

**THE IMPACT OF FINANCIAL STRUCTURE ON FINANCIAL SUSTAINABILITY  
OF SMALL AND MEDIUM SIZED ENTERPRISES IN MUKONO TOWN**

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**S21B12/117**

**A DISSERTATION PROPOSAL SUBMITTED TO THE SCHOOL OF BUSINESS IN PARTIAL  
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**DECLARATION**

I, Byarugaba Godfrey Leon declare that this work is my original work and that I have not copied or plagiarized any material from any other source. All sources that have been used in this have been properly cited.

I further declare that I have completed all the work required for this report independently and have not received any assistance from any other person except for the guidance from my research supervisor.

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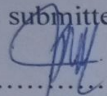
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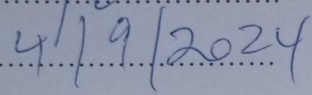
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**APPROVAL**

I confirm Byarugaba Godfrey Leon conducted research with my guidance. This research report has been submitted under my endorsement as a supervisor of student's research.

Sign.....

Date.....

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## ABSTRACT

Financial structure refers to a mix of debt and equity that a company uses to finance its operations whereas financial sustainability refers a business's ability to consistently have enough reserves to cover unexpected expenses without relying on borrowing or compromising essential services. This study aimed at to find out the impact of financial structure on financial sustainability of SMEs in mukono town. The objectives of the study were, To examine the impact of short-term debt levels on financial sustainability of small and medium sized enterprises, to assess the relationship between long-term debt levels and financial sustainability of small and medium sized enterprises and to examine the influence of equity on financial sustainability of small and medium sized enterprises. The sample size of the study was about 60 SMEs and the following were discovered the following, a significant majority 90% find equity financing preferable to debt financing, with 28%. While 46% of respondents acknowledge that equity investors bring valuable expertise, a notable 38% weren't too sure. In terms of financial risk, 60% believe equity financing helps reduce it, though 20% disagree. Finally, 42% of respondents feel that equity investors demand significant control over business operations, with 32% expressing neutrality and a small minority 24% were not agreeing. A majority 64% agree that their business has experienced revenue growth over the past three years, with 22% strongly agreeing. Some of the conclusions included Short-term Debt, while its essential for daily operations and liquidity management, short-term debt is a double sided, it provides necessary funding but also poses significant risks to financial sustainability of SMEs in mukono town, long-term debt has been beneficial for business expansion and stability, but its associated costs and risks prove to be challenging to SMEs, making it a less favorable option for some businesses, equity financing is preferred by SMEs as it reduces financial risk. However, the potential for loss of control due to the involvement of equity investors is a notable drawback and some of the recommendations included,short-term Debt Management, SMEs in mukono should carefully assess their reliance on short-term debt, balancing the need for liquidity with the associated risks and Implementing strict financial management practices can help mitigate these risks and the long-term Debt Strategy, SMEs in mukono should consider long-term debt for business expansion and stability but should be cautious of the costs involved. It is recommended that businesses negotiate favorable terms and conditions to minimize the financial burden.

## CHAPTER ONE

### 1.1 Introduction

This chapter consists of the background study, problem statement, purpose of study, objectives of study, research questions.

### 1.2 Background of study

Small and Medium-sized Enterprises (SMEs) are fundamental to economic growth and development worldwide, acting as significant contributors to employment, innovation, and wealth creation (Beck & Demirguc-Kunt, 2006). However, their financial sustainability is often precarious, due to inherent vulnerabilities such as limited resources, market volatility, and susceptibility to economic shocks (Berger & Udell, 1998). A crucial determinant of SME sustainability is their financial structure, which refers to the mix of debt and equity financing used to fund their operations and growth (Degryse et al., 2012).

The relationship between financial structure and firm performance has been a long-standing subject of inquiry in corporate finance literature. The Modigliani-Miller theorem (1958), a cornerstone of financial theory, posits that in a perfect market, a firm's value is independent of its capital structure. However, subsequent research has challenged this view, highlighting the role of factors such as taxes, bankruptcy costs, agency conflicts, and information asymmetry in influencing the optimal capital structure (Myers, 1984).

In the context of SMEs, the pecking order theory (Myers & Majluf, 1984) has been particularly influential. It suggests that SMEs prefer internal financing over external debt and equity due to information asymmetry concerns, leading to a hierarchical preference for funding sources. However, recent empirical evidence suggests that SMEs may not strictly adhere to this pecking order, and their financing decisions are influenced by a multitude of factors, including industry characteristics, macroeconomic conditions, and firm-specific attributes (Fatoki & Asah, 2022).

Recent studies have explored the impact of various financial structure choices on SME performance and survival. For instance, research by Demsetz & Lehn (2019) indicates that higher leverage ratios may increase financial distress risk for SMEs, while Bessler, Drobetz, & Grüninger (2021) suggest that equity financing can enhance firm growth and innovation.

However, the findings are not always consistent, and the optimal financial structure for SMEs may vary depending on their specific context and objectives.

Despite the growing body of research, a comprehensive understanding of the complex relationship between financial structure and SME sustainability remains elusive. This study aims to address this gap by examining how different financial structure choices influence SME financial performance and resilience. In doing so, it seeks to provide valuable insights for SME owners, managers, policymakers, and financial institutions on how to design and implement effective financial strategies that can foster SME growth and sustainability.

### **1.3 Statement of the problem.**

Small and Medium-sized Enterprises (SMEs) are critical drivers of economic growth, innovation, and employment worldwide. However, their financial sustainability remains a pressing concern due to the complex interplay of various factors, including their financial structure. A growing body of research suggests that the composition and configuration of a firm's financial resources – the mix of debt and equity financing, short-term and long-term capital, internal and external funds – can significantly influence its ability to generate profits, manage risks, and adapt to changing economic conditions. Despite this recognition, a comprehensive understanding of how specific financial structure choices impact SME sustainability remains elusive, particularly in the context of rapidly evolving financial markets and regulatory landscapes.

