

CREDIT ACCESSIBILITY AND FINANCIAL PERFORMANCE OF SMALL AND MEDIUM ENTERPRISES IN EASTERN DIVISION OF BUSIA MUNICIPALITY

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**UGANDA CHRISTIAN
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DECLARATION

I, Nekesa Morine, hereby declare that this research report titled “Credit accessibility and financial performance of small and medium enterprises in eastern division of busia municipality” is my original work; and to the best of my knowledge, it has not been published and/or submitted before to any University or Institution of higher learning for any academic award.

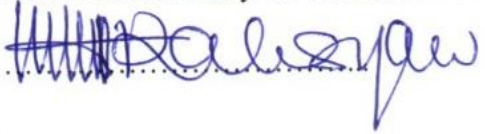
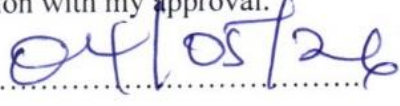
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APPROVAL

This is to certify that this titled "credit accessibility and financial performance of small and medium enterprises in eastern division of Busia municipality; has been done under my supervision and it is now ready for submission for examination with my approval.

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Supervisor

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DEDICATION

I dedicate this research work to my brother Omwero Robert with all my heart. This project is my small way of saying thank you for the support offered to me since childhood.

ACKNOWLEDGEMENT

First, I want to thank God sincerely. His love, strength, and guidance carried me through every late night, every moment of doubt, and every small victory along the way. Without Him, none of this would have been possible.

It is in a particular manner that I express my gratitude to my supervisor, Mr. AGUME ANTHONY KABISYAKI. Not only were you my supervisor but you were a true mentor who really cared about me. It is greatly appreciated that you had the patience to go through my drafts, giving me constructive criticism and encouraging me throughout the way.

ABSTRACT

The primary aim of the study was to determine the effect of access to credit on the financial performance of the small and medium enterprises operating in the Eastern Division of Busia. These factors included access to credit, conditions for credit and the interest rate involved.

These variables are correlated with financial performance measures such as profitability, return on investment and assets, sales, and job creation capabilities.

This research adopted the cross-sectional survey approach where surveys were done using questionnaires and interview guides. Questionnaires were used to collect information from 62 business owners/managers (of the targeted 70 businesses), whereas interviews were held with 12 loan officers from banks, micro finance companies and SACCOs.

The results from correlation showed positive relationships between performance and availability of credit ($r=0.445$), credit terms ($r=0.512$ – highest correlation) and interest rate ($r=0.468$). Regression analysis shows that the three credit factors explained 37.5% of variation in performance, with credit terms being the most significant variable ($\beta=0.348$).

In conclusion, credit availability does influence the performance of the SMEs in the border region; however, it is important to focus more on credit terms than mere presence of banks. This could be achieved by banks using different types of currency for lending, accepting movable securities like equities and machinery, allowing for longer grace period and being clear on the cost of credit. It is important for the government to start a credit guarantee scheme and help Kenya facilitate cross-border credit facilities. For the SMEs, it would be advisable to keep proper accounting records, legalize their businesses and learn about credit terms before borrowing.

TABLE OF CONTENTS

DECLARATION	ii
APPROVAL	iii
DEDICATION	iv
ACKNOWLEDGEMENT.....	v
ABSTRACT	vi
CHAPTER ONE	1
INTRODUCTION.....	1
1.0 Introduction	1
1.1 Background to the Study.....	1
1.2 Statement of the Problem.....	2
1.3 Purpose of the Study.....	3
1.4 Research Objectives	3
1.4.1 General Objective	3
1.4.2. Specific Objectives.....	3
1.5. Research Questions.....	4
1.6 Significance of the Study	4
1.7 Justification	4
1.8 Scope of the Study.....	4
1.8.1 Geographical Scope	4
1.8.2. Content Scope	4
1.8.3 Time Scope.....	5
1.8. Conceptual framework.....	5
Financial literacy	5
Credit guarantee schemes,	5
1.10 Operational Definitions of Key Terms.....	6

CHAPTER TWO	7
LITERATURE REVIEW	7
2.0 Introduction	7
2.1 Conceptual Review	7
2.1.1 SME financial Performance	7
2.1.2 Credit Accessibility.....	7
2.2 Theoretical Review	8
2.3 EMPIRICAL STUDIES.....	9
2.3.1 Credit Availability and SME financial Performance.....	9
2.3.2 Credit Terms and financial Performance of SME	10
2.3.3 Interest rate and financial Performance SME	13
2.4 Chapter Summary.....	15
CHAPTER THREE	16
RESEARCH METHODOLOGY	16
3.0 Introduction	16
3.1 Research Design	16
3.2 Target Population	16
3.3 Sample Size and Sampling Techniques	17
3.3.1 Determination of Sample Size	17
3.4 Data Sources.....	18
3.4.1 Primary Data	18
3.4.2 Secondary Data.....	19
3.5 Research Instruments	19
3.5.1 Questionnaire for SME Owners.....	19
3.5.2 Interview Guide for Loan Officers	19
3.5.3 Document Review Checklist	20
3.6 Quality Control	20

3.6.1 Validity of Instruments	20
3.6.2 Reliability of Instruments	20
3.7 Measurement of Variables.....	21
3.8 Data Collection Procedures.....	21
3.9 Data Analysis Techniques.....	22
3.9.1 Quantitative Data Analysis	22
3.9.2 Qualitative Data Analysis.....	22
3.10 Ethical Considerations.....	22
CHAPTER FOUR	23
PRESENTATION, ANALYSIS AND INTERPRETATION OF FINDINGS	23
4.0 Introduction	23
4.1 Response Rate.....	23
4.2 Background of Respondents	24
4.3 Descriptive Statistics for Study Variables.....	26
4.3.1 Credit Availability.....	26
4.3.2 Credit Terms	27
4.3.3 Interest Rate	29
4.3.4 Financial Performance of SMEs	30
4.4 Correlation Analysis.....	31
4.4.1 Credit Availability and Financial Performance	32
4.4.2 Credit Terms and Financial Performance	32
4.4.3 Interest Rate and Financial Performance	32
4.4.4 Relationships among independent variables.	32
4.5 Regression Analysis	33
4.6 Qualitative results	34
4.6.1 Theme 1: Border Area Problems	34
4.6.2 Theme 2: Collateral is Hard	34

4.6.3 Theme 3: SMEs Do not Understand Finance Well.....	35
4.6.4 Theme 4: Flexibility is Important.....	35
CHAPTER FIVE	36
SUMMARY, DISCUSSION, CONCLUSIONS AND RECOMMENDATIONS	36
5.0 Introduction	36
5.1 Summary of Findings.....	36
5.2 Discussion of Findings	36
5.2.1 Credit Availability and Performance.....	36
5.2.2 Credit Terms and Performance	37
5.2.3 Interest Rate and Performance	37
5.3 Conclusions.....	38
5.3.1 Credit Availability.....	38
5.3.2 Credit Terms	38
5.3.3 Interest Rate	38
5.4. Recommendations	38
5.4.1. For Banks and Microfinance	38
5.5 Contribution of the study.....	39
5.7 Areas of further Research	39
5.8 Chapter Summary.....	40
REFERENCES	41
APPENDICES	44

CHAPTER ONE

INTRODUCTION

1.0 Introduction

SMEs act as the bedrock for the economy of Uganda since they are responsible for employment creation and innovative ideas that promote inclusiveness within the country. As a matter of fact, in business centers like the Eastern division of Busia municipality, SMEs have played an integral part in ensuring sustenance as well as promoting cross-border trade. However, despite all their efforts, the problem that SMEs have been facing is that of poor access to finances.

The present research focuses on exploring the impact of access to financing on SME performance in the Eastern Division of Busia Municipality. Through examining access to financing in terms of availability, affordability, and usability of financing, this research hopes to offer some insights into how SMEs can help in furthering local development.

1.1 Background to the Study

The Small and Medium Enterprises (SMEs) have proved vital for the economic development of Uganda because they act as catalysts in job creation, innovation, and growth. There are about 1.1 million MSMEs in Uganda, contributing about 20% of the GDP in the country and providing over 2.5 million job opportunities (Uganda Bureau of Statistics [UBOS], 2020). The enterprises are especially important in rural and border areas as they keep the economy alive through trading, agriculture, and services offered. However, although the enterprises are very important for the economy, they continue to encounter many challenges towards sustainable development, including lack of finance (World Bank, 2020).

Access to finance entails the availability of affordable financing options and loans, which allow companies to invest and develop. Only 10 percent of businesses in Uganda have access to a bank loan or credit line, which is much lower than the Sub-Saharan average (World Bank, 2020). Some of the main issues associated with low access to finance include the lack of collateral, credit history, and financial literacy of entrepreneurs. About 70 percent of MSMEs experience credit gaps, especially for microenterprises, where 31 percent of the total number of companies indicate that finance is the main challenge in contrast to 21 percent of small firms and 10 percent of medium-sized enterprises (International Finance Corporation [IFC], 2021). Such constraints

limit the ability of these firms to make a contribution to the economy through investment and creating new jobs.

