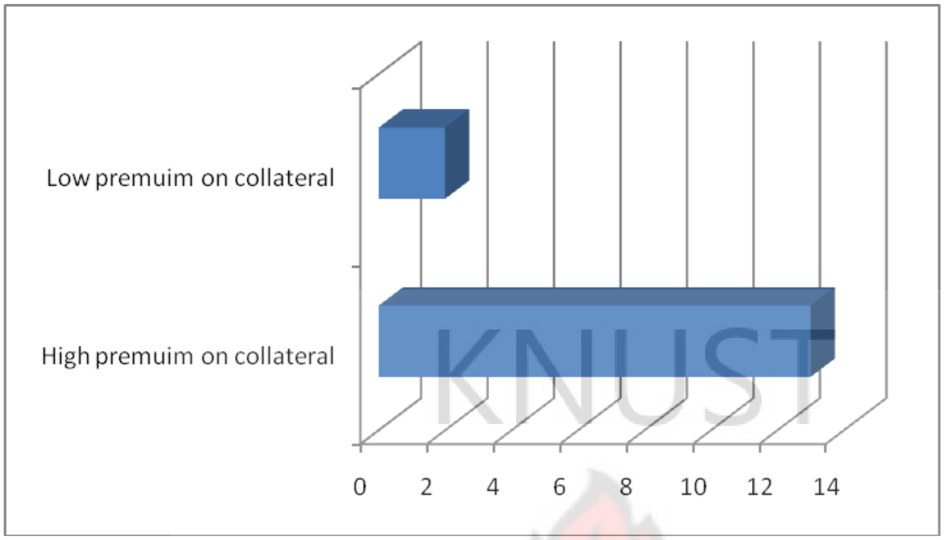


Majority (48%) of the respondents were credit managers in their various institutions, 35% of the respondents were credit officers whilst 13% were relationship managers and 4% was a credit appraisal officer, details are shown in figure 2.

4.1.3 PREMIUM PLACED ON COLLATERAL BY FINANCIAL INSTITUTIONS

Figure 3 contains summary of approval or other wise of cost of SME loan without collateral and the calculating of the interest rates.

Fig. 3: Premium placed on collateral by financial institutions



The interviewer wanted to know the importance of collateral to advancing credit to SMEs. Thirteen out of the fifteen institution require collateral as a prime requirement to offer credit while only two are willing to do without it

4.1.4: PREMIUM PLACED ON AUDITED ACCOUNTS

Interestingly the interview indicates that only five out of the fifteen institutions required audited accounts to grant credit to SME's. As many as many as Ten do not require audited accounts to have access to credit .Among this Ten are all the Five non-bank financial institutions.

