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Effect of Microfinance Credit on the Financial Performance of Micro, Small and Medium Enterprises in Muhanga District, Rwanda

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Abstract

The purpose of this study was to examine the effects of microfinance credit on the financial performance of Micro Small and medium enterprises in Muhanga district, Rwanda This study was guided by the following research objectives: To assess the effects of microfinance credit on the MSMEs Return on capital, to analyze the extent of the microfinance credit improve the financial performance of micros mall and medium enterprise in Muhanga district, to determine how microfinance credit affect the growth of micro small and medium enterprises, to establish the reason why the microfinance credit is less popular in the Muhanga district an ex-post facto research design was used; both stratified and random sampling techniques were used to select 50 respondents out of 58 MSMEs with questionnaire and observation guide as the main data tools while document analysis was used in secondary data. Data were analyzed using both descriptive and inferential statistical methods. These findings strongly reveal there is an effect of microfinance credit on the financial performance of MSMEs. The positive relationship between microfinance credit and financial performance of MSMEs may reflect how MSMEs need to access microfinance credit and the government should put into consideration the rules and regulations that facilitate MSMEs to access easily the microfinance credit. This study concluded that High interest rate, credit ceiling have been mentioned as one of the challenges in accessing credit facilities of MFIs. However, this study indicated that MFIs have had a positive effect on the financial performance of MSMEs in Muhanga District, Rwanda.

Key words: *microfinance credit, financial performance micro, small and medium enterprises*

Introduction

1.1 Background to the Study

In recent years, both developed and developing countries support for MSMEs development and growth has increased. This is because of the contribution of MSMEs to the employment creation.

Evidence shows that a dynamic and growing MSMEs sector can contribute to the achievement of a wide range of development objectives, including: the attainment of income distribution and poverty reduction as noted by (DFID, 2000); creation of employment which was echoed by (Daniels &Ngwira, 1993); savings mobilization as opinioned by (Beck et al., 2005); and production of goods and services that meet the basic needs of the poor as noted by (Cook &Nixson, 2000), Phillips &Kirchhoff (1989) cited by Pasanen (2006) found that young firms that grow have twice the probability of survival as young non-growing firms. It has been also found that strong growth may reduce the firm's profitability temporarily, but increase it in the long run (Pasanen, 2003). The growth of MSMEs is believed to be a desirable end as the key drivers of employment and economic development.

In a study done in India by Stuti Kacker (2013) asserted that, MSMEs have been almost established in all major sectors in the Indian industry such as food processing, Agricultural inputs, Chemicals and pharmaceuticals, Textiles, plastic products and Computer software. MSMEs are known for innovations as new product with good quality service as well it also provides employment opportunities. It is also known as backbone of the company. MSMEs constitute above 80% of total number of industrial enterprise and from the backbone of development. Not only in India but across the world MSMEs provides incredible contribution to the economy. MSMEs have above more than 40% share in industries, producing more than 8000 value-added products which contribute nearly 35% direct export and up to 45% in the export. After agriculture MSMEs is one of the biggest employment providing sector which provide employment nearly 28.28 million people. (Stuti Kacker, Ministry Small Scale industries 2013**).**

According to Peprah & Muruka (2010:52), echoed by Brune (2009:6), Lindsay (2010:3), and Nwigwe et al. (2012:34) micro-finance institutions aim at reducing poverty worldwide among financially excluded people. Suberu et al. (2011:253), stated that micro-finance institutions have a grass roots orientation and greater expertise in financing smaller enterprises.

Small and medium enterprises (SMEs) are considered to be the key engine of the economic development according to (Chittithaworn, Islam & Keawchana, 2011; Ionita, et al, 2009; Deros, Yusof & Salleh, 2006). The relative importance of the SME sector varies greatly across countries, whereby SMEs have been known to make important economic contributions, whether in developed or developing countries. A number of large enterprises develop from SMEs and some of them even rely on SMEs.