Busia Municipality in Eastern Uganda is an example that illustrates such characteristics at the national level with its own regional specifics. Located at the border between Uganda and Kenya, the town acts as a large commercial center providing a channel for cross-border business related to agriculture, consumption goods, and even gold mining (Busia Municipal Council, 2022). Eastern division of Busia Municipality is a highly populated urban area where numerous SMEs work predominantly in areas of retail and wholesale businesses, food processing, and small-scale manufacturing. Convenient geographic location and efficient transport networks help local SMEs to benefit from their access to the local and East African markets (Busia Municipal Council, 2022). In recent times, such phenomena as small-scale gold prospecting in the municipality that began in 1932 has contributed to increasing involvement of SMEs in related activities (Ministry of Energy and Mineral Development, 2023). However, SMEs in the region face some specific problems such as currency fluctuations connected with cross-border trade operations and a lack of access to formal financial resources. Studies have proved that financial accessibility affects SMEs' performance (Kasozi & Nakayi, 2021).

There is empirical evidence that improved financial inclusion results in better performance by SMEs globally and regionally. For instance, the case of the support by Norfund to the activities of DFCU Bank shows how access to finance can lead to increased borrowing for SMEs from USD 28 million in 2003 to USD 360 million in 2017 with SMEs accounting for 89% of total loans (Norfund, 2018). Filling the gaps in this regard is in line with development initiatives at the national level, especially as regards the National Development Plan III (2020/21-2024/25) whose main agenda is sustainable industrialization. This research paper seeks to investigate the impact of access to finance on the performance of SMEs in the Eastern Division of Busia Municipality.

1.2 Statement of the Problem

SMEs are crucial for the economic development of Uganda, but their operations in areas like Busia Municipality are hindered by obstacles related to finances. Even though there are more than 1.1 million MSMEs operating in Uganda, the country's financial services provided UGX 6.1 trillion (about USD 1.7 billion) in financing in 2019, of which only 17% was disbursed to

this sector (World Bank, 2020). The Busia area, where MSMEs operate along the border through trading and agricultural practices, still struggles with inflexibility when it comes to collaterals, costliness of lending, and information asymmetry, discouraging the uptake of formal financing. Research conducted in Busia Municipality recently showed that lack of accessibility to finances results in poor performances of SMEs, such as slow revenue generation and employment creation (Kasozi & Nakayi, 2021).

Without proper financing, small medium enterprises in the Eastern Division are unable to benefit from the regional market, thus resulting in a higher rate of failure of about 50% within five years due to lack of contribution to the GDP of Uganda (UIA, 2021). Previous measures undertaken include the program by DFCU Bank that assists women in starting businesses and have resulted in assistance to over 19,000 women entrepreneurs. However, the current programs still fall short of addressing the underlying problems faced by other SMEs. This study is, therefore, aimed at filling this knowledge gap.

1.3 Purpose of the Study

The purpose of this study was to investigate the relationship between access to finance and the financial performance of Small and Medium Enterprises in the Eastern Division of Busia Municipality, Uganda.

1.4 Research Objectives

1.4.1 General Objective

To examine the influence of access to finance on the financial performance of SMEs in the Eastern Division of Busia Municipality.

1.4.2. Specific Objectives

To assess the effect of Credit availability on financial performance of SMEs in the Eastern Division of Busia Municipality.

To establish the effect of Credit terms on financial performance of SMEs in the Eastern Division of Busia Municipality.

To assess the effect of interest rate on financial performance of SMEs in the Eastern Division of Busia Municipality.

1.5. Research Questions

What is the effect of Credit availability on financial performance of SMEs in the Eastern Division of Busia Municipality?

What is the effect of Credit terms on financial performance of SMEs in the Eastern Division of Busia Municipality?

What is the effect of interest rate on financial performance of SMEs in the Eastern Division of Busia Municipality.

1.6 Significance of the Study

The results obtained from the study will inform the relevant authorities such as Uganda Microfinance Regulatory Authority and Busia Municipal Council in making policies and developing strategies aimed at improving the ability of SMEs to get loans.

This can help SME proprietors and banks overcome challenges facing them in getting loans and perform better.

1.7 Justification

The Busia District's Eastern Division, which is known for its unique status as a border trading area between Uganda and Kenya, has its own unique problems to contend with, including those related to changes in the value of money and lack of integration with formal financial services (Busia Municipal Council, 2022). Previous studies carried out in regards to funding of small businesses have been broad, not taking into consideration the specificities of any given region.

1.8 Scope of the Study

1.8.1 Geographical Scope

The study was limited to the Eastern division of Busia municipality in Uganda due to the prevalence of SMEs practicing cross border trading and agro-processing in the region (Busia municipal council, 2022).

1.8.2. Content Scope

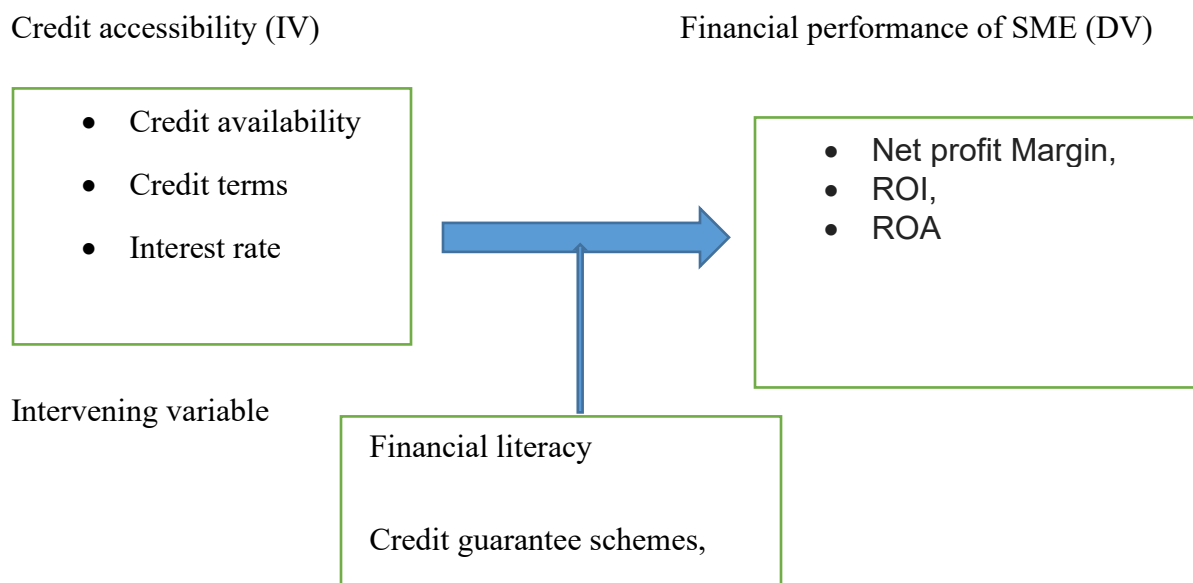
The study was concerned with access to finance factors such as credit availability, affordability, and usability of financial services and their effects on SME financial performance in the eastern division, Busia municipality.

1.8.3 Time Scope

The research used Data from 2020 to 2025 for the analysis of recovery patterns after the pandemic.

1.8. Conceptual framework

Figure 1 below provides a conceptual framework that outlines the way forward in examining the effects of access to finance on SME performance by showing the relationship between the two dimensions. It is important to identify intervening variables within this relationship to be able to make conclusions from collected data.



Adapted from Kasozi, J., & Nakayi, R. (2021) and modified by the researcher.

The model argues that credit access (in terms of credit availability, credit conditions, and credit surveillance) will have a direct effect on SME performance. As an illustration, increased credit availability allows SMEs to purchase new machinery and equipment, resulting in increased income and employment opportunities.

Intervening Effects: Access to finance will not have a straightforward effect on performance, but may be influenced by other intervening factors. To give an example, high financial literacy ensures better utilization of loans.

1.10 Operational Definitions of Key Terms

Small and Medium Enterprises (SMEs): Organizations employing less than 250 individuals and having revenues below UGX 500 million annually, according to the Uganda Investment Authority (UIA, 2021).

Financial Access: Refers to the ease and cost of accessing various financial services such as loans, credits, and leasing offered by formal organizations for businesses.

Performance: Assessed through metrics such as sales growth, profit margins, and job creation.

CHAPTER TWO

LITERATURE REVIEW

2.0 Introduction

In this chapter, a literature review related to credit availability and SME financial performance is conducted in detail. The literature review is divided into three broad categories, which include: Conceptual Literature Review, Theoretical Literature Review, and Empirical Literature Review related to the research questions.

2.1 Conceptual Review

2.1.1 SME financial Performance

The literature that describes the financial performance of SMEs has relied on a variety of theories. In the past, researchers have concentrated their focus on financial measures such as profitability, liquidity, and growth, among other financial indicators (Garengo et al., 2021). However, today, the focus is changing. A growing body of researchers is advocating for the use of other factors that influence SMEs, especially in the context of the developing world, where many unique features affect the performance of SMEs (Hansen & Hamilton, 2020).