Recent studies, such as those by Demsetz & Lehn (2019) and Bessler, Drobetz, & Grüninger (2021), have highlighted the importance of financial structure decisions for firm performance and survival, but their focus has primarily been on larger corporations. Research specifically addressing the unique challenges and opportunities faced by SMEs in this regard is still limited. Moreover, existing studies often rely on traditional financial theories and models that may not fully capture the nuances of SME financial behavior. For instance, the pecking order theory (Myers, 1984) suggests that SMEs prefer internal financing over external debt and equity due to information asymmetry concerns. However, recent empirical evidence (e.g., Fatoki & Asah, 2022) suggests that SMEs may also strategically utilize a combination of financing sources to optimize their capital structure and enhance their sustainability.

In this context, the dissertation will aim to investigate the complex relationship between financial structure and financial sustainability of SMEs, drawing on both theoretical frameworks and empirical evidence. The study will examine how different financial structure choices, such as leverage levels, debt maturity, and equity ownership affect SME profitability, liquidity, solvency, and growth potential.

#### **1.4 Purpose of the Study**

The research purpose of this study is to investigate the link between financial structure and sustainability of SMEs. Since SMEs are crucial in the economy, most of them face long-term sustainability challenges because of inadequate capital and sensitivity to environmental changes. There is a gap in the literature that this study intends to address through investigating the effects of leverage, debt maturity, and equity ownership decisions on SMEs' profitability, liquidity, solvency, and growth. In this context, the study aims at comparing and contrasting various theoretical models and empirical findings in order to define the most suitable financial arrangements that may support the enhancement of SME resilience and sustainability. The results will contribute to the scholarly knowledge and provide guidance on how to create relevant policies and procedures to promote SMEs' finance. Besides, the findings of the study will be valuable for preparing SME owners and managers for making well-grounded financial decisions and enhancing the stability of the enterprises.

##### **1.4.2 Research objectives**

- i. To examine the impact of short-term debt levels on financial sustainability of small and medium sized enterprises.
- ii. To assess the relationship between long-term debt levels and financial sustainability of small and medium sized enterprises.
- iii. To examine the influence of equity on financial sustainability of small and medium sized enterprises.

### **1.4.3 Research Questions**

- i. To examine the impact of short-term debt levels on financial sustainability of small and medium sized enterprises.
- ii. To assess the relationship between long-term debt levels and financial sustainability of small and medium sized enterprises.
- iii. To examine the influence of equity on financial sustainability of small and medium sized enterprises.

### **1.5 Scope of the study**

The study will be guided by the content subject scope, geographical scope and time scope as follows;

#### **1.5.1. Content scope**

This study is concentrated on an in depth analysis of the relationship between financial structures and the financial sustainability of small and medium sized enterprises. The scope covers the different short term debt levels, long term debt levels and equity.

#### **1.5.2. Geographical scope**

The intended areas from which the research is to be carried out is mukono town, various businesses within the town shall be visited.

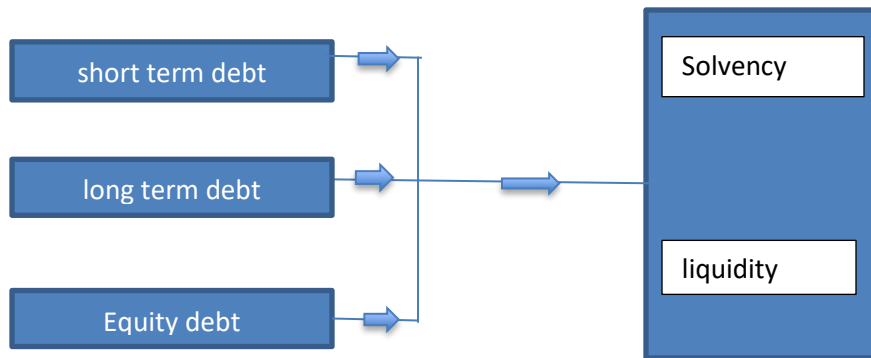
#### **1.5.3. Time scope**

The scope of this research will encompass data and information collected over the past five years, ensuring that the analysis reflects the most current trends and any developments that may be relevant to the study.

## 1.6 Conceptual framework

Financial Structure

Financial sustainability



Source: Constructed by the researcher

Figure 1.1: Conceptual Framework

## **CHAPTER TWO**

### **LITERATURE REVIEW**

#### **2.0 INTRODUCTION**

Small and Medium-sized Enterprises (SMEs) play a crucial role in economic growth, employment, and innovation. However, their financial sustainability is often challenged by various factors, including their financial structure. This literature review explores the relationship between financial structure, specifically debt levels and debt-equity mix, and the financial sustainability of SMEs. It delves into theoretical underpinnings, empirical findings, and identifies research gaps to inform the specific objectives of this study.

#### **2.1 THEORETICAL REVIEW**

This will involve reviewing literature that had been put forward by other scholars regarding financial structure and financial structure.

##### **2.1.1 Pecking Order Theory**

This theory posits that SMEs prefer internal financing (retained earnings) over external financing due to information asymmetry and transaction costs (Myers & Majluf, 1984). When external financing is needed, they prefer debt over equity because debt signals less risk to investors. However, excessive reliance on debt can increase financial risk and jeopardize sustainability.