In most parts of the continent of Africa, people are suffering from severe lack of basic needs, and therefore there is need to talk about the need to reduce poverty. The argument behind the introduction of micro finance institutions was to bring people out of poverty and into better living standards with the focus of being able to meet their basic needs. Because the poor will always be with us, it is more attainable and measurable to enable the poor people access the basic needs like shelter, food and water than to simply make a goal of reducing poverty cited by (Yunus, 2007). Macro, Small and Medium enterprises are the backbone of many economies in Sub-Saharan Africa (SSA) and hold the key to possible revival of economic growth and the elimination of poverty on a sustainable basis. Despite the substantial role of the SMEs in SSA's economies, they are denied official support, particularly credit, from institutionalized financial service organizations that provide funds to businesses. According to, these enterprises account more than one – half of the economic activities of the countries within the sub- region, by contributing about 12% and 34% of rural and urban employment activities in Tanzania. Numerous evidences have pointed to the fact that the number of these enterprises in Tanzania is declining at an alarming rate and little has been achieved in Tanzania, despite of the many efforts done to fight for poverty reduction noted by (Hamisi Madole, 2013).

Perkowski (2012:1) asserted that access to finance is a challenge for businesses in any country. Entrepreneurs in developing countries require micro-credit and other services from micro-finance institutions for several reasons; to speedily expand their operations, for start-up capital, for working capital or for other purposes. Providing micro-credit and other services to small and medium enterprises has traditionally been challenging for micro-finance institutions. On the one hand, the challenge may be related to a lack or non-existence of financial history and the inability to provide required collateral among small and medium enterprises. On the other hand the absence of credit bureau data and regulatory bodies at national level is challenging. In addition, Suberu et al. (2011:254) stated that a shortage of both debt and equity financing is one of the major barriers to rapid development of the small and medium enterprises.

Kibet et al, (2015) noted that with the introduction of MFI's in Tanzania is seen as the best alternative source of financial services for low income earners and their MSMEs as a means to raise their income, hence reducing their poverty level and contributing in country economy as asserted by (Kessy & Urio, 2006). The service of microfinance institution to majority of Tanzanians who are low income earners have created opportunity to them including managing scarce household and enterprises resources more efficiently, protection against financial risks by taking advantages of investment opportunities and gaining economic returns as echoed by (Chijoriga, 2000). Micro finance enables clients to protect, diversify and increase their incomes, as well as to accumulate assets, reducing their vulnerability to income and consumption shocks (Robinson, 2002).

MSMEs in Kenya have the tendency to serve as sources of livelihood to the poor, create employment opportunities, generate income and contribute to economic growth. They have been seen as the means through which accelerated growth and rapid industrialization have been achieved according to (Koech, 2011). MSMEs have been recognized as socio-economic and political development catalysts in both developed and developing economies as noted by (Mwangi, 2011). Maalu, et al. (1999) discussed the role of Small and Medium Enterprises in the economy of Kenya and noted the important role it has played and continues to play, as being employment creation and income generation, the study noted other important roles in the economy such as production of goods and services and development of skills.

Small and Medium Enterprises have huge potential for employment generation and wealth creation in any economy, yet the sector has stagnated and remains relatively small in terms of its contribution to GDP or to gainful employment according to (FSD Kenya, 2007). Beck, Demirguc,Kunt, & Maksimovic (2004) determined the financing obstacles faced by firms in over 10,000 sampled firms from 80 countries established that SMEs are faced with higher financing constraints than larger and older firms as part of the reason that limits their growth. In addition, small and medium enterprises have been forced to make extensive reports to financial institutions when applying for finances and at the same time, agree with more restrictive asset usage as noted by (Zeller & Sharma, 2000).

Even though the definitions of "SMEs‟ come in variation, the importance of SMEs in the contemporary global economy has demonstrated the shift of emphasis towards SMEs in all countries according to (Olomi, 2009). This is justified by both the quantitative and qualitative contributions of SME sections to the well –being of a nation's economy. Their effects can be seen in a number of areas, including providing job opportunities for the workers, distributing income, alleviating poverty, providing a training ground for the development and upgrading entrepreneurship skills, and serving as important vehicles for promoting forward and backward linkages in geographically diverse sectors of the economy in many countries (ibid). According to a World Bank report (2016) 600 million jobs are needed across Africa in the next 15 years to absorb a growing global workforce. Most formal jobs in emerging markets are with small and medium enterprises (SMEs), which also create 4 out of 5 new positions and yet more than 50% of SMEs lack access to finance, which hinders their growth.