In the case of Uganda, the financial performance of SMEs must be understood within the context of the formal and informal sectors. The Uganda Investment Authority describes the three stages of SME performance as survival, stability, and growth. In the case of Busia, which is a border town, the issue of exchange rates and the extent of the market must also be taken into consideration, especially when trade is involved (Kasozi & Nakayi, 2021).

2.1.2 Credit Accessibility

However, credit accessibility is not just about the availability of credit. It is also, about whether it is appropriate, accessible, and usable. Over time, the concept of credit accessibility has evolved from being a simple yes/no question to being more complex in the sense that different factors play varying roles in determining the level of credit accessibility (Beck & Demirgüç-Kunt, 2020).

Credit Availability: This factor is about the supply side of credit. It is about not only whether banks and other lenders are present in the country but also about the variety of credit products

offered and how accessible they are to potential borrowers in terms of transparency, ease of access, and reach (Abor & Biekpe, 2021). In border areas, things are more complex in the sense that SMEs are likely to access credit from lenders in other countries and hence create another dimension of financial access in the cross-border financial access environment (Munyambonera et al., 2022).

Credit Terms: This dimension of credit accessibility is about the factors that are between credit access and credit usage. This means it is about the interest rate of the credit offered, the collateral required in exchange for credit access, and the repayment period and requirements (Berger & Udell, 2020). The problem here is to differentiate between the credit terms offered and those experienced by SMEs in reality.

Credit Monitoring: This dimension of credit accessibility is often not given the attention it deserves. This is about the oversight and support aspects of credit access and usage (Diamond, 1984).

2.2 Theoretical Review

The basis of this study is the Pecking Order Theory of Myers and Majluf (1984). The rationale behind it is that, due to information asymmetry, firms would rather rely on internal sources of finance, then debt, and then equity as a last resort. However, in the case of SMEs in a developing country, due to real-world constraints such as meager profits, hence meager internal finance; difficulty in acquiring debt due to credit constraints; and an almost non-existent stock market (Mutesasira, 2021), the picture is a bit different. According to the pecking order theory, firms prefer a certain order of capital structure, which starts with internal financing, followed by debt financing, and then equity financing (Wanja & Muriu, 2020). Myers and Majluf (1984) opined that firms prefer retained earnings because of lower costs, followed by debt financing because of minimal information costs, and then, at last, equity financing because of higher transaction and information costs. Descriptively, the pecking order theory can be said to be a pyramid structure, where retained earnings are at the lower pyramid, debt financing at the middle pyramid, and equity financing at the upper pyramid of the pyramid structure, which reflects the risk appetite of the firms in descending order. In case retained earnings are not available, firms prefer to issue

debt instead of equity because of lower information costs of issuing debt, and equity financing is very rare.

Over time, these lofty ideas were intellectually polished into testable predictions. Shyam-Sunder and Myers (1999) were the first researchers to carry out a study on testing the impact of pecking order theory on firms financing decisions (Hsu, Chiang & Liao, 2019). In the views of Hsu, Chiang & Liao (2019), the pecking order theory was emphasized because of the short fall in the internal funds of a firm. The short fall in a firm's internal funds arises because of continuous losses in earnings, the amount of capital outlay earmarked for viable projects, variability in current assets, excess of divide

2.3 EMPIRICAL STUDIES

2.3.1 Credit Availability and SME financial Performance.

A deep dive by Beck & Demirgüç-Kunt in 2020 analyzed 120 studies across 79 countries to discover that simply being able to access credit accounts for 28-35% of the difference in the performance of SMEs in developing countries. The researchers identified three different ways that credit access works, with different effects in each case. Having physical access to credit increases the survival of an SME by 12%. Having the right credit products increases growth by 18%. Having an easier application process increases profitability by 22%. The researchers noted that the benefits of credit access start to dwindle when access becomes widespread. They also reminded readers that credit alone is not enough; other supporting factors are equally important.

A 2021 International Finance Corporation report identified that there was a significant financing gap for SMEs in 25 African countries. Urban SMEs are much more likely to have formal relationships with banks than rural ones 68% compared to 32%. For border towns, 45% of SMEs had formal relationships with banks, although only 18% had accessed formal credit over the past year. The report also highlighted the issue of "Availability Deserts," where credit is available but products are not appropriate.

The financing environment in Uganda is characterized by high unavailability. According to the World Bank Enterprise Survey (2020), 10% of Ugandan SMEs used bank loans, while the regional average was 15%, and the average in the developing economy was 25%. Geographic discrepancies were also evident, with SMEs from Kampala having 45% more credit availability

than SMEs in Eastern Uganda (Bwire et al., 2023). Disparities in sectors were also significant, with trade SMEs having 30% higher credit availability than manufacturing SMEs due to lenders' favoritism of liquid collateral.

Studies conducted in Uganda's border areas have shown unique characteristics. In a study conducted by Munyambonera et al. (2022) on five Uganda-Kenya border cities, 55% of SMEs operated bank accounts in both nations. This situation presented increased availability opportunities but posed issues of cross-border collateral pledges and credit history. SMEs who utilized transnational banks performed better by 25% but incurred 40% higher compliance expenses.

Kasozi and Nakayi (2021) reported credit availability among SMEs in Busia Municipality at 35%, which is lower than the national urban average of 48%. They pointed out three distinct obstacles faced by SMEs in Busia:

1. Border risk premium, whereby the lenders assessed that there was a higher likelihood of default among SMEs owing to cross-border activities
2. Currency mismatch, in which case the loan products available did not cater for multi-currencies
3. Unclear regulations regarding whose laws apply to the cross-border collateral

New research indicates that digital means have begun transforming credit availability. According to the Economic Policy Research Centre (2022), using mobile money for loans has boosted credit availability for SMEs in Uganda by 15 percentage points from 2020 to 2022. The effect is more pronounced in other regions than in border areas, where SMEs received an additional seven percentage points of credit availability due to interoperability issues between the mobile money systems in Uganda and Kenya.

2.3.2 Credit Terms and financial Performance of SME

Research findings have continuously shown nonlinear relationships between interest rates and SME performance. As per Abor & Biekpe (2021)'s study in six African countries, interest rates below 15% had threshold effects, with each percentage drop corresponding to a 5% improvement in performance. Interest rates ranging from 15%-25% had neutral effects on performance, whereas those above 25% had negative effects, correlating to an 8% decline for every percentage

rise. In Uganda, where interest rates for SME lending lie between 19%-22%, the majority of enterprises fall into the neutral category, hence the modest growth observed even when credit is available (Bank of Uganda, 2023).

Collateral continues to be the major impediment to SME financing. According to Berger & Udell (2020), 65% of rejected loans in developing nations had to do with collateral. Innovations in collateral frameworks have brought hope with regard to financing of SMEs; for instance, movable collateral registries in Ghana led to a 40% rise in loans approved (IFC, 2021). Nonetheless, in Uganda, the percentage of SME loans financed via non-traditional collateral stood at only 15% in 2023.

Another essential yet underexplored factor regarding credit terms is maturity mismatch. Hansen and Hamilton (2020), in their East African study, indicated that 70% of SME loans have maturities below 12 months, compared to 24-month investments. The resulting maturity mismatch led to unnecessary loan rollover costs that reduced profitability by 15-20%. Term structure flexibility that matched the business cycle led to better results: Kenyan SMEs that implemented seasonal repayments enjoyed a 35% improvement in profitability relative to those with rigid monthly payments (FSD Kenya, 2022).

The credit term problems faced by border SMEs are unique. Kasozi & Nakayi (2021) discovered that 60% of the Busia SMEs considered unfavorable terms as their biggest financing problem; 15-25% of firms had no effect on their performance, while more than 25% correlated with declining performance at a rate of 8% per 1%. In Uganda, where average SME lending rates are 19-22%, most businesses remain in the neutral zone, which explains limited growth even when credit is available (Bank of Uganda, 2023).

Collateral continues to be the most significant constraint in SME finance. According to the global review of Berger & Udell (2020), collateral requirements account for 65% of loan denials in developing nations. Innovations in collateral systems have potential benefits, as evidenced by Ghana's movable collateral registers, which raised SME loan approvals by 40% (IFC, 2021). However, progress in this area in Uganda has been slow, with only 15% of SME loans collateralized using non-traditional assets like receivables, equipment, and warehouse receipts (Uganda Bankers Association, 2023).

The maturity mismatch of loan terms presents another important but often overlooked issue. Hansen & Hamilton (2020) revealed in their East Africa study that 70% of SME loans matured within one year, although investment horizons ranged from 24 months on average. Such a maturity mismatch necessitated expensive rollovers, which cut profits by 15-20%. A more flexible term structure consistent with business cycles yielded positive results: Kenyan SMEs that used seasonal repayment plans posted 35% higher profitability than firms following strict monthly repayment plans (FSD Kenya, 2022).

There are unique problems with credit terms that SMEs operating along borders have. According to Kasozi and Nakayi (2021), 60% of SMEs in Busia cited unfavorable terms as the most significant obstacle for financing. Some of the problems associated with the credit terms involved having a single currency in a multi-currency economy, rigid repayment terms when the borders were closed, and difficulties with cross-border collateral valuation. The SMEs that accepted such conditions had a 25% slower growth rate than other firms that relied on other means of financing.