##### **2.1.2 Trade-off Theory**

The Trade-off Theory, introduced by Kraus and Litzenberger (1973), suggests that SMEs aim to achieve an optimal capital structure that balances the tax benefits of debt with the costs of financial distress. According to this theory, debt financing offers tax advantages because interest payments are tax-deductible, which can enhance profitability. However, the increased use of debt also raises the risk of bankruptcy, as higher debt levels lead to greater financial obligations. SMEs must, therefore, carefully weigh the benefits of the tax shield against the potential costs of financial distress. This theory implies that there is an optimal debt-equity ratio where the marginal benefit of the tax shield equals the marginal cost of financial distress, thereby maximizing the firm's value and financial sustainability..

## **2.2 EMPIRICAL REVIEW**

### **2.2.1 The Impact of Short-Term Debt Levels on Financial Sustainability of SMEs.**

Short-term debt, with its quick access and flexibility, is a common financing tool for SMEs, especially for managing working capital needs and covering temporary cash flow gaps. This includes trade credit from suppliers, bank overdrafts, and short-term loans. However, while short-term debt offers immediate liquidity, it also poses risks to the financial sustainability of SMEs due to its inherent volatility and higher interest rates compared to long-term debt.

Empirical evidence on the impact of short-term debt on SME financial sustainability is mixed. Some studies suggest a positive relationship, as short-term debt can provide the necessary funds for growth and operational needs (Kyarikunda, 2018). It can also be less costly than long-term debt due to lower information asymmetry and monitoring costs (Petersen & Rajan, 1994). However, excessive reliance on short-term debt can lead to several issues:

**Liquidity Risk**, short-term debt matures quickly, requiring frequent refinancing, which can be challenging during economic downturns or credit crunches. This can expose SMEs to liquidity risk and increase their vulnerability to financial distress (García-Teruel & Martínez-Solano, 2007).

**Higher Interest Rates**, short-term debt often carries higher interest rates than long-term debt, increasing the financial burden on SMEs and reducing their profitability.

**Volatility**, short-term debt is more sensitive to interest rate fluctuations, leading to increased volatility in financing costs and cash flows, which can negatively impact financial sustainability (Ebaid, 2013).

Therefore, while short-term debt can be a valuable financing tool for SMEs, it is essential to manage it prudently. Excessive reliance on short-term debt can lead to a debt trap, where SMEs struggle to repay maturing debt and are forced to take on more debt, leading to a vicious cycle of financial instability. This objective seeks to identify the optimal level of short-term debt that maximizes its benefits while minimizing its risks, considering factors such as firm size, industry, and macroeconomic conditions.

### **2.2.2 The relationship between long-term debt levels on financial sustainability of SMEs.**

Long-term debt, including bank loans and bonds, is often essential for SMEs to finance growth-oriented investments, such as purchasing equipment, expanding facilities, or developing new products. While long-term debt can provide a critical source of capital, excessive reliance on it can pose significant risks to an SME's financial sustainability.

Several studies have examined the relationship between long-term debt levels and various measures of SME financial sustainability. Some research suggests that moderate levels of long-term debt can positively impact SME performance due to the tax shield effect and the disciplining effect on management (Sogorb-Mira, 2005). However, beyond a certain threshold, high long-term debt levels can lead to solvency risk and financial distress (Hall et al., 2004).

Empirical evidence on this relationship is mixed. Some studies have found a negative correlation between long-term debt and SME profitability (Michaelas et al., 1999), suggesting that high interest payments and principal repayments can burden a company's financial resources and hinder its ability to generate profits. Other studies have reported a positive association between long-term debt and SME growth, indicating that access to long-term financing can enable SMEs to invest in growth opportunities and expand their operations (Bhaird & Lucey, 2010).

However, the impact of long-term debt on SME financial sustainability is not uniform across all firms. Firm-specific factors, such as size, age, industry, and ownership structure, can moderate this relationship (Psillaki & Daskalakis, 2009). Additionally, macroeconomic conditions, such as interest rates and economic growth, can also influence the effect of long-term debt on SME financial health (Esperança et al., 2003).

Therefore, understanding the optimal level of long-term debt for SME financial sustainability requires considering various factors, including the specific context of the SME and the prevailing economic environment.

### **2.2.3 To examine the influence of equity on financial sustainability of small and medium sized enterprises.**

In emerging markets such as Mukono equity plays a critical role in the financial sustainability of Small and Medium-Sized Enterprises (SMEs). The money raised through the sale of common or preferred stock is referred to as equity financing since it signifies ownership in the company. Knowing the different ways that equity affects SMEs ability to maintain a stable financial position is essential.

Access to Capital, giving people access to capital is one important way that equity affects the long-term viability of the financial system. In contrast to debt financing which requires regular repayments equity financing allows SMEs to raise substantial amounts of capital. Due to their strict credit requirements and lack of collateral SMEs frequently struggle to obtain traditional bank loans for this reason this type of financing is essential.

SMEs that rely on equity financing according to Beck and Demirguc-Kunt (2006) are in a better position to invest in long-term projects and innovation improving their chances of growth and financial sustainability. In addition to risk mitigation equity financing is a major factor in risk reduction. In contrast to debt equity does not have set payback dates which can strain cash flows especially in times of economic recession or poor business performance. Myers (2001) highlights that equity can function as a safeguard against economic hardship offering solace during difficult periods and guaranteeing the companys existence and longevity.

Ownership and control however presents a unique set of difficulties in equity funding. The diluting of ownership and control is one of the main issues. When outside equity investors are involved control and decision-making authority are frequently shared which can be a big disadvantage for the original owners who are afraid of losing control over how the company is run. However, these investors may also provide worthwhile networks experience and strategic insights that enhance the firms sustainability (Berger and Udell 1998).