According to MINECOFIN (2007), In Rwanda microfinance emerged in the 1980s in response to the poor results achieved through state delivered subsidized credit to poor farmers. Evidence began to show that low-income people could be credit-worthy and save money, if enabled to access tailored financial services. This shift in development thinking presented low-income people not as a focus for charity but rather as partners in development. In 2008, the Law Nº 40/2008, regulating the organization of microfinance sector activities was published in the Official Gazette. It was followed by the Central Bank's instruction 02/2009.

Micro Small and Medium Enterprises (MSMEs) are commonly believed to have very limited access to deposits, credit facilities and other financial support services provided by Formal Financial Institutions (FFIs). This is because these MSMEs cannot provide the necessary collateral security demanded by these formal institutions and also, the banks find it difficult to recover the high cost involved in dealing with small firms. In addition to this, the associated risks involved in lending to MSMEs make it unattractive to the banks to deal with micro and small enterprises (World Bank, 1994). Statistically, small enterprises are reported to have high failure rates making it difficult for lenders to assess accurately the viability of their enterprises, the abilities of the entrepreneur, and the likelihood of repayment.

MSMEs in Rwanda have the tendency to serve as sources of livelihood to the poor, create employment opportunities, generate income and contribute to economic growth.

Micro-finance, on the other hand, according to Otero (1999) is not just about providing capital to the poor to combat poverty on an individual level, it also has a role at an institutional level. It seeks to create institutions that deliver financial services to the poor, who are continuously ignored by the formal banking sector.

According to MINICOM (2010), MSMEs Definition, MSMEs are to be considered based on the following conditions (in line with the World Bank report of 2004) whereby two of the three conditions must be met. For the avoidance of doubt, in this policy when using the popular term “MSME”, it is taken to include micro enterprises as well as small and medium enterprises. Registered cooperatives may also benefit from this policy in so far as they are SMEs.

TABLE1. 1: MICRO, SMALL AND MEDIUM ENTERPRISES IN RWANDA

Size of the Enterprise	Net capital investments (Million RwF)	Annual Turnover (Million RwF)	Number of Employees
Micro Enterprises	Less than 0.5	Less than 0.3	1 to 3
Small Enterprises	0.5 to 15	0.3 to 12	4 to 30
Medium Enterprises	15 to 75	12 to 50	31 to 100
Large Enterprises	More than 75	More than 50	More than 100

Source: Secondary data, February 2018

However, Muhanga District most owners of MSMEs invest mostly on agriculture and industries to sustain its economy. The managers and owners of these MSMEs access credit from different microfinance institutions. Although; this cannot be achieved without removing barriers that hinder MSMEs from accessing credit facilities from financial institutions. Despite these contributions of MSMEs, their major barriers to financial performance and development appear to be shortage of both equity financing and debt.

1.2 Statement of the problem

Ideally access to financial services can boost job creation, raise income, reduce vulnerability and increase investments in human capital. MSMEs account for a significant share of employment and GDP around the world, but, when they have limited access to finance, the economy suffers a series of negative consequences: Economic and social opportunities are restricted, enterprise creation and growth are restrained, households and enterprises are more vulnerable to threats, and payments are costlier and less safe.

Unfortunately in Muhanga, the risk of start-up or expansion and the burden of taxation and other regulations have made even entrepreneurs who see opportunities in the market find it hard to bring those ideas into reality due to potential of failures. This challenge is exacerbated by the fact that financial institutions find it too high risk to lend to MSMEs given the cost/benefit ratio in terms of time and resources required to process MSME loans as well as the difficulties most SMEs face in consolidating capital and creating business plans to become viable lending candidates. This creates a blockage to growth where MSMEs that have the skills to scale-up or move into manufacturing and processing are constrained due to their limited access to finance, even if they are willing to assume the risk.