Fig 4: Premium placed on Audited Accounts

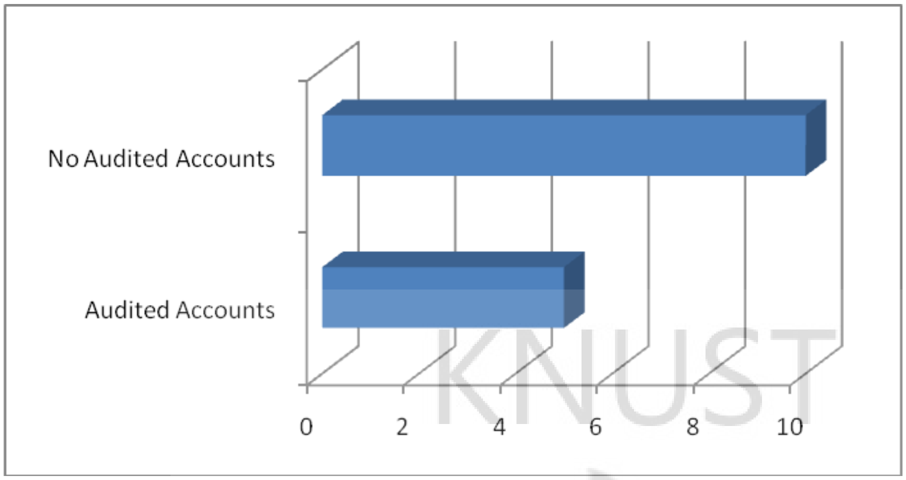


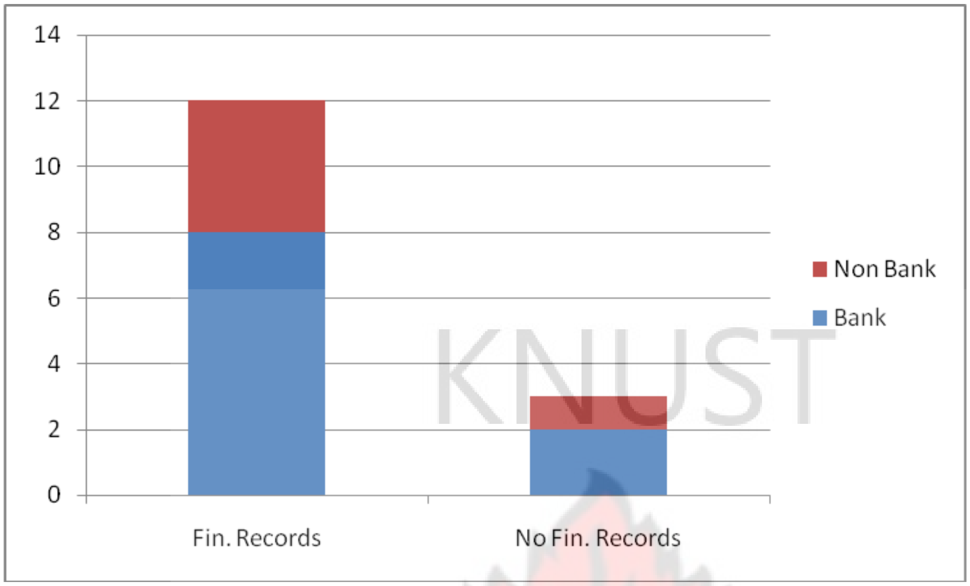
Table 1: indicates the importance financial institutions place on audited accounts of SMEs as a requirement for access to credit.

Table 1: Premium placed on Audited Accounts

	Frequency	Percent
Yes	5	33
No	10	67
Total	15	100.0

Table 1: shows the summary of the extent to which the respondents who were comfortable dealing with SMES that kept financial records.

Fig. 5: premium placed on financial records.



4.1.5 PREMIUM ON FINANCIAL RECORDS

Eight of the ten banks request for financial report as a requisite to access to credit. Similarly for the five non-bank financial institution also require financial record as a criterion for giving credit. Financial records in this study are defined to include bank statement, accounts operations and tax documents.

4.2 COMPARATIVE ANALYSIS

4.2.1: LOAN ELIGIBILITY CRITERIA OF BANKS.

Table 2: Summary of loan eligibility criteria by banks

No.	Eligibility criteria	Frequency	Percent
1	Collateral security	8	80.0%
2	Not less than six months account operation	9	90.0%
3	Audited account where applicable	5	50.0%
4	Bank statements	3	30.0%
5	Registered business and its documents.	1	10.0%

Table 2: presents data on loan eligibility requirements that was obtained from 10 banks. Out of the 10 banks 8 (representing 80%) listed collateral security as a requirement to qualify SMEs for loan. 9 banks (representing 90%) indicated that they would require customer's operation of banks account for not less than six month. 5 banks (representing 50%) listed an audited accounts as part of their eligibility criteria. 3 banks (representing 30%) also included the SMEs bank statements as a criterion., registered business and its documents, previous credit history and recommendation by the risk manager were each listed as criterion for loan eligibility by 4 different banks, and constitute 10% each.

Table 3: Summary of loan eligibility criteria by non-bank financial institutions

No.	Eligibility criteria	Frequency	Percent
1	Collateral security	5	100.0%
2	Audited account where applicable	0	0%
3	Registered business and its documents	5	100.0%
4	Guarantor	5	100.0%
5	Tax documents	1	20%
6	Age of business existence	1	20%
7	Six months bank statement	3	60.0%

Table 3 presents data on loan eligibility requirements that was obtained from five Non-Bank Financial Institutions (NBFIs). All five banks (representing 100%) listed collateral security, registered business and its document, and guarantor as requirement to qualify SMEs for a loan. 1 bank (representing 20%) indicated that they would require tax documents of the business. 3 banks (representing 60%) listed six months bank statement as part of their eligibility criteria. Audited account, bank statements were each listed as criteria for loan eligibility by two institutions, and constitutes 20% each.