Long-Term View, the goals of SMEs for sustainable growth are well-aligned with the long-term perspective that most equity investors possess. Because these investors are more patient and willing to wait for their returns the company can focus on strategic initiatives rather than short-term financial performance. Because it encourages investment in innovation market expansion

and capacity building this long-term focus is essential to the sustainable growth of SMEs (Paul et al. (2007)).

### **2.3 Summary of Literature Review and Research Gaps**

A vast number of studies have been made regarding the effect of the financial structure on the financial sustainability of SMEs and the conclusion are still ambiguous. Therefore, there is evidence of a positive association between debt financing and SME performance in some case while in others there is negative association or no association at all. From this it can be inferred that the effect of debt on the aspect of financial sustainability for SMEs depends on several factors including the following: The kind of debt taken, the amount of debt taken, and on the SME firm itself.

Most of the previous studies have been conducted in developed economies, and few studies addressed the issue of developing countries, which ignore the problems and circumstances of SMEs in these countries.

Minimal attention to informal financing; the involvement of informal financing for instance from the family and friends into the SMEs financial sustainability.

Insufficiency of context-specific research, context-specific research or even more longitudinal studies are necessary to investigate the impacts of financial structure choices on the sustainability of the SMEs in the long run.

Insufficiency of the existing theories for mapping the combinations and connections to SME financial structure and sustainability may be the reason for limited applicability of more comprehensive theoretical frameworks.

Making sure Such gaps can be useful in enhancing knowledge on how SMEs can manage their financial structures to attain sustainable financial management in the future.

## **CHAPTER THREE**

### **METHODOLOGY**

#### **3.0 Introduction**

This chapter aims at looking the methods that can be used while collecting data from the relevant respondents within the SMEs in the organizations that were chosen. The methods used will determine how valid and reliable the data will be in relation to the topic of study , that is the impact of financial structure on the financial sustainability of SMEs within the organization.

#### **3.1 Research Design**

A research design is a guide or a strategy for carrying out research according to Kothari (2004). It describes the approaches and techniques used to obtain pertinent data and information evaluate that data and come to dependable and legitimate conclusions. A research design that combined qualitative and quantitative methodologies was used in this study and design aligned with its objectives and facilitates an in-depth examination of the impact of short term debt levels and long-term debt debt levels on the financial sustainability of small and medium-sized enterprises in Mukono Town.

#### **3.2 Study Population**

The target population of the study comprises of a portion of SMEs located within Mukono Town. The sampling size consisted of 62 SMEs. Given the the level of difficulty in surveying the entire population due to time and cost constraints, a sample was selected. The data collected from was from the chosen people in their respective companies.

#### **3.3 Sampling Technique**

The target population was divided into subgroups according to a set of characteristics and an equal number of participants were chosen from each subgroup. This method of sample selection is known as stratified sampling. According to Kothari (2004) and Saunders Lewis and Thornhill (2016) stratified sampling is known to increase the samples representativeness and the studys findings generalizability.

#### **3.4 Sample Size Determination**

Using Yamane's formula for sample size calculation the sample size was calculated, which is given by:

$$n = \frac{N}{1 + N(e)^2}$$

$$N = \frac{60}{1 + 60(0.05)^2}$$

$$n = 52$$

Where:

- N= Study population (60 SMEs)
- n = Sample size
- e = Margin of error 0.05 will be considered for a 95% confidence level

Category	Study population		Sample size
Wholesale Shop	10	$10 * 52 / 60$	9
Healthcare Clinic	9	$9 * 52 / 60$	8
Restaurant	11	$11 * 52 / 60$	9
Salon	9	$9 * 52 / 60$	8
Retail store	10	$10 * 52 / 60$	9
Other SMEs	11	$11 * 52 / 60$	9

### 3.5 Data Collection Methods

A mix of both quantitative and qualitative methods were required to carry out the research, Qualitative and quantitative data collection methods were used and this approach provided an-in-depth look into the research topic, the primary data collection tool was a questionnaire which was used to gather the relevant information relevant to the research Topic.

### **3.5.1 Questionnaire Survey Method**

Questionnaires were distributed to all respondents, who were managers, co-owners, employees and supervisors of SMEs. The questionnaire that were presented to the respondents with a set of closely defined choices for recording their answers were intended for data collection. This structured approach helped to standardize the responses, making it easier for quantification and analysis.

### **3.6 Data Sources**

The research collected both primary and secondary data. Primary data was obtained through questionnaires to capture the current situation and perceptions of respondents. Secondary data was sourced from previous research findings and the district SME database. The primary data helped to answer specific questions designed to capture issues not available from secondary information.

### **3.7 Data Collection Instrument**

#### **3.7.1 Self-Administered Questionnaires**

A targeted approach involved the distribution of 80 questionnaires to individuals engaged within the chosen SMEs. The questionnaire method facilitated precise data collection, ensuring that respondents' input aligned coherently with the research's logical sequence. The standardized questionnaire employed a five-point Likert scale ranging from 1 (Strongly Disagree) to 5 (Strongly Agree), allowing respondents to express their opinions on a structured scale.

### **3.8 Validity and Reliability**

#### **3.8.1 Reliability**

Amin (2005) defined reliability as the dependability or trustworthiness in context of a measuring the instrument. It is the degree to which the instrument consistently measures what it is measuring. In order to ascertain reliability, instruments will be tested in a pilot run in Mukono district in the month of July, 2024. The results from pilot test in Mukono district will be used to measure reliability of the study instruments. The CRONBACH formula will be used:

$$\alpha = \frac{K}{K-1} \left( 1 - \frac{\sum SD^2 i}{SD^2 t} \right)$$

Where:  $\alpha$  = Alpha is Reliability co-efficient. K = Number of items included.

$\sum SD^2_i$  = Sum of variance of individual items.  $SD^2_t$  = variance of all items.