In addition to the explicit terms, there are also implicit costs involved in credit terms that can impact the effectiveness of the borrowing process. A study conducted by the Uganda Microfinance Regulatory Authority in 2023 found that the actual interest rates were eight percentage points higher than what was explicitly stated since the cost of fees, insurance, and savings accounts was factored in. The problem was more pronounced among borrowers who lacked financial knowledge and were unable to understand some of the details of the loan terms.

However, besides what is explicitly stated, the effective terms may involve hidden charges. In one such analysis conducted in 2023 by Uganda Microfinance Regulatory Authority, the average effective interest rate was recorded to be eight percent. During the interest rate cap experiment in Kenya (2016 – 2019), access to credit among SMEs initially increased but later decreased as lenders pulled out of higher-risk groups (Central Bank of Kenya indicates that once charges, premiums, and saving plans are added, actual interest rates are much higher than what was stated in 2020). The same applies to Uganda.

The recent policy innovations have provided some valuable lessons, although there have been mixed results. For instance, in the case of interest rate capping in Kenya between 2016 and 2019,

at first, it increased the availability of credit for SMEs, but then it decreased. This is due to the fact that the gradual approach, which does not involve imposing caps on interest rates but only relies on persuasion, has led to inconsistent results. Another important issue that should be investigated is how innovative segments of term risk management, including multi-currency loans, cross-border collateral pooling, and grace periods across borders, would affect SMEs' performance in countries such as Uganda.

2.3.3 Interest rate and financial Performance SME

According to global empirical evidence, the rise in interest rates impacts the investment of SMEs in productive capacity within the region. For instance, the World Bank Enterprise Surveys (2022), which surveyed 50 emerging countries, indicated that an increase of five percentage points in real interest rates causes a 12% fall in the capital spending of SMEs. Besides profitability, the impact of interest rates on SMEs depends on the degree of profit-making in SMEs. Specifically, SMEs that are highly profitable with a gross margin exceeding 30% can cope with high-interest rates. In contrast, SMEs that do not earn much profit, such as in retail, feel the effects of high-interest rates immediately (Demirgüç-Kunt et al., 2020). It is crucial to mention that Busia is considered a border economy and, thus, trade SMEs operate with tight margins there.

The examples from Africa show the highest effective interest rates around the world, leading to unique performance trends. According to the Financial Sector Deepening report by the African Development Bank (2023), SME lending rates on the continent of Sub-Saharan Africa were at 18–25%, while those in South Asia stood at 8–12%, and in East Asia at 5–8%. Such high interest rates were the result of various structural issues, such as high-risk perception, weak competition, expensive due diligence, and volatility of prices. A study of twelve countries in Africa by Beck and Cull (2022) showed the effect of “performance penalty,” where SMEs that paid above-median interest rates had 28% less employment growth and 35% less reinvestment.

There is a unique interest rate environment prevailing in Uganda. According to the Bank of Uganda (2023), the average interest rates for SMEs' commercial lending are 19.2%. By sector, the interest rate ranges are: trade at 18.5%, manufacturing at 20.1%, and agriculture at 21.3%. The real interest rate, considering inflation rates, over the last ten years has varied from 8–15%,

far higher than the 5% ideal interest rate recommended for SME development in developing countries (Mugume & Lwanga, 2022). The interest costs account for 15–25% of SME revenues, while those of large firms range from 5–10%.

The economy of the border is characterized by a highly elastic reaction towards the changes in interest rates. The researchers of Busia, for example, observed that interest rates were around 2 to 3 percent higher than the national average due to the risk and costs involved in dealing with cross-border customers. The interest rate that they experienced with formal credit was 24%, which contrasted with the figure of 18% that the Kampala-based enterprises enjoyed. The increased cost was an indication that the margin of profit in the cross-border trade, which stood at 5 to 15 percent, had been eroded.

According to Kasozi and Nakayi (2021), specific information is provided about the impacts of interest rates on SMEs based in Busia. From a sample size of 150 firms, 65% indicated that interest rates are the major issue they faced when seeking credit from formal lenders. Interest rate increases by 1%, leading to a decrease in the profits by 2.3%, were an obstacle to them. A firm facing an interest rate more than 25% has 40% higher chances of being in distress in any particular year. However, while coping with high-interest rates proved hard, the fluctuation of the interest rates is even harder, with a response of seeking alternative sources of funding among them. For example, 45% sought informal sources of financing that charged interest rates of between 30 and 50% per month. They were impressed by the flexibility and the ability to provide financing despite the irregularity of inflow of finances. From this, it is clear that interest rates are not the sole variable determining their impacts.

Studies into the role of technology-based lenders indicate conflicting findings. For example, Turyahebwa et al. (2023) revealed that mobile money lenders in Eastern Uganda charge a total interest rate ranging from 30-60% considering charges and mandatory savings. Even with that, 35% of small and medium-sized enterprises (SMEs) in Busia were engaging in such lending services. Though this practice might hinder the growth of SMEs in the long term, it enables them to use short-term liquidity in making border transactions.

With regard to the Eastern Division of the Busia Municipality, there are other relatively overlooked variables. To begin with, there is the matter of foreign currency since the SMEs

located across the Uganda-Kenya border borrow in Ugandan shillings while earning in Kenya shillings, which means that the interest rate problem escalates owing to the exchange rate difference (Munyambonera et al., 2022). The second variable relates to seasonality since the business environment across the Uganda-Kenya border depends heavily on the weather, holidays, and academic term. However, lenders require borrowers to make monthly payments, meaning that there is the need for costly rescheduling when business becomes tough. Thirdly, there is the matter of competition where Kenyan financial institutions in Busia operate at interest rates lower by 2-3% compared to Ugandan institutions, yet cross-border borrowing is not possible.

2.4 Chapter Summary

This literature review has set up various essential pillars for the research. The first one pertains to the conceptualization of both concepts: credit availability and performance. The second one refers to the theoretical frameworks, which have been used in previous studies to explain the phenomena, such as the Pecking Order Theory. The review proves that this research is important and novel since the connection between the concepts has been explored in the past, but only generally.

CHAPTER THREE

RESEARCH METHODOLOGY

3.0 Introduction

This chapter presents the research methodology that was used in the research in an easily understood manner. It includes an explanation of the research design, the people involved in the research, the number of people involved, and the selection of the people involved in the research. It also includes an explanation of the sources of data used in the research, the methods of collecting data, the quality checks that made sure that the data collected was of high quality and reliable, and the methods used to analyze the collected data.

3.1 Research Design

The researcher used a cross-sectional descriptive survey that integrated numerical and descriptive information. Descriptive surveys are essential in collecting information from a given population concerning a given aspect without any form of bias, as Amin (2005) noted. To enhance understanding, the researcher used a combination of quantitative and qualitative methods of exploration for the subject matter. In the quantitative aspect, questionnaires were used to collect information and reveal the quantitative associations between the variables of interest. According to Creswell (2014), a combination of methods provides a deeper understanding and increases the validity of the information obtained.

3.2 Target Population

There were two main groups for targeting: one group consisted of owners and managers of SMEs registered within the Eastern Division of the Busia Municipality, while the other was comprised of loan officers working within the financial institutions serving the same area. The combination of both groups provided a balanced approach to credit availability, considering both sides of demand and supply.

Table 3.1: Target Population Distribution

Category	Population
SME Owner	50
Loan Officers from commercial banks	15
Loans officers from microfinance institutions	12
Loans officers from SACCO's	8
GRAND TOTAL	85

Source: Busia Municipal Council Business Registry (2024) and researcher's compilation

This sample of 85 persons served as a strong basis for the analysis of the issues surrounding credit availability and SMEs' performance within the Eastern Division. Both the owners of the SMEs and the lending officials were included in order to triangulate the data and insights gained.

3.3 Sample Size and Sampling Techniques

3.3.1 Determination of Sample Size

The sample size was calculated using the Yamane formula (1967). This is a common way of deriving sample sizes for populations. The formula gives an easy way of determining sample sizes at various confidence levels and errors of approximation:

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

Where:

n = required sample size

N = total population size

e = desired margin of error (expressed as a decimal)

For this study, the following parameters were applied:

Population of SME owners (N) = 85

Confidence level = 95%

Margin of error (e) = 0.05

Substituting these values:

$$n = 851 + 85(0.05)^2 = 851 + 85(0.0025)$$

$$n = 851 + 1.3 = 851.21 \approx 70$$

Thus, the sample size of 70 SME owners is statistically adequate for drawing meaningful conclusions about credit accessibility and performance.

Sample Size for Loan Officers

Table 3.2: Sample Size Distribution

Category	Population	Sample Size	Sampling Technique
SME Owners/Managers	50	91	Purposive sampling
Loans officers from commercial banks	15	41	Simple random sampling
Loans officers from microfinance institutions	12	31	Simple random sampling
Loans officers from SACCOs	8	37	Simple random sampling
Sub-total SME Owners	85	70	

3.4 Data Sources

3.4.1 Primary Data

The structured questionnaires were conducted among the SME owners and managers in order to gather information about credit availability, terms, monitoring, and the indicators for financial performance. Additionally, the semi-structured interviews were conducted among the loan officers and key informants in order to gather in-depth information. According to Kothari (2004),

the use of primary data is beneficial because of its originality, relevance, and specificity to particular research problems.