4.3 SME DEFINITIONS OF BANKS IN GHANA

The definition of SME's in Ghana is not fixed based on information obtained from the financial institutions. (Mensah 2004; Kayanula and Quartey , 2000) SME definition is characterized by variations according to firm size, number of employee, firm annual turnover and value of fixed assets. In a working paper of the United Nations International Development organization (UNIDO), Mensah (2004) also defined SME's based on annual turnover. However, Mensah classifies SME's into three categories; Micro enterprise, Small enterprise and Medium enterprises. It is significant to observe that Mensah (2004) also uses number of employees to define SME's.

Table 4.3.1: Definition of SMEs using turnover by 15 banks in Ghana

Amount (GH¢)	**Frequency**	**Percent**
1 to 1,000,000	6	40.0%
1,000,001 to 2,000,000	1	6.7%
2,000,001 to 3,000,000	1	6.7%
3,000,001 to 4,000,000	0	0.0%
4,000,001 to 5,000,000	1	6.7%
5,000,001 to 6,000,000	6	40.0%

Table 4.3.1 presents information on how 15 banks in Ghana define SME using annual turnover. From the table, 6 banks (representing 40%) categories loan clients with annual turnover between GH¢1 to GH¢1,000,000 as SMEs. 1 bank (representing 6.7%) defines loans clients as SMEs if their annual turnover fall within GH¢1,000,001 to GH¢2,000,000. Only 1 bank (representing 6.7%) considers clients with annual turnover ranging between GH¢2,000,001 and 3,000,000 as SMEs. 1 bank (representing 6.7%) considers clients with annual turnover ranging between GH¢4,000,001 to GH¢5,000,000 as SMEs while 6 banks (representing 40%) also consider loan clients with annual turnover between GH¢5,000,001 to

GH¢6,000,000. The financial institutions that provided the definitions may have done so based on skewed business interactions they have had with either small or medium enterprises. Therefore, banks that interact more with small enterprises in their SME lending operations may have provided the definition of SMEs skewed towards small enterprises while banks that interact more with medium scale enterprises may have given a definition of SMEs skewed towards medium enterprises.

4.4 ANALYSES OF PRIMARY DATA (DETERMINANTS)

4.4.1 DEMOGRAPHIC CHARACTERISTICS

A total of 206 responses were received, 19 were detected to be incomplete or with errors. Correct and defect free responses summed up to 187 and formed the basis for this analysis.

4.4.1.1 GENDER ANALYSIS

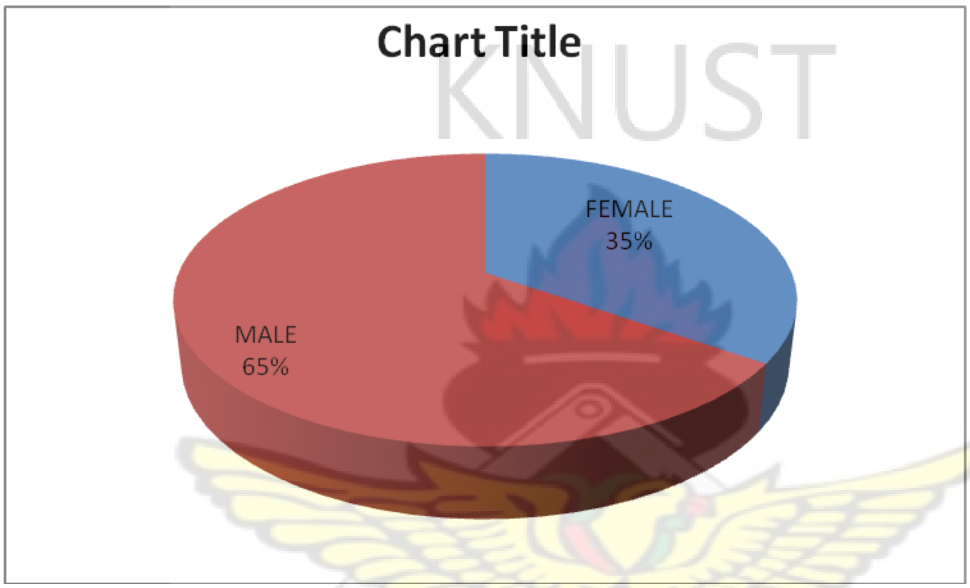
Frequency statistics carried out on gender showed that majority of the 187 respondents were male, 122 giving 65% of the total, while female respondents were 65 giving 35% (See figure 1 and table 1 below).