When the reliability co-efficient is equal to 0.83 which is more than the standard minimum of 0.7, then the researcher will go on to use the instruments. The test for reliability will be conducted in a pilot run in Mukono district.

### **3.8.2 Validity**

The consistency of the results with their apparent causes is what determines a study's validity and significance (Saunders et al. 2009). This means making certain that the study's participants are chosen to accurately reflect the intended audience. In context the study focused on individuals within the SMEs enabling a true and genuine comprehension of the topic at hand. Using a descriptive case study design allowed for an even greater improvement in validity. thorough examination of the study setting enhancing abilities in data evaluation and consolidating knowledge

### **3.9 Data Management and Analysis Plan**

Data analysis is a crucial in attaining information that would make meaning from collected data. This section presents the analytical methods and tools used to analyze the data and come up with conclusions regarding the impact of financial structure on the financial sustainability of SMEs. Quantitative data was analyzed using Stata statistical software and MS Excel.

### **3.10 Measurement of Variables**

In order to ensure that the study's key variables are operationalized for efficient analysis this section outlines the measurement techniques used. Market share and revenue growth are included in the dependent variable Financial Sustainability. . On a Likert scale ranging from 1 (Low) to 5 (High) respondents rated these dimensions. A Likert scale was also used to measure the independent variables; this therefore was used a compile the necessary information that could be used during analysis of the data obtained from the respondents.

### **3.11 Ethical Consideration**

One of the key elements of research are Ethical considerations, The ethical concerns in relation to the study are considered within this section, consent from participants was mandatory within the data collection process because this would guarantee confidentiality and anonymity of data, and adhering to ethical guidelines and regulations, the study involved letting the participants know prior before disclosing any information that its would be keep safe and anonymous , no personal data was collected from the respondents , only information relevant to the topic of study.

### **3.12 Conclusion**

A detailed methodology for examining the impact of financial structure on the financial sustainability of SMEs in Mukono Town has been included within this chapter. This chapter contains the data collection methods, ethical concerns, validity and reliability of the information.

## **CHAPTER FOUR**

### **PRESENTATION, ANALYSIS AND INTERPRETATION OF FINDINGS**

#### **4.0 Introduction**

In this chapter, data analysis , results and discussion are presented in line with objectives of the study .(1) To examine the impact of short-term debt levels on financial sustainability of small and medium sized enterprises.(2)To assess the relationship between long-term debt levels and financial sustainability of small and medium sized enterprises.(3)To examine the influence of equity on financial sustainability of small and medium sized enterprises.

#### **4.1 General characteristics of the respondents**

##### **4.1.1 Response Rate**

Detailed questionnaires were designed and issued to establish the impact of financial structure on financial sustainability of small and medium sized enterprises in Mukono.

**Table 4.1: Response Rate**

*Table 1. The response rate*

<b>Questionnaires administered</b>	<b>Sample size</b>	<b>Questionnaires issued</b>	<b>Questionnaires returned</b>	<b>Percentage</b>
<b>Restaurants</b>	9	10	8	88%
<b>Retail stores</b>	8	10	7	88%
<b>Whole sale shops</b>	9	10	9	100%
<b>Health care clinics</b>	8	10	9	100%
<b>Saloons</b>	9	10	8	100%
<b>others</b>	9	10	9	100%
<b>Total</b>	54	60	50	93%

**Source: Primary data**

According to table 4.1, there were 60 questionnaires issued to the respondents and 50 of those questionnaires were filled and returned by respondents where 88% percent were returned by restaurants, 88% were returned by retail stores and the responded with 100% response rate.

#### **4.1.2 Findings of the Demographic characteristics of Respondents**

*Table 2 Positons in SME Demographic Information*

<b>Demographic data</b>	<b>Description</b>	<b>Frequency</b>	<b>Percentage %</b>
<b>Position in the SME</b>	Owner	23	46.9%
	Manager	14	28.6%
	supervisor	5	10.2%
	Other Positions	8	14.3%

**Source: Primary data**

#### **4.1.3 Nature of business**

The different businesses within mukono town were taken into consideration while collecting data.

*Table 3 Nature of business Demographic Data.*

Demographic data	Description	Frequency	Percentage %
Nature of the business	Wholesale Shop	8	16%
	Healthcare Clinic	7	14%
	Restaurant	9	18%
	Salon	9	18%
	Retail store	8	16%
	Other	9	18%

**Source: Primary data**

The table above shows the percentage of the nature of the businesses visited while and the following data was obtained 16% was for wholesale shops, 14% for health care clinics , 18% for restaurants, 18% for saloons, 16% for retail stores and 18% for other SMEs.

#### **4.1.4 Employee demographic Data**

*Table 4 How many employees does the business have?*

Demographic data	Description	Frequency	Percentage %
How many employees does your business have	1-5	25	50%
	6-10	19	38%
	10-15	4	8%
	21-50	2	4%
	More than 50	0	0%

**Source: Primary data**

The table provides a demographic overview of the number of employees in businesses. Half of the businesses (50%) have between 1 to 5 employees, while 38% have 6 to 10 employees. A smaller portion, 8%, have 10 to 15 employees, and only 4% of businesses have 21 to 50 employees. None of the businesses reported having more than 50 employees. This indicates that the majority of the businesses surveyed are small, with a workforce primarily under 10 employees.

#### 4.1.5 The duration the business been in operation

*Table 5. How long the businesses have been in operation.*

Demographic data	Description	Frequency	Percentage %
How long has your business been in operation	Less than 1 year	6	12.5%
	1-3 years	15	31.3%
	4-6 years	18	37.5%
	7-10 years	7	14.6%
	More than 10 years	2	4.2%

**Source: Primary data**

The table above shows the 31.3% of business range between 1-3 years, 37.5% between 4-6 years, 12.5% less than one year, 7-10 years comprise about 14.6% and 4.2% are over 10 years, this indicates most business have a span between 4-6 years.