3.4.2 Secondary Data

Secondary data was collected from sources that were published and unpublished, which include books, articles, reports, dissertations, proceedings, annual reports of commercial banks, Busia Municipal Council archives, Ugandan Bureau of Statistics literature, and policy papers of respective ministries. The examination of secondary data enabled the study to gain perspective on SME financing in Uganda, establish the existing gap in research, and corroborate findings obtained through primary data sources (Saunders et al., 2019).

3.5 Research Instruments

3.5.1 Questionnaire for SME Owners

Questionnaires were the main data collection tools utilized to gather quantitative information from the owners/managers of the small and medium-sized enterprises (SMEs). Most questions on the questionnaires involved a 5-point Likert Scale from one, which indicated 'strongly disagree', to five, which indicated 'strongly agree'. In other words, questionnaires were utilized to measure both perceptions and attitudes and generate data amenable to statistical analysis (Amin, 2005).

3.5.2 Interview Guide for Loan Officers

The study is still developing its interview protocol to provide guidance for the in-depth interviews to be conducted with loan officers and key informants. The main topics to be discussed are the individuals involved and their backgrounds (you and your organization), the current credit landscape (problems and how to obtain credit), the credit terms (how interest is calculated and what collateral is needed), how credit is monitored and whether the system works, the current financial state of SMEs in relation to credit, and opportunities to improve credit access within a border context.

A semi-structured interview plan was followed to provide some guidance while allowing for exploration of interesting issues that may arise, ensuring all-important aspects are covered (Kvale & Brinkmann, 2015). This will provide room to explore deeper, previously unimaginable aspects of the ability of SMEs to gain credit within a border context.

3.5.3 Document Review Checklist

The researcher will utilize a checklist to extract information from secondary sources using a document review checklist. This will facilitate a comprehensive analysis of available literature and other documents through various categories such as financial statistics, financial policies, financial regulations, and research studies conducted previously.

3.6 Quality Control

3.6.1 Validity of Instruments

Validity refers to the ability of the research tools to measure what they are intended to measure (Best & Kahn, 2003). To ensure that there was content validity, a rigorous review of the questionnaires and interview schedule was conducted. First, the questionnaires and interview schedule were sent to the research supervisor and two SME experts with vast experience and expertise in SME studies and financing.

These experts were asked to evaluate each of the items for relevance, clarity, completeness, and consistency with the objectives and concepts of the study. After receiving feedback from the experts, vague items were clarified, irrelevant items were removed, and new items were included where necessary, where there were identified gaps. The Content Validity Index (CVI) was computed as the ratio of the total number of items that were rated as relevant to the total number of items used in the tool. Mugenda and Mugenda (2003) argue that a CVI of 0.70 and above was acceptable, and the tools had a CVI of 0.78, which was adequate for the intended data collection.

3.6.2 Reliability of Instruments

Reliability is a measure of the accuracy of the measuring instruments used in a study. The accuracy of the instruments is reflected by the degree of stability and consistency that they produce when they are used several times on different occasions (Donald, 2006). A reliability study was done involving a pilot group of 30 SME owners and managers in another division of the Busia Municipality not included in the primary sample.

This was because of the resemblance between the pilot sample and the target population. In order to determine the level of reliability, a test-retest procedure was adopted. The questionnaire was given to the same sample twice after a period of two weeks. The Pearson's product-moment

correlation coefficient between the test and retest scores was computed to provide a reliability coefficient of 0.78, which is above the recommended minimum of 0.70 (Mugenda & Mugenda, 2003).

The internal consistency of the questionnaire was established by computing the Cronbach's alpha coefficient for each construct. The reliability coefficients were computed to be 0.82, 0.79, 0.81, and 0.84 for credit availability, credit terms, credit monitoring, and financial performance constructs, respectively. These reliability coefficients are above the minimum acceptable value of 0.70 (Nunnally & Bernstein, 1994).

3.7 Measurement of Variables

Measuring the variables involved in a study will make sure that the concepts proposed for investigation are specific and operationalizable. The independent variable in the study, which is access to credit, was subdivided into three aspects namely, access to credit, access terms, and credit monitoring. Each of these aspects was measured using multiple indicators through the use of Likert scales from one to five points.

For the dependent variable SME financial performance, the researcher used four indicators: revenue growth, profitability, return on investment, and job creation. These measures used perceptual measures of five-point Likert scales to assess SME financial performance because it is often difficult to obtain actual financial statements from SMEs in a developing economy setting (Hansen & Hamilton, 2020)

3.8 Data Collection Procedures

The data collection process was characterized by a well-structured sequence that was geared towards enhancing response rates as well as maintaining high quality data. After receiving the go-ahead from the Uganda Christian University School of Business Research Ethics Committee, the researcher then proceeded to seek formal authorization from Busia Municipal Council as well as the financial institutions operating in the Eastern Division.

The researcher then sought to bring on board two research assistants to be trained on the procedures of data collection, ethics of data collection, and the appropriate use of the research tools. The research assistants were trained on how to approach the respondents, explain to them the purpose of the research, as well as the appropriate handling of the information collected.

3.9 Data Analysis Techniques

3.9.1 Quantitative Data Analysis

Quantitative data was coded, entered into a computer database, and analyzed using the Statistical Package for Social Sciences (SPSS) version 26. Data cleaning was performed to identify and correct errors, inconsistencies, or missing values. Both Descriptive and inferential statistics were used to analyse quantitative data.

3.9.2 Qualitative Data Analysis

Qualitative information gathered from the interview was analyzed through thematic content analysis following Braun & Clarke's 2006 thematic content analysis guidelines.

3.10 Ethical Considerations

Ethical integrity was at the core of the research and was followed at every step of the way. Informed consent was sought from all the respondents. The respondents were clearly and fully informed about the objectives of the research, methods, potential benefits, and possible harm, and their right to refuse to participate in the research without any consequences was clearly explained to them.

Confidentiality of the respondents was strictly adhered to. Not using names but instead coding the answers on the questionnaires and the computer data did this.

Privacy of the respondents was a key consideration during the actual collection of the data. Interviews and questionnaires were conducted in comfortable and private environments. The researcher was mindful of the cultural nuances of Busia Municipality and made sure that she was appropriately dressed, used appropriate language, and was mindful of the way of doing business in the region.

Finally, the researcher was honest and transparent throughout the entire research and reporting process, and the findings were accurately and truthfully represented without any form of fabrication, falsification, and misrepresentation, contributing to the existing body of academic literature on SME financing in the border economies of Uganda.

CHAPTER FOUR

PRESENTATION, ANALYSIS AND INTERPRETATION OF FINDINGS

4.0 Introduction

This chapter discusses the findings obtained during the field work. In other words, this is the section that discusses the interpretation and analysis of data gathered from the SMEs within the Eastern Division of Busia Municipality. The main focus of this research was the issue of credit access and financial performance among SMEs. This chapter begins with discussion on response rate, respondent background, descriptive analysis of all variables, correlation analysis, regression analysis and qualitative analysis of loan officers' responses.

4.1 Response Rate

The researcher targeted 70 SME owners and managers and 15 loan officers from financial institutions in Eastern Division. Table 4.1 shows how many responded.

Table 4.1: Response Rate

Category	Given Out	Returned	Response Rate (%)
SME Owners/Managers	70	62	88.6%
Loan Officers	15	12	80.0%
Total	85	74	87.1%

Source: Field data, 2025

From Table 4.1, 70 copies of questionnaires distributed to SMEs owners had 62 submitted, giving a response rate of 88.6%. From the 15 loan officers selected, 12 responded, representing a rate of 80.0%, making the overall response rate of 87.1%. In accordance with Mugenda & Mugenda (2003), a response rate exceeding 70% is highly acceptable in research. Such an excellent response rate was obtained due to continuous follow-up by the researcher and assurances of anonymity of responses.

4.2 Background of Respondents

This section covers gender, age, education, type of business, years in business, and whether they have ever taken a loan.

Table 4.2: Background of SME Owners (n=62)

Characteristic	Category	Number	Percentage (%)
Gender	Male	28	45.2
	Female	34	54.8
Age	18-25 years	8	12.9
	26-35 years	22	35.5
	36-45 years	19	30.6
	46-55 years	9	14.5
	56 years and above	4	6.5
Education	No school	5	8.1
	Primary	12	19.4
	Secondary	26	41.9
	Tertiary/University	19	30.6
Business Type	Retail shop	24	38.7
	Wholesale	10	16.1
	Cross-border trade	15	24.2
	Agro-processing	7	11.3
	Small factory	4	6.5
	Other services	2	3.2

Years in Business	Less than 1 year	6	9.7
	1-3 years	18	29.0
	4-6 years	21	33.9
	7-10 years	12	19.4
	Above 10 years	5	8.1
Ever Taken Loan	Yes	38	61.3
	No	24	38.7
Where they got loan (n=38)	Commercial bank	14	36.8
	Microfinance	16	42.1
	SACCO	8	21.1

Source: Field data, 2026

Gender: According to the table above, more women (54.8%) own SMEs than men (45.2%). This means that women are involved in doing business in Eastern Division, particularly trading. This is common in border regions, where women conduct cross-border trading.