Several studies have been carried out both internationally and locally on the factors that influence lending to SMEs. For example, in a study by wanambisa, A. N & Bwasi,H.M (2013) on Effects of Microfinance Lending on Business Performance: A Survey of Micro and Small Enterprises in Kitale Municipality, Kenya, found that the amount of loans is significantly and positively related with performance of MSEs in Kitale Municipality, also the amount of loan given by MFIs to MSMEs should be increased to enable the MSMEs grow to medium scale enterprises. In yet another study by Akinyi, S.I (2014) on the effect of bank financing on the financial performance of small and medium-sized enterprises in Nairobi County, Kenya found that bank financing and SMEs’ size positively affected the SMEs’ financial performance while SMEs tangibility had an inverse relationship with the SMEs’ financial performance. However, in a study done by Barungi, F. & Gashija,F (2017) on contribution of business development fund to the financial access by small and medium enterprises in Rwanda, found that Small and medium sized enterprises in Kigali city and the southern Province have easy access to finance.

The majorities of the SMEs in these areas are given loan guarantees, and are trained in business investment; however, the majorities do not receive mentorship and business advisory services from BDF. This study therefore, examines the Effects of Microfinance Credit on the financial performance of Micro small and medium Enterprises in Muhanga District, Rwanda

Most studies on MSMEs performance, growth and development acknowledge that lack of credit is the greatest constraint that SMEs face. Nonetheless, majority of the studies focus on the factors that influence the performance of SMEs and determinant of SMEs growth and conclude that access to credit is utmost problem, which if solved can help mitigate the other factors. As such, most of these studies deviate from an in-depth analysis of the financial challenge facing SMEs. Instead, the studies give recommendations to SMEs and other stakeholders on how to mitigate or solve the financing problem without determining the factors that influence access to credit. Moreover, there is no comprehensive study on the Effects of Microfinance Credit on the financial performance of Micro small and medium Enterprises in Muhanga District, Rwanda.

1.3 Objectives of the study

1.3.1 General Objective

i. To examine the effects of microfinance credit on the financial performance of micro small and medium enterprise in Muhanga district,

1.3.2 Specific Objectives

To ensure an in-depth research is done in this study, the researcher investigates the following objectives:

i. To assess the effects of microfinance credit on the MSMEs Return on capital,
ii. To analyze the extent of the microfinance credit improve the financial performance of micros mall and medium enterprise in Muhanga district,
iii. To determine how microfinance credit affect the growth of micro small and medium enterprises,
iv. To establish the reason why the microfinance credit is less popular in the Muhanga district.

1.3.3 Research questions:

To provide direction to this study, the researcher developed research questions from the objective of the study. By answering the following research questions the objective of this study was achieved

i. What are the effects of microfinance credit on the MSMEs Return on capital?
ii. To what extent does the microfinance credit improve the financial performance of micro small and medium enterprises?
iii. How does microfinance credit affect the growth of micro small and medium enterprises?
iv. Why is it that the microfinance credit is less popular in the Muhanga district?

1.4 Research Hypothesis

H_1. There is a relationship between microfinance credit and MSMEs Return on capital
H_2. There is a relationship between microfinance credit and financial performance of MSMEs.
H_3. There is a relationship between microfinance credit and growth of MSMEs
H_4. There is a relationship between microfinance credit and popularity of microfinance Credit in Muhanga district.

1.6 Significance of the Study

1.6.1Significance to MFIs

This study was centered on the activities of MFIs and their contributions to the development of macro small and medium size businesses in Muhanga, Rwanda

1.6.2 Significance to MSMEs

Microfinance as a whole provides the average Rwandan a means to have access to financial services in their localities to boost their living standards in a sustainable manner in line with the millennium development goal of alleviating poverty in developing countries. The study assist MFIs to adopt the necessary measures needed to ensure the desired growth in the SME industry.

1.6.3 Significance to the Government

For a country to grow, the government should actively promote business enterprises. Among business enterprises, the Micro Small and Medium Enterprises (MSME) deserve special attention. Though MSMEs are small investment enterprises, but their contribution to the Country economy is very significant.

1.6.4 Significance to Policy makers

This study is significance to the policy makers as they develop roadmaps to the Inter-Ministerial Committee for Accelerating Manufacturing in Micro, Small and Medium Enterprises made recommendations on (a) the promotion of start-ups (b) facilitating operation and growth (covering credit, technology, and marketing) (c) closure and exit (d) labor laws and regulations.

1.6.5 Significance to Others

This study is also be very important to other researchers who will be doing more research in the areas of MFIs and MSMEs as it will also help them come up with more recommendations on the area under the study.