#### 4.2. Financial structure.

Financial structure refers to the type of financing that a business may preferable adopt. This aspect was measured using 8 items at a five point Likert scale ranging from 5 – strongly agree, 4 – agree, 3 – Not sure, 2 – disagree, and 1 –strongly disagree. The finding from the analysis are as presented in the table below

*Table 6. financial structure of the SMEs*

	SA		N		D	
	(F)	(%)	(F)	(%)	(F)	(%)
Our business primarily relies on personal savings for financing.	22	46%	19	14%	17	40%
We frequently use bank loans for our financing needs.	37	62%	8	16%	7	22%
Microfinance loans are a significant source of our business financing.	22	26%	25	20%	3	52%
We often rely on family and friends for financing our business.	29	50%	17	12%	4	34%
The proportion of our financing from short-term debt is high.	33	50%	14	18%	3	30%
The proportion of our financing from long-term debt is high.	26	44%	18	14%	8	40%
The proportion of our financing from equity is high.	20	40%	13	6%	19	52%

**Source: Primary Data**

The table on the financial structure of SMEs reveals that while personal savings and bank loans are common sources of financing, with 46% and 58% of respondents respectively agreeing or strongly agreeing to their use, there is considerable reliance on diverse sources. However,

microfinance loans are that significant for most SMEs, as 70% disagree or strongly disagree with using them. Family and friends are relied upon, with 46% agreeing, although 34% disagree. Opinions are split on short-term debt, with 26% agreeing and 30% disagreeing, and long-term debt is less favored, with 40% disagreeing. Equity financing is also not widely used, as 32% disagree with its significant use. This indicates that SMEs employ varied financing strategies, with no single method being overwhelmingly dominant.

#### 4.2.2 Perceptions of short term debt.

This aspect was measured using 8 items at a five point Likert scale ranging from 5 – strongly agree, 4 – agree, 3 – Not sure, 2 – disagree, and 1 –strongly disagree. The finding from the analysis are as presented in the table below

*Table 7. The extent to which the following statements regarding short-term debt are agreed with.*

	A		N		D	
	(F)	(%)	(F)	(%)	(F)	(%)
Short-term debt helps to manage daily operations effectively.	35	70%	3	6%	2	4%
Short-term debt has improved our business liquidity.	38	76%	9	18%	3	6%
The cost of short-term debt is manageable for our business.	27	54%	17	34%	6	12%
Short-term debt poses a significant risk to our financial sustainability.	38	76%	6	12%	6	12%

**Source: Primary Data**

A majority 70% agree that short-term debt helps manage daily operations effectively, though 6% disagree. Similarly, 76% believe it has improved their business liquidity, but 18% remain neutral, and 6% disagree. Regarding costs, 46% find short-term debt manageable, yet 34% disagree, indicating some concerns. Lastly, 76% agree, that short-term debt poses a significant risk to financial sustainability, reflecting a notable concern among SMEs.

### 4.2.3 Perceptions of long term debt.

Long term debt is a form of financing obtained through borrowing that typically exceeds 12 months. This aspect was measured using 8 items at a five point Likert scale ranging from 5 – strongly agree, 4 – agree, 3 – Not sure, 2 – disagree, and 1 –strongly disagree. The findings from the analysis are as presented in the table below

*Table 8. The extent to which the following statements regarding long-term debt are agreed with.*

	<b>A</b>		<b>N</b>		<b>D</b>	
	<b>(F)</b>	<b>(%)</b>	<b>(F)</b>	<b>(%)</b>	<b>(F)</b>	<b>(%)</b>
Long-term debt has facilitated business expansion.	34	68%	3	6%	10	20%
Long-term debt has improved our business stability.	31	62%	9	18%	11	22%
The cost of long-term debt is manageable for our business.	20	40%	17	34%	8	16%
Long-term debt poses a significant risk to our financial sustainability.	33	66%	6	12%	6	12%

**Source: Primary Data**

The table on long-term debt reveals that 68% of respondents believe it has facilitated business expansion, with 40% strongly agreeing. Additionally, 62% agree that long-term debt has improved their business stability, although 20% disagree. When it comes to the cost of long-term debt, 44% find it manageable, but an equal percentage remain neutral, indicating uncertainty or variability in their experiences. Lastly, 66% are concerned about the risks of long-term debt, with 22% strongly agreeing that it poses a significant threat to financial sustainability, suggesting cautiousness among SMEs in using long-term debt.

### 4.2.3 Perceptions of Equity

Equity refers to the sale of ownership of a business in return for capital. This aspect was measured using 8 items at a five point Likert scale ranging from 5 – strongly agree, 4 – agree, 3 – Not sure, 2 – disagree, and 1 –strongly disagree. The finding from the analysis are as presented in the table below

*Table 9. The extent to which the statements regarding Equity are agreed with.*

	SA		N		D	
	(F)	(%)	(F)	(%)	(F)	(%)
Equity financing is a preferable option compared to debt financing.	45	90%	3	6%	2	4%
Equity investors bring valuable expertise to our business.	23	46%	9	18%	8	16%
Equity financing helps in reducing financial risk for our business.	0	0%	17	34%	0	0%
Equity investors demand significant control over business operations.	30	60%	6	12%	10	20%

**Source: Primary Data**

The table presents the extent to which respondents agree with various statements regarding equity financing. A significant majority (90%) find equity financing preferable to debt financing, with 28% strongly agreeing and 62% agreeing. While 46% of respondents acknowledge that equity investors bring valuable expertise, a notable 38% remain neutral. In terms of financial risk, 60% believe equity financing helps reduce it, though 20% disagree. Finally, 42% of respondents feel that equity investors demand significant control over business operations, with 32% expressing neutrality and a small minority (24%) disagreeing.