Age: The largest percentage (35.5%) of the respondents fall within the age range of 26-35 years. Other 30.6% of the respondents are aged between 36 and 45 years. This means that young people and middle-aged individuals are managing SMEs in Busia. Six and half percent of the respondents were aged above 56 years.

Education: The largest percentage (41.9%) of the respondents had attained secondary education. Those who had completed tertiary education were 30.6%, while only 8.1% were illiterate. The findings show that majority of the SME owners could be literate and, therefore, able to maintain business records. However, according to a loan officer, the SME owners:

“They can read but understanding the loan conditions is another thing. Many just sign without really understanding.” (Loan Officer, Microfinance).

Business Type: The largest business type is retail trade at 38.7%. Cross-border trade stands at 24.2% since Busia is bordering with Kenya. Wholesale accounts for 16.1%. Agro-processing and manufacturing account for little share, which indicates limited value addition activities in this region.

Years in Business: Most firms (33.9%) are aged 4-6 years. Firms aged 1-3 years stand at 29.0%. Less than 10 percent of businesses are above 10 years old. This implies that many businesses do not last up to 10 years, or they diversify into other types.

Loan History: Over half of the firms (61.3%) had loans from formal sources. From those who borrowed, microfinance dominated the list at 42.1%, followed by banks (36.8%), SACCOs (21.1%). This confirms the importance of microfinance to SMEs in Busia.

4.3 Descriptive Statistics for Study Variables

The scale was 1 to 5 where 1=Strongly Disagree, 2=Disagree, 3=Not Sure, 4=Agree, 5=Strongly Agree. Mean scores are interpreted as: 1.0-1.8 (Very Low), 1.81-2.60 (Low), 2.61-3.40 (Medium), 3.41-4.20 (High), 4.21-5.00 (Very High).

4.3.1 Credit Availability

This was the first objective of the study and its findings were presented in table Table 4.3 below.

Table 4.3: Descriptive statistics on Credit Availability Results

Statement	Mean	Std. Dev.	Meaning
There are enough banks and microfinance in Eastern Division	3.85	0.89	High
They have different types of loans for my business	3.26	1.02	Medium
The process of applying is simple	2.94	1.14	Medium
Loans are processed fast (within 2 weeks)	2.71	1.21	Medium
Banks are willing to lend to people like me	3.18	1.08	Medium
The loan amounts given are enough for my needs	2.68	1.16	Medium
Bank branches are near my business	4.12	0.76	High

Loan officers are easy to talk to	3.77	0.92	High
Average	3.31	1.02	Medium

Source: Field data, 2026

The mean score for credit availability is 3.31, representing a medium level. It implies that despite the presence of banks, accessing loans is still a difficult task.

The highest ratings are for "banks are accessible geographically" (4.12) and "enough financial institutions" (3.85). Hence, physical access does not appear to be a major issue. A female trader from the retail sector indicated,

"Banks are available everywhere in Busia town. You can find them along the main road. However, accessing funds from within is another issue altogether." (Female trader, retail)

Conversely, the lowest mean score is for "sufficient amount of funds offered" (2.68) and "quick processing of loan application" (2.71). Hence, the loans accessed are often insufficient in terms of amount and processing time. For example, a male trader from the cross-border sector commented,

"I applied for five million; I received two million after one month. In the meantime, my intended purchase had been acquired by some other person." (Male trader, cross-border)

These results demonstrate that credit availability goes beyond accessibility. It encompasses sufficient fund amounts and timely processing times.

4.3.2 Credit Terms

This was the second objective of the study and its findings were presented in table 4.4 below.

Table 4.4: Descriptive statistics on Credit Terms Results

Statement	Mean	Std. Dev.	Meaning
Interest rates are affordable	2.31	1.08	Low
Collateral requirements are fair	2.45	1.21	Low
Repayment period is long enough	2.58	1.14	Low
There is flexibility in repayment	2.62	1.19	Medium
They give grace period before repayment starts	2.18	1.06	Low
Fees are explained clearly	2.89	1.12	Medium
Total cost of loan is clear	2.77	1.18	Medium
They accept other things as collateral (not just land)	2.36	1.24	Low
Average	2.52	1.15	Low

Source: Field data, 2026

Credit terms have a mean score of 2.52, which is quite low. It implies that SME proprietors do not find credit terms favorable.

The least score was "grace period," having a mean of 2.18. Most lending organizations require immediate repayment or at least one month after taking the loan. An entrepreneur lamented:

"You borrow the money, then after one month they will demand their first payment. But by then, you haven't started earning any income. So, you must pay out of your own pocket." (Female, wholesale)

Interest rates received a low score of 2.31. Most interviewees argued that interest rates were too high. For example, one respondent said:

"I took a loan worth 3 million from microfinance. After I settled my debt, I had paid 5 million. My profit disappeared." (Male, Retail)

The issue of collateral was another challenge (2.45). Banks seek land titles; however, most SMEs use rented land. The loan officer stated,

"We require collateral because of policy. However, we are aware that most reputable companies do not own land. We are striving to introduce collective guarantees for small amounts." (Loan Officer, SACCO)

The only factors rated as moderate were flexibility (2.62) and explanation of charges (2.89). Even these are relatively low. Credit conditions are a major hindrance to SME development in Busia.

4.3.3 Interest Rate

This was the third objective of the study and its findings were presented in table 4.5 below.

Table 4.5: Descriptive statistics on Interest Rate Results

Statement	Mean	Std. Dev.	Meaning
The interest rate I pay is affordable	2.26	1.11	Low
High interest reduces my profits a lot	4.18	0.84	High
I understand the difference between advertised rate and what I actually pay	2.54	1.23	Low
I prefer higher interest if repayment is flexible	3.42	1.08	High
Current interest allows me to grow my business	2.21	1.16	Low
Interest changes make it hard to plan	3.95	0.91	High
I have rejected loans because of high interest	4.06	0.88	High
High interest forces me to do only quick business, not long-term	4.11	0.86	High
Average	3.34	1.01	Medium

Source: Field data, 2026

The average is 3.34, which is medium, but this hides the real story. Some items scored very high and some very low.

Most people agreed that high interest reduces profits (4.18) and forces them to focus on short-term business (4.11). Many have rejected loans because rates were too high (4.06). A business owner explained:

"If I borrow at 25%, I have to sell things which have high velocity. I cannot think of borrowing to buy a machine or to expand because it will take some time to repay." (Male, agro-processing)

"Understanding interest rate" received low scores (2.54). This implies that most borrowers do not understand their obligations well. The loan officer commented:

"We inform them on monthly interest rates but there are other costs such as charges and insurance. When added together, it becomes high. They don't get it until they start making repayments." (Loan Officer, Bank)

Surprisingly, many stated they preferred high interest with flexible repayment (3.42). It reveals that flexibility was a key determinant of interest preferences by SMEs. The cross-border trader explained:

"I can even accept a little high interest as long as they can give me flexibility during difficult periods. If the borders close or the value of our currency falls, I cannot make payments." (Female, cross-border trade)

4.3.4 Financial Performance of SMEs

This was the dependent variable and its findings were presented in table 4.6 below.

Table 4.6: descriptive statistics on Financial Performance Results

Statement	Mean	Std. Dev.	Meaning
My sales have increased in the last three years	3.52	1.04	High
My profits have grown steadily	2.84	1.12	Medium
I have been able to put profits back into business	3.08	1.08	Medium

My return on investment has improved	2.71	1.15	Medium
I have expanded my business	2.66	1.21	Medium
I have hired more workers	2.48	1.18	Low
My business assets have increased	2.93	1.09	Medium
I am serving more customers now	3.37	0.98	Medium
Average	2.95	1.11	Medium

Source: Field data, 2025

The mean score is 2.95, which implies that SME performance is moderate. This shows that the business entities are performing reasonably well but are far from being good.

There has been a rise in sales (3.52), however, profits have remained at an average level (2.84). This indicates that while businesses are selling more products and services, they are not making as much profit as possible. As stated by one respondent,

"I am selling more than I used to sell earlier, but the amount of money I retain? Not much, loan interest consumes it all." (Female, retail)

The lowest mean score obtained was on employment of new employees (2.48). This is quite concerning because the businesses are not able to generate jobs for their people. According to a loan officer,

The business expansion was rated very poorly (2.66). This indicates that there is no growth among SMEs in terms of expansion. They maintain their size.

Number of clients went up (3.37), reflecting the increase in sales. But without any profit increase, an increase in number of clients will not translate into increased profitability.

In general, it is evident that SMEs in Busia are having problems converting sales into growth and job creation. The credit conditions, particularly the high interest rates, may be limiting them.