LITERATURE REVIEW

2.1 Review of theories

Critical review of theory

The study is anchored by three theories namely: Microfinance Credit Theory, Credit Access theory and Theory of Financial Intermediation and other relevant theoretical literature which shows the effect of microfinance credit on the financial performance of MSME's.

2.1.1 Microfinance Credit Theory

Microfinance in Kenya is now fully fledged sector. (Dondo, 1999) traced the history of MFIs in Kenya to the mid-1950s when the joint Loan Board Scheme was established to provide credit to indigenous Kenyans with small trading business loans. The Microfinance Institutions in sector in Kenya has grown since it inceptions in the 1970s and is one of the most established in Africa (Kashangaki et al, 1999). The birth of specialized microfinance in Kenya was in the 1980s when Kenya Rural Enterprises Fund (K-REP) and the Kenya Women Finance Trust (KWFT) were established. In the 1990s more MFIs emerged for example Faulu Kenya, Small and Medium Enterprise Program commonly known as SMEP and Jamii Bora

The concept of group lending is commonly heralded as the main innovation of microfinance and claims to provide an answer to the shortcomings of imperfect credit markets, in particular to the challenge of overcoming information asymmetries. Information asymmetries may lead to the distinct phenomena of adverse selection and moral hazard. In the case of adverse selection, the lender lacks information on the riskiness of its borrowers. Riskier borrowers are more likely to default than safer borrowers, and thus should be charged higher interest rates to compensate for the increased risk of default (Rahman, 2010).

Accordingly, safer borrowers should be charged less provided each type can be accurately identified. Since the lender has incomplete information about the risk profile of its borrowers, higher average interest rates are passed on to all borrowers irrespective of their risk profile. In moral hazard generally refers to the loan utilization by the borrower that is the lender cannot be certain a loan, once disbursed, is used for its intended purpose, or that the borrower applies the expected amounts of complementary inputs, especially effort and entrepreneurial skill, that are the basis for the agreement to provide the loan. If these inputs are less than expected then the borrower may be less able to repay it (Rahman, Davanzo & Sutradhar, 2006)

The standard model of lending commonly contains two mechanisms which address the issue of information asymmetries: assortative matching or screening to deal with adverse selection, and peer monitoring to overcome moral hazard. Early models were developed by (Stiglitz, 1990), (Swain, 2008).These models examined how group liability schemes resolve moral hazard and monitoring problems. Other models developed by (Rafiq et al, 2009). (Gangopadhyay et al. 2005) were inspired by (Stiglitz & Weiss, 1981) and focused on adverse selection and screening mechanisms. Moreover, social ties among group members, i.e. social connections in the language of (Anand&Kanbur, 1993), also referred to as social capital; appear to play an important role in the context of group liability schemes in terms of enhancing repayment behaviour, as theorized by (Pisani &Yoskowitz, 2010).

2.1.2 Credit Access Theory

The credit theory was postulated by Stiglitz & Weiss (1981), they provided a framework for analyzing financial market inefficiencies. This framework provides that information asymmetry is the main cause of financial market malfunctioning in developing countries. Financial institutions that advance loans to economic agents are not only interested in the interest they receive on loans, but also the risks of such loans.

Most financial institutions screen and monitor borrowers more efficiently than other investors can. They are specialized in gathering private information and treating it. Managing money and deposit accounts, banks own highly strategic information on firms‟ receipts and expenditures as well as the way that firms develop (Kashyap, Stein & Wilcox, 1993).Despite this plethora of information, relationships between bankers and firms are not perfect. Banks suffer from informational asymmetries such that evolution of prices (interest rates) cannot clear the credit market. Finally, non- Walrassian equilibrium arises with a fringe of unsatisfied agents (Pinaki, 1998).

In reference to (Stiglitz & Weiss, 1981) adverse selection and thus credit rationing still occurs if banks require collateral. They argue that low-risk borrowers expect a lower rate of return on average. Thus, they are less wealthy than high-risk borrowers on average after some periods. Low-risk borrowers are therefore not able to provide more collateral. Increasing collateral requirements may have the same adverse selection effect as a higher interest rate. Instead Walsh (1998) argues that banks only offer contracts in which they simultaneously adjust interest rates and collateral requirements. He proved that there is always a combination of interest rate and collateral requirements so that credit rationing does not occur (Jaffee& Russell, 1996).