Table .1: Frequency Distribution Table - Respondent by Gender

Gender	**Frequency**
MALE	122
FEMALE	65
Total	**187**

Source: Field data 2012

Figure 1: Frequency Distribution of Responses by Gender

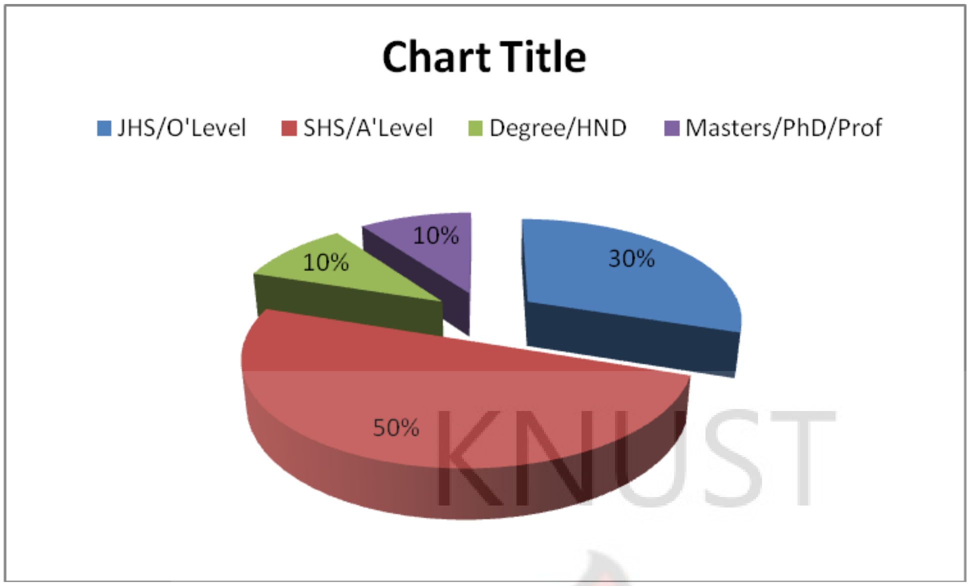


Source: Field data 2012

4.4.1.2 Level of Education

Out of the 187 respondents who completed questionnaires, 50% were Senior High School Leavers/Advance Level holders; 30% had completed Junior High School/ Ordinary Level while 10% had completed their Masters and Degrees respectively.

Figure 2 Frequency Distribution of level of Education



Source: Field Data 2012

According to the frequency distribution of the level of education, the majority of firm owners (50%) only had education up to the Senior High Level and Advanced Level. This demonstrates the trend in most developing economies where people who are highly educated are mostly found in the civil and public services rather than in the SME sector. It is observed that a substantial percentage (30%) have Ordinary Level or have completed Junior High School. This can be explained in terms of the need to make a living as one is unable to get higher education.

4.5 RESULTS AND DISCUSSIONS FOR DETERMINANTS OF SME FINANCING.

4.5.1 DESCRIPTIVE STATISTICS

The median as a measure of central tendency was extensively for analysis to provide an organized and summarized view for the field data. It was used to determine the single value that identifies the center of the distribution and best represents the entire set of data for each construct. The median was used because it serves as a valuable alternative to the mean especially for ordinal data. Methodological and statistical texts are clear that for ordinal data one should employ the median or mode as the measure of central tendency (Jamieson, 2004). This is because, comparatively, the arithmetical manipulations required in calculating the mean (and standard deviation) are inappropriate for ordinal data where the numbers generally represent verbal statements (ibid). As argued by Kuzon Jr et al. (1996), the average of fair and good is not fair-and-a half; this is true even when one assigns integers to represent fair and good. Median is appropriate for ordinal scale because it's defined by direction and ordered sequence as in ordinal scale. Other descriptive statistics that may be used to describe Ordinal data include frequencies or percentages of response (Jamieson, 2004).

Regarding the analysis of this study, the median for each construct per observation was computed. This provided a single value or score for each construct per observation as proposed by Bryman and Bell (2003). The median score matrix defined per observation per construct was developed to give a summarized view showing responses per respondent. The complete median score matrix showing responses for all 187 observations was fed into SPSS software for further computation and analysis including frequency distribution .