4.4 Correlation Analysis

A correlation analysis helps determine the existence and strength of association between two variables. In this study, Pearson correlation was applied. Correlation coefficients range from -1 to +1. The closer to +1, the stronger the positive correlation. See Table 4.7 below.

Table 4.7: Correlation Results

Variable	Credit Availability	Credit Terms	Interest Rate	Financial Performance
Credit Availability	1			
Credit Terms	0.412**	1		
Interest Rate	0.386**	0.528**	1	
Financial Performance	0.445**	0.512**	0.468**	1

**Significant at 0.01 level

Source: Field data, 2025

4.4.1 Credit Availability and Financial Performance

The correlation coefficient of 0.445 is medium-positive. This implies that there is a direct relationship between credit accessibility and financial performance. It is highly significant (0.01).

4.4.2 Credit Terms and Financial Performance

Credit terms showed the strongest correlation of 0.512, indicating a high level of positive association between the two variables. It implies that credit terms with fair interest, sufficient security, and adequate time lead to improved business performance.

4.4.3 Interest Rate and Financial Performance

Interest rate correlated positively with 0.468, showing a moderate relationship. People perceive interest rates as more affordable if financial performance is good. Conversely, firms performing well are likely to consider the interest rates cheaper.

4.4.4 Relationships among independent variables.

There are also connections between the three variables. The correlation between credit terms and interest rate is quite high (0.528), since both variables belong to the same category. Nevertheless, there are no correlations higher than 0.70, thus, they can be used in the analysis together.

4.5 Regression Analysis

The regression analysis is aimed at examining how well the independent variables account for financial performance. Moreover, it indicates the key variable. The model summary is provided in Table 4. 8..

Table 4.8: Model Summary

Model	R	R Square	Adjusted R Square
1	0.612	0.375	0.352

Source: Field data, 2025

The value of R is 0.612, a strong one. The value of R square is 0.375. It implies that 37.5 percent of variation in financial performance is explained by credit availability, credit terms, and interest rates together, while the remaining 62.5 percent may be attributed to other factors.

Table 4.9: ANOVA

Model	Sum of Squares	df	Mean Square	F	Sig.
Regression	14.823	3	4.941	16.872	0.000
Residual	24.692	58	0.426		
Total	39.515	61			

Source: Field data, 2025

The F value is 16.872 and significance is 0.000. This means the model is good and the results are not by chance.

Table 4.10: Coefficients

Model	Unstandardized B	Std. Error	Standardized Beta	t	Sig.
(Constant)	0.847	0.312		2.715	0.009
Credit Availability	0.241	0.098	0.251	2.459	0.017

Credit Terms	0.336	0.112	0.348	3.000	0.004
Interest Rate	0.218	0.104	0.235	2.096	0.041

Source: Field data, 2025

The dependent variable shows that credit terms is the best predictor since Beta = 0.348. Therefore, it adds more to financial performance than any other variable. Other variables are interest rate with beta = 0.235 and credit availability with beta = 0.251. The p-value is less than 0.05 for all. As a result, a unit improvement in credit terms raises financial performance by 0.336 units.

4.6 Qualitative results

Twelve loan officers from banks, microfinance, and SACCOs were interviewed to give their opinions about lending to SMEs in Busia. Four major themes emerged from the discussions.

4.6.1 Theme 1: Border Area Problems

The credit situation in Busia is distinct because of its location in proximity to Kenya. According to one bank manager:

"Our clients trade in Kenya. They make money in Kenyan currency but borrow in Ugandan currency. Any variation in the exchange rates alters their capacity to repay. This must be considered."

The second respondent said:

"If our client's venture is in Kenya and fails to repay, how will we get the money back? It costs too much to pursue this process in Kenya, so we minimize the loan amount or demand security." (Microfinance officer, 5 years' experience)

This is how the presence of many banks cannot guarantee credit access.

4.6.2 Theme 2: Collateral is Hard

The officers agreed that collateral is a huge problem. For example:

"The Bank of Uganda requires us to have collateral. However, SMEs do not usually own land, and they rent their premises. We normally use the concept of group lending for small amounts, but for larger amounts, we require land." (Bank officer, 15 years)

However, some are doing something different:

"We currently allow group guarantees to an amount of 2 million. Also, we are testing warehousing receipts whereby collateral is based on the products stored." (SACCO officer, 7 years)

4.6.3 Theme 3: SMEs Do not Understand Finance Well

"Many of the SME owners do not have financial awareness," one officer said.

"They don't record. They can tell what they have in business in their mind, but they cannot put it on paper. This makes our job difficult."

Another officer mentioned that "They see the monthly interest rate, which seems low. However, with all the charges and insurance, it gets very high. Once they pay, they feel that we cheated them despite all the information we gave them."

This highlights the importance of training along with lending.

4.6.4 Theme 4: Flexibility is Important

The officers concurred that flexible terms enhance the performance of SMEs. One of them stated:

"We have standard products, but we try to be flexible. With farmers, we give them loans that can be repaid after harvesting. With traders, we give them loans that can be repaid after the trade cycle. They work best."

(Microfinance officer, 7 years)

CHAPTER FIVE

SUMMARY, DISCUSSION, CONCLUSIONS AND RECOMMENDATIONS

5.0 Introduction

The chapter contains summary, discussion, conclusion and recommendations from the results obtained in the research. Credit is one of the significant connecting factors and also a catalyst for growth among Small and Medium Enterprises Sandu et al (2017). The chapter will be divided into three objectives, which include analysis of the availability and performance of credit, the relationship of credit terms on organization performance and effects of interest rate on capacity.

5.1 Summary of Findings

Together, the three variables accounted for 37.5% of performance ($R^2 = 0.375$). This indicates that credit availability plays an essential part; however, other elements matter as well. The loan officers brought up issues like currency differences and the difficulties involved in recovering loans from Kenya, which are examples of border-related issues. Lack of collateral poses a significant challenge. SME owners lack finance skills. Being flexible is crucial. They recommended developing superior products, government intervention, and SME training.

5.2 Discussion of Findings

This section looks at how the findings relate to what other researchers found before.

5.2.1 Credit Availability and Performance

The study has found out that there is a moderately positive correlation between the ease of obtaining loans and the performance of SMEs ($r = 0.445$). The findings support Beck & Demirgüç-Kunt (2020), who noted that loan availability contributes to 28% to 35% of the performance of SMEs in developing countries. The findings of this study fall within this range.

There is an average level of ease to access physical services offered by banks in Busia ($M = 4.12$). However, loan sizes tend to be low, while time required for processing the loans tends to be long. It is consistent with the observation made by IFC (2021), which noted the existence of “availability deserts” whereby the banks exist, but their offerings do not fit the needs of people. Similarly, the challenges highlighted in this research were found in the border areas of Uganda-Kenya, where businesses keep accounts in two countries.

5.2.2 Credit Terms and Performance

The credit terms emerged to be the most significant variable (Beta=0.348) and correlated ($r=0.512$). This is in agreement with Abor and Biekpe (2021), who observed that interest rates greater than 25% negatively impact performance. In Busia, the effective interest rate tends to exceed 25%, and respondents noted that high interest rates result in lower profitability (4.18).

Difficulties in Collateral Availability (M=2.45) were consistent with Berger and Udell (2020), who indicated that 65% of loan denials emanate from collateral in developing nations. Banks in the study are attempting to utilize group guarantees and warehouse receipt guarantees, similar to those in Ghana where the International Finance Corporation (IFC) (2021) indicated that such measures had increased lending by 40%. However, in Uganda, just 15% of small and medium enterprise loans

Repayment period (mean = 2.58) and grace period (mean = 2.18) are problematic. According to Hansen and Hamilton (2020), 70% of SME loans in East Africa are below 12 months while the investments need 24 months, which means the borrower will be forced to take on expensive refinancing. In Busia, high interest rates with flexibility in repayment (3.42) are preferred, just like in the case reported by FSD Kenya (2022), who reported that flexible loans earn 35% more profits.

Lack of transparency in fees (mean = 2.89) and overall cost (mean = 2.77) is a problem. According to Uganda Microfinance Regulatory Authority (2023), the effective rate is 8% higher

5.2.3 Interest Rate and Performance

Interest rate correlation ($r=0.468$) should be analyzed cautiously. It can either mean that better interest rates contribute positively to performance, or vice versa, better firms can access better interest rates. According to Stiglitz and Weiss (2021), such a relationship is complicated because high interest lowers profitability (4.18) and shortens the perspective (4.11). According to World Bank (2022), an increase in the interest rate by 5% reduces investment by 12%. Kasozi and Nakayi (2021) found that the repayment of loans at a rate exceeding 25% is linked to a 40% probability of financial distress. This proves that cost is not the sole concern for SMEs. The low awareness of effective interest rates (2.54) correlates with Turyahebwa et al. (2023) research findings. The researchers revealed that while mobile lending services provide interest between 30% and 60%, around 35% of SMEs in Busia accessed such informal sources of financing due to

the urgency of the needs. While Pecking Order Theory postulates cost minimization, SMEs opt for informal lenders for the sake of flexibility.