#### 4.2.4 Financial sustainability.

Financial sustainability refers to the ability of a business to meet its obligations during the span of its operations. This aspect was measured using 8 items at a five point Likert scale ranging from 5 – strongly agree, 4 – agree, 3 – Not sure, 2 – disagree, and 1 –strongly disagree. The finding from the analysis are as presented in the table below

*Table 10. The extent to which the statements regarding long-term debt are agreed with.*

	SA		N		D	
	(F)	(%)	(F)	(%)	(F)	(%)
Our business has experienced revenue growth over the past three years.	32	64%	3	6%	7	14%
Our business maintains a positive cash flow.	19	38%	9	18%	12	24%
Our business has a stable market share.	12	24%	17	34%	18	36%
We have been able to reinvest profits into the business.	44	88%	6	12%	2	4%

**Source: Primary Data**

A majority (64%) agree that their business has experienced revenue growth over the past three years, with 22% strongly agreeing. However, there's less confidence in maintaining positive cash flow, as only 38% agree, and 38% are neutral. Stability in market share is less certain, with 40% disagreeing that their business has a stable market share, and only 24% agreeing. Notably, a significant 88% agree that they have been able to reinvest profits into the business, with 28% strongly agreeing.

### 4.3 Challenges and strategies.

These refer to the obstacles that may hinder a business from achieving its objectives

*Table 11. Major challenges businesses face in achieving financial sustainability?*

	Frequency	Percentage
Limited access to credit	18	36%
High interest rates	12	24%
Poor financial management	2	4%
Regulatory Issues	8	16%
Market competition	30	60%
Others	15	30%

**Source: Primary Data**

The table above indicates that about 60% of the businesses are faced with competition, 36% limited access to credit, 24% with high interest rates, 16% regulatory issues, 4% poor financial management and 30% comprise of other challenges.

### 4.4 Strategies employed to improve financial sustainability

*Table 12. Strategies that have been employed to improve business financial sustainability.*

	Frequency	Percentage
Cost cutting measures	26	52%
Diversification of products/services	16	32%
Improving financial management	24	48%
Seeking alternative financing	19	38%
Other	6	12%

**Source: Primary Data**

The table shows the percentage of strategies the various business has employed where 52% of the businesses have adopted cost cutting measures, 48% improving their financial management

practices, 38% seeking alternative financing options and 32% diversification of products/services and 12% choosing other ways to improve their financial sustainability.

## **4.5 CONCLUSION**

In this chapter, the findings from the study were presented in form of tables. The results were interpreted and discussed with the literature that was reviewed in chapter two of the study.

# **CHAPTER FIVE**

## **SUMMARY, CONCLUSION AND RECOMMENDATIONS**

### **5.0 INTRODUCTION**

This chapter presents a summary of findings observed and inferred from the data presented in chapter four. The summary of findings is based on the literature available in chapter two. This chapter also provides the conclusions, recommendations and suggested areas for further study

#### **5.1 Summary of Findings**

The study aimed to find out the relationship between short term debt, long term debt and equity and their influence on financial sustainability of businesses within mukono town. The study discovered that majority of the businesses rely on short and long term debt for their operational activities and expansion activities, it was also discovered that the form of debt has a strong impact on the financial sustainability of businesses.

##### **5.1.1 Impact of Short-term Debt on Financial Sustainability**

The findings indicated that majority of the businesses rely on short term debt as a way of financing their operations and meeting their short term obligations , it was also identified that the due to the nature of short term loans having a short maturity period and having high interest rates , it posed a threat to the financial sustainability of the businesses as a whole.

##### **5.1.2 Relationship Between Long-term Debt and Financial Sustainability**

The findings of the study show that long term debt is the preferred option when it comes to financing options due to the nature of how it structured , it long maturity period and lower interest rates prove to be a better option compared to short term debt though the manageability costs prove to be a challenge overtime, but when well managed long term debt becomes the

favorable financing option because it allows room for growth and expansion within the businesses within mukono.

### **5.1.3 Influence of Equity on Financial Sustainability**

The findings showed that equity financing would be the most preferable option because of the lessened risk exposure giving businesses room to raise capital and avoid the costs associated with debt, the major concern with equity financing was the fact most business owners didn't want to lose control of their businesses in the process of accepting capital from external investors.

## **5.2 Conclusions**

Short-term Debt may essential for daily operations and liquidity management but short-term debt is may either improve business or financially strain it and even though it provides necessary funding it poses significant risks to financial sustainability of SMEs in mukono town.

Long-term debt has multiple uses and some being business expansion and stability, but its associated costs and risks can prove to be challenging to SMEs in whatever industry, making it a less favorable option for some businesses.

Equity financing as an option may be preferred by SMEs as it reduces financial risk because the investors are only entitled to profits. However, the potential for loss of control due to the involvement of equity investors is a notable drawback.

## **5.1 Recommendations**

Short-term Debt Management implementation, SMEs in mukono should carefully review their reliance on short-term debt and determine whether its manageable, this can help them know what to prioritize first and meet the obligations due before they pose a problem to the buissness and threaten financial sustainability.

Long-term Debt Strategy, SMEs in mukono that have taken on long-term debt for business expansion and stability should keep in mind the risks associated with long term debt and should consider drawing up a plan that would be able to track and manage the debt costs associated with long term debt.

Equity Financing, while equity financing may be important in reducing financial risk, SMEs should consider potential loss of control and should establish clear terms and agreements in the

presence of a legal party with equity investors to maintain a balance between capital provision and operational control within the business.