Table 1: Reliability Coefficient and Descriptive Statistics for Ten Constructs on Determinants SME Financing

	Age of business	Firm size	Owner-ship Type	Locat-ion of Firm	Audited A/C	Asset tangibility	Firm Perfor-mance	Educational Background	Entrepreneurial Experience.	Network
Valid Number of Respondents	187	187	187	187	187	187	187	187	187	187
Mean	3.9	4.0	4.0	2.6	3.5	4.0	3.9	2.6	3.6	2.6
Median	4	4	4	4	4	4	4	4	4	4
Std. Deviation	1.00	1.11	1.11	0.97	1.25	1.11	1.00	0.97	1.98	0.97
Cronbach's Alpha	0.8327	0.9333	0.9333	0.7852	0.896	0.9333	0.9623	0.5262	0.823	0.7852

Source: Field data 2012

Table 1 above presents the overall scores of the median, mean, standard deviation and Cronbach's Alpha for each construct. The reliability coefficients (Cronbach's Alpha values) for each of the five constructs were all above the threshold of 0.7 and this demonstrated that all question items under each construct had an acceptable level of internal relation and combined to give a single measure for their respective constructs. On a five-point Likert scale, the mean mark for firm size, asset tangibility and ownership type for all 187 respondents was 4. This indicates that respondents' perception about the importance placed on the three determinants as a basis for granting loans is quite high. It was also observed that the mean mark for other determinants such as age of business, firm performance, and entrepreneur experience were 3.9, 3.9, and 3.6 respectively. This implied that though these determinants were not very important as compared to the determinants which scored 4.0, they were still necessary factors which influenced the access to credit by SMEs. Furthermore, though the empirical literature discussed ten determinants of SME financing, only three were found to be significant in the case of the SMEs located in the Tema Metropolis.

CHAPTER FIVE

SUMMARY OF FINDINGS, CONCLUSION AND RECOMMENDATIONS

5.0 INTRODUCTION

This section of the study summarizes the findings and draws conclusion, upon which recommendations were made.

5.1 Determinants of SME financing in Ghana

The results indicate that out of the ten determinants discussed in the literature, only three are significant to SME financing in the Tema Metropolis. These three include firm size, ownership type and asset tangibility which score a mean of 4.0 on the Likert-scale. Closely related to these three in significance are firm performance, age of business and entrepreneur experience, which score a mean of 3.9, 3.9 and 3.6 respectively.

5.2 LOAN ELIGIBILITY CRITERIA BY BANKS

The results in the study indicate that the following were listed as SME Loan eligibility criteria by banks in Ghana: collateral security; Customer's operation of bank's account; audited account; SME's bank statement; Registered business and its documents, and Recommendation by the risk manager.

A comparison before the SME Loan eligibility criteria for banks in Ghana shows that the most important criteria is "collateral security". This is followed by "Customer's operation of bank's account. This is also followed by the following, whiles share the same level of importance: "An audited account"; "SMEs bank statement". The next level of importance was shared by the following: "Registered business and its documents"; and "Recommendation by the risk manager".

The findings in this study are partially consistent with findings in previous studies, such as Beck, Demirguc-Kunt and Martínez Pería (2009).

5.2.2 LOAN ELIGIBILITY CRITERIA BY NON-BANK FINANCIAL INSTITUTIONS

The results in the study also indicate that the following were listed as the SME Loan eligibility criteria by non-bank financial institutions: Collateral security; Registered business and its documents; Guarantor; Six months bank statement; Tax documents; and Age of business existence

Overall, the following were ranked the most important lending criteria: Collateral security; Registered business and its documents; and Guarantor. These were followed by bank statement", which was the second most important lending criteria for non-banking financial institutions.

5.2.3 COMPARISON OF LOAN ELIGIBILITY CRITERIA OF BANKS AND NON-BANK FINANCE INSTITUTIONS.

5.2.3.1 LOAN ELIGIBILITY CRITERIA OF FINANCIAL INSTITUTIONS

Putting the banking and non-bank financial institutions together, the most important criterion was "collateral security". The other common criteria, although having different relative levels of importance, were "audited account"; "Registered business and its documents"; and profit of financial. In this study, financial records include bank statements, Tax document and credit history as well as account operation".