5.3 Conclusions

5.3.1 Credit Availability

The credit accessibility in the Eastern Division is reasonable, but far from good. The banks are present, but loans are low, and procedures slow. Credit availability is important for the performance, yet its mere presence is not enough. Presence of banks alone cannot be considered accessibility when loan terms fail to suit businesses.

5.3.2 Credit Terms

Credit terms are most important. Interest rate, collateral requirements, repayment period, grace period etc. associated with borrowing impact the ability of SMEs to utilize loan money efficiently. Even with provision of loan facilities, negative credit terms prevent SMEs from developing further. Improvement of terms must be the main priority.

5.3.3 Interest Rate

The interest rate significantly influences performance. It reduces profit margins and creates a mindset that only cares about the here and now. Despite all this, however, most small business owners do not really comprehend what they pay. Some people prefer to borrow from unprofessional sources because of the ease and speed it offers, not for price reasons.

5.4. Recommendations

5.4.1. For Banks and Microfinance

- i. Create loan facilities for border entrepreneurs. Enable loans and repayments to be in Ugandan and Kenyan currency. Allow repayment according to the trading cycle instead of months.
- ii. Accept different kinds of collateral such as warehouse receipts, machinery, vehicles. Apply group lending strategy for sums above 2 million.
- iii. Provide a grace period of 3 to 6 months after which repayment begins. Business should be able to utilize funds and generate income prior to repaying the loan.

For Government

Initiate a credit guarantee facility. Where the government shares the risk, banks would extend loans to SMEs without collateral.

Ensure that the movable property registry operates smoothly. Allow SMEs to pledge movable assets such as goods and equipment, like they do in Ghana.

Require that banks reveal interest rates truthfully. Penalize them for concealment.

Cooperate with Kenya on facilitating cross-border financing. Same regulations, information exchange, and interconnection of payments.

For SME Owners

- i. Establish a credit guarantee scheme. If the government takes part in the risk, banks will provide loans to SMEs without collateral.
- ii. Make sure that the movable asset registration system is working well. SMEs will be allowed to use their movable assets as collateral, just like they do in Ghana.
- iii. Force banks to disclose interest rates honestly. They should not hide anything.
- iv. Work together with Kenya to help cross-border financing. Same laws, same information sharing, same linkages between payment systems.

5.5 Contribution of the study

- i. It describes the features of credit accessibility within a border town context, something not commonly addressed by previous researchers.
- ii. It confirms that credit conditions, rather than bank proximity, are crucial.
- iii. It highlights that despite the cost involved; SMEs seek flexibility in terms of credit arrangements.
- iv. It highlights other credit-related challenges such as time and relationship management.

5.7 Areas of further Research

Comparison between border towns within Uganda and Kenya.

Research on cross-border traders alone and their specific finance needs.

Research on mobile money services and digital loans.

5.8 Chapter Summary

The research established that credit accessibility has an impact on the performance of SMEs within Busia. The importance of credit conditions, credit availability, and interest rates were in that order of importance and explained 37.5% of the variation in performance.

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APPENDICES

Appendix A: Questionnaire for SME Owners/Managers

Questionnaire on Credit Accessibility and Financial Performance of SMEs in Eastern Division, Busia Municipality

Dear Respondent,

My name is Nekesa Morine. I am a student at Uganda Christian University performing a research study titled, "Credit Availability and Financial Performance of Small and Medium-Sized Enterprises in Eastern Division of Busia Municipality." The aim of this survey is to collect data for research purposes only. All your answers will remain confidential.

SECTION A: DEMOGRAPHIC AND BUSINESS CHARACTERISTICS

Please tick (✓) the appropriate response or fill in the blank.

Gender: Male Female

Age bracket: 18-25 years 26-35 years 36-45 years 46-55 years 56 years and above

Education level: No formal education Primary level Secondary level
Tertiary/University

Business sector: Retail trade Wholesale trade Agro-processing Cross-border trade
 Small-scale manufacturing Other (specify) _____

Years of business operation: Less than 1 year 1-3 years 4-6 years 7-10 years
Above 10 years

Number of employees: 1-5 employees 6-10 employees 11-25 employees 26-50 employees
Above 50 employees

Have you ever accessed credit from a formal financial institution?

Yes No

If yes, which type of financial institution? Commercial bank Microfinance institution
SACCO Other (specify) _____

SECTION B: CREDIT AVAILABILITY

Please indicate the extent to which you agree or disagree with the following statements using the scale:

1 = Strongly Disagree (SD), 2 = Disagree (D), 3 = Neutral (N), 4 = Agree (A), 5 = Strongly Agree (SA)

No.	Statement	SD	D	N	A	SA
B1	There are sufficient financial institutions offering loans to SMEs in Eastern Division					
B2	Financial institutions in Busia offer a variety of loan products suitable for my business					
B3	The loan application process is simple and straightforward					
B4	Loan application processing time is reasonable (within 2 weeks)					
B5	Financial institutions are willing to lend to businesses like mine					
B6	The loan amounts offered are adequate for my business needs					
B7	Financial institutions have branches conveniently located near my business					
B8	Loan officers are easily accessible for consultation					

SECTION C: CREDIT TERMS

Please indicate the extent to which you agree or disagree with the following statements using the scale:

1 = Strongly Disagree (SD), 2 = Disagree (D), 3 = Neutral (N), 4 = Agree (A), 5 = Strongly Agree (SA)

No.	Statement	SD	D	N	A	SA
C1	The interest rates charged on loans are affordable					
C2	Collateral requirements are reasonable and flexible					
C3	The loan repayment period is long enough for my business to generate returns					
C4	There is flexibility in repayment schedules					
C5	Grace periods are provided before loan repayment begins					
C6	Loan processing fees and other charges are clearly explained					
C7	The total cost of borrowing (including all fees) is transparent					
C8	Financial institutions accept alternative collateral					

SECTION D: Interest rate

Please indicate the extent to which you agree or disagree with the following statements using the scale:

1 = Strongly Disagree (SD), 2 = Disagree (D), 3 = Neutral (N), 4 = Agree (A), 5 = Strongly Agree (SA)

SECTION D: INTEREST RATE

Please indicate the extent to which you agree or disagree with the following statements using the scale:

1 = Strongly Disagree (SD), 2 = Disagree (D), 3 = Neutral (N), 4 = Agree (A), 5 = Strongly Agree (SA)

No.	Statement	SD	D	N	A	SA
D1	The interest rate charged on my loans is affordable for my business operations.					
D2	High interest rates significantly reduce my business profit margins.					
D3	I fully understand the difference between the advertised interest rate and the effective interest rate					
D4	I prefer loans with higher interest rates but more flexible repayment schedules.					
D5	The current interest rates allow me to invest in growing my business					
D6	Interest rate fluctuations (instability) make it difficult for me to plan my business finances.					
D7	I have rejected loan offers because the interest rates were too high.					
D8	Using loans with high interest rates forces me to focus on short-term trading rather than long-term business growth.					

SECTION E: FINANCIAL PERFORMANCE

Please indicate the extent to which you agree or disagree with the following statements using the scale:

1 = Strongly Disagree (SD), 2 = Disagree (D), 3 = Neutral (N), 4 = Agree (A), 5 = Strongly Agree (SA)

No.	Statement	SD	D	N	A	SA
E1	My business revenue has increased over the past three years					

E2	My business profits have grown consistently					
E3	I have been able to reinvest profits back into the business					
E4	My return on investment has improved					
E5	I have been able to expand my business operations					
E6	My business has hired additional employees					
E7	My business assets have increased in value					
E8	I have been able to serve more customers					

Thank you for your participation!

Appendix B: INTERVIEW GUIDE FOR LOAN OFFICERS

Interview Guide for Loan Officers on Credit Accessibility and SME Financial Performance in Eastern Division, Busia Municipality

Introduction:

Nekesa Morine is my name, and I am studying at Uganda Christian University. I am doing research on credit availability and financial performance of small and medium enterprises in the Eastern Division. Your contribution as a loan officer would help me get an insight into the supply side of credit for SMEs.

Section A: Background Information

Name of financial institution: _____

Your position: _____

Years of experience in SME lending: _____

Section B: Credit Availability

What is your institution's experience with lending to SMEs in Busia's Eastern Division?

What are the main criteria your institution uses to assess SME loan applications?

What challenges do SMEs in this border area face in accessing credit from your institution?

How does your institution determine loan amounts for SMEs?

Section C: Credit Terms

How does your institution determine interest rates for SME loans?

What are your collateral requirements, and do you accept alternative forms of collateral?

What repayment periods do you typically offer to SMEs, and why?

How do you address the unique needs of cross-border traders regarding loan terms?

Section D: Credit Monitoring

How does your institution monitor SME loans after disbursement?

Do you provide any business advisory support or training to SME borrowers?

How effective do you find your monitoring practices in ensuring loan repayment?

What challenges do you face in monitoring SMEs in a border area?

Section E: SME Financial Performance

Based on your experience, how does credit accessibility affect SME financial performance?

What differences have you observed between SMEs that access credit and those that don't?

What recommendations would you make to improve credit accessibility for SMEs in Busia?

Thank you