Diversification of Financing Sources, to be able to enhance financial sustainability, SMEs should diversify their financing sources SMEs may now consider a mix of equity and debt this approach can help spread the risks reducing the exposure entirely to one form of financing and this provide a more stable financial structure.

Financial Management Training, It is recommended that SMEs invest in financial management training, this will therefore reduce the cost that the businesses incur due to poor financial management and this will put them in a position to financially sustain their business.

#### **5.4 Areas for Further Research**

Research areas that could looked at include finding out the influence of equity financing on financial sustainability of listed companies in the Ugandan stock exchange, additionally the long term effects of debt financing on financial sustainability of small and medium sized enterprises could also be considered as an area for further study. By looking at these there will be an in-depth understanding on the influence of financial structure and these studies may reveal other areas of concern that SMEs may have to address for survival within the marketplace.

#### **5.5 Conclusion**

Chapter five has is a comprehensive summary of the research findings and conclusions that have been drawn up based on the analysis on the collected data, recommendations have been suggested to improve the financial sustainability of SMEs in Mukono Town. The study contributes to the understanding of how different financial structures impact the sustainability of SMEs in Mukono and provides a starting point for further research in this area to be carried out. Further studies will reveal and identify any unidentified gaps.

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## **APPENDICES**

### Appendix I: Questionnaire

Questionnaire: The Impact of Financial Structure on the Financial Sustainability of SMEs in Mukono Town

Please you are kindly required to tick where necessary.

### Section A: Demographic Information

1. What is your position in the SME?

Owner

Manager

Supervisor

Other (Please specify): \_\_\_\_\_

2. **What is the nature of your business?**

Wholesale Shop

Healthcare Clinic

Restaurant

Salon

Other (Please specify): \_\_\_\_\_

3. **How long has your business been in operation?**

Less than 1 year

1-3 years

4-6 years

7-10 years

More than 10 years

4. **How many employees does your business have?**

1-5

6-10

11-20

21-50

More than 50

**Section B: Financial Structure**

5. To what extent do you agree with the following statements regarding short-term debt? (1 = Strongly Disagree, 5 = Strongly Agree)

Statement	Strongly Disagree (1)	Disagree(2)	Neutral (3)	Agree(4)	Strongly Agree (5)
Our business primarily relies on personal savings for financing.					
We frequently use bank loans for our financing needs.					
Microfinance loans are a significant source of our business financing.					
We often rely on family and friends for financing our business.					
The proportion of our financing from short-term debt is high.					
The proportion of our financing from long-term debt is high.					
The proportion of our financing from equity is high.					

**Section C: Perceptions of Short-term Debt**

6. To what extent do you agree with the following statements regarding short-term debt? (1 = Strongly Disagree, 5 = Strongly Agree)

Statement	Strongly Disagree (1)	Disagree(2)	Neutral (3)	Agree(4)	Strongly Agree (5)
Short-term debt helps to manage daily operations effectively.					
Short-term debt has improved our business liquidity.					
The cost of short-term debt is manageable for our business.					
Short-term debt poses a significant risk to our financial sustainability.					

**Section D: Perceptions of Long-term Debt**

**7. To what extent do you agree with the following statements regarding long-term debt? (1 = Strongly Disagree, 5 = Strongly Agree)**

Statement	Strongly Disagree (1)	Disagree(2)	Neutral (3)	Agree(4)	Strongly Agree (5)
Long-term debt has facilitated business expansion.					
Long-term debt has improved our business stability.					
The cost of long-term debt is manageable for our business.					

Long-term debt poses a significant risk to our financial sustainability.					
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**Section E: Perceptions of Equity**

8. To what extent do you agree with the following statements regarding debt-equity mix? (1 = Strongly Disagree, 5 = Strongly Agree)

Statement	Strongly Disagree (1)	Disagree(2)	Neutral (3)	Agree(4)	Strongly Agree (5)
Equity financing is a preferable option compared to debt financing.					
Equity investors bring valuable expertise to our business.					
Equity financing helps in reducing financial risk for our business.					
Equity investors demand significant control over business operations.					

**Section F: Financial Sustainability**

9. To what extent do you agree with the following statements regarding your business's financial sustainability? (1 = Strongly Disagree, 5 = Strongly Agree)

**Section G: Challenges and Strategies**

Statement	Strongly Disagree (1)	Disagree(2)	Neutral (3)	Agree(4)	Strongly Agree (5)
Our business has experienced revenue growth over the past three years.					
Our business maintains a positive cash flow.					
Our business has a stable market share.					
We have been able to reinvest profits into the business.					

**10. What are the major challenges your business faces in achieving financial sustainability? (Select all that apply)**

- Limited access to credit
- High-interest rates
- Poor financial management
- Market competition
- Regulatory issues
- Other (Please specify): \_\_\_\_\_

**11. What strategies have you employed to improve your business's financial sustainability? (Select all that apply)**

- Cost-cutting measures

Diversification of products/services

Improving financial management practices

Seeking alternative financing sources

Other (Please specify): \_\_\_\_\_

**Section H: Additional Insights**

12. Please provide any additional comments or suggestions regarding the financial structure and sustainability of SMEs in Mukono Town.

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**Thank you for your participation!**



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30<sup>th</sup> Aug, 2024

**TO WHOM IT MAY CONCERN**

Name: **BYARUGABA GODFERY LEON**

Reg. **S21B12/117**

A bachelor's student who is seeking permission from your office to collect data for his dissertation titled

**The Impact of Financial Structure on Financial Sustainability of Small and Medium Sized Enterprises in Mukono**

We shall be grateful if you could render assistance to him in collecting the necessary data for his dissertation

The Uganda Christian University School of Business thanks you in advance

.....  
Mukisa Simon Peter  
Research coordinator



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