5.2.4 DEFINITION OF SMES USING TURNOVER BY 15 FINANCIAL INSTITUTIONS IN GHANA

The findings in this study indicate two main definitions for SMEs based on turnover: annual turnover between GH¢1 to GH¢1,000,000; and annual turnover between GH¢5,000,001 to

GH¢6,000,000. The huge gap between these definitions could be due to the gap between the two extreme ends of SMEs: the small enterprises and medium enterprises. In other words, the first range of GH¢1 to GH¢1,000,000 could be referring to small enterprises, while the second range of GH¢5,000,001 to GH¢6,000,000 could be referring to the medium enterprises.

5.3 CONCLUSIONS

The findings in this study have implications for practical applications in the financial industry. Firstly, the findings provide valuable information on what banking and non-bank financial institutions consider as important in their decision to lend money to SMEs. Knowledge of this information can provide SMEs with a broad check list of criteria that has to be satisfied in order to be considered for funding by the financial institutions in Ghana.

In addition, with the findings in the current study, financial institutions can have a sense of the general situation of lending criteria in the financial industry. This has the potential of providing a basis for analyzing competition in the SME lending industry and an opportunity for company policy reviews aimed at providing a competitive edge.

5.3 RECOMMENDATIONS

The current study could be extended in future studies by assessing and investigating how effective the various lending criteria serve to help financial institutions make sound SME lending decisions in Ghana. Also, future studies can investigate what peculiar SME characteristics are good predictors of an SME that would be able to successfully manage funds given to them.

Considering the fact that only three out of the ten determinants for SME financing were significant in the case of SMEs in the Tema Metropolis, it is recommended that the firms should take a close look at other determinants such as firm performance, entrepreneur experience and audited accounts in order to increase their chances of securing credit in future.

In light of the challenges related to the granting of credit by bank and NBFI based on credit criterion, it is recommended that an SME credit bureau should be established. This is because the SME credit bureau will access loan eligibility criteria of SME using other requirements apart from the main six mentioned earlier in the study. Secondly it is recommended the Bank of Ghana provide a comprehensive definition of SMEs.

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APPENDIX

APPENDIX 1

‘Determinants of SME financing by Financial Institutions’.

Interview Guide.

1. Gender
2. Title of interview
3. Availability of products for SMEs.
4. Definition of SMEs.
5. Criteria for lending to SMEs
6. Purpose for each criterion (confirmatory question to criteria)
7. Type of financial institution.
8. Any other comment

APPENDIX 2

Questionnaire

'Determinants of SME financing by Financial Institutions'.

This questionnaire is designed to know your determinants of SME financing. *This survey is part of my master's degree thesis, and your kind support is crucial for the successful completion of this research project. Your responses will be anonymous; data will be combined and analyzed as a whole. Please attempt to answer all the questions and check* ***one*** *appropriate box that best suits your perspective for* ***each*** *statement.*

Your participation in the study will be greatly appreciated. Thank you very much for your time and assistance.

Section A

1. Name of Organisation ---

2. Gender Male [ ] Female [ ]

3. Age ---

4. Educational level --

5. Position ---

Section B

There is a positive relationship between:

1. A ge of the firm and access to credit.
   [ ] strongly agree [ ] agree [ ] neutral [ ] disagree [ ] strongly disagree

2. Firm size and access to credit
   [ ] strongly agree [ ] agree [ ] neutral [ ] disagree [ ] strongly disagree

3. Ownership type and access to credit

[ ] strongly agree [ ] agree [ ] neutral [ ] disagree [ ] strongly disagree

4. Location of business and access to credit

[ ] strongly agree [ ] agree [ ] neutral [ ] disagree [ ] strongly disagree

5. Having audited financial statements and access to bank credit

[ ] strongly agree [ ] agree [ ] neutral [ ] disagree [ ] strongly disagree

6. Asset Tangibility and access to credit

[ ] strongly agree [ ] agree [ ] neutral [ ] disagree [ ] strongly disagree

7. Firm performance and access to credit

[ ] strongly agree [ ] agree [ ] neutral [ ] disagree [ ] strongly disagree

8. Education background of entrepreneur and access to credit

[ ] strongly agree [ ] agree [ ] neutral [ ] disagree [ ] strongly disagree

9. Entrepreneur's experience and access to credit

[ ] strongly agree [ ] agree [ ] neutral [ ] disagree [ ] strongly disagree

10. Networking and access to credit

[ ] strongly agree [ ] agree [ ] neutral [ ] disagree [ ] strongly disagree