The proponents of this theory argue that the most interesting form of credit rationing is equilibrium rationing, where the market has fully adjusted to the public whereby banks ration credit free, available information and where demand for loans for a certain market interest rate is greater than supply.(Stiglitz & Weiss, 1981) explains that credit rationing occurs if a financial institution charge the same interest rate to all borrowers, because they cannot distinguish between borrowers and screening borrowers perfectly is too expensive.

Both assumptions are very simplifying and do not occur in this manner in the real world. Banks are usually able to distinguish their borrowers up to a certain degree.

2.1.3 The Theory of Financial Intermediation

According to the theory of intermediation, current theories of the economic role of financial intermediaries build on the economics of imperfect information that began to emerge during the 1970s with the seminal contributions of Akerl of (1970) & Spence, 1973) and (Bernanke & Blinder, 1992).Financial intermediaries exist because they can reduce information and transaction costs that arise from an information asymmetry between borrowers and lenders. Financial intermediaries thus assist the efficient functioning of markets, and any factors that affect the amount of credit channeled through financial intermediaries can have significant macroeconomic effects (Spence, 1973).

There are two strands in the literature that formally explain the existence of financial intermediaries. The first strand emphasizes financial intermediaries‟ provision of liquidity. The second strand focuses on financial intermediaries‟ ability to transform the risk characteristics of assets. In both cases, financial intermediation can reduce the cost of channeling funds between borrowers and lenders, leading to a more efficient allocation of resources. (Bernanke &Gertler1995) analyzed the provision of liquidity and the transformation of illiquid assets into liquid liabilities by banks. In (Adolfson2002) model, depositors are risk averse and uncertain about the timing of their future consumption needs. Banks can improve on a competitive market by providing better risk sharing among agents who need to consume at different times.

An intermediary promising investors a higher payoff for early consumption and a lower payoff for late consumption relative to the non-intermediated case enhances risk sharing and welfare. The optimal insurance contract in (Claus & Smith, 1999).Financial model is a demand deposit contract, but it has an undesirable equilibrium, in which all depositors panic and withdraw immediately, including even those who would prefer to leave their deposits in the bank if they were not concerned about the bank failing (Adolfson, 2002).

The proponents of this theory explain that the modern theory of financial intermediation, financial intermediaries are active because market imperfections prevent savers and investors from trading directly with each other in an optimal way.

The most important market imperfections are the informational asymmetries between savers and investors. Financial intermediaries, banks especially, fill as agents and as delegated monitors' information gaps between ultimate savers and investors. They screen and monitor investors on behalf of savers to ensure the sustainability of financial intermediation, safety and soundness regulation has to be put in place (Bernanke & Blinder, 1992).

2.2 Determinants of Financial Performance

There are various determinants of financial performance of a firm

2.2.1 Growth of the firm

Growth of the firms is an essential determinant of the firm, growth of the firm is attributable to increase in net assets. Firms are a collection of a certain number of resources that provide the means to successfully take advantage of those opportunities and grow (Pinaki, 1998). Formal there is no limit to the growth of the firms; it is the rate of growth what is limited in the short run but there is no limit to the size of the firm.

2.2.2 Size of the Firm

The other determinant of financial performance of commercial and services firm is the size of the firm. Large firms are more likely to manage their working capitals more efficiently than small firms. Most large firms enjoy economies of scale and thus are able to minimize their costs and improve on their financial performance (Kumar, 1995).Firm size is determinant of investment behavior and access to capital and liquidity management in SME‟s (Raheman and Nasr, 2007). Smaller firms exhibit larger degrees of information asymmetry between insiders and outsiders. In addition, these firms also face higher costs in issuing new equity (Sebastian 2010).

There are a number of ways that can be used in measuring the size of a firm. Sales turnover is one of the measures that can be used. Sales turnover (Sales revenue) is the money that you get from the sale of products and thus the costs of sales have not been deducted from this. Number of employees, is one of the simplest measures to know about the size of the firm, capital employed by a business may and can vary depending in the size of the business. A small business will need less capital to finance its investment, whereas, a large business enterprise will need a lot of capital to plan and finance the investments (Pandey, 2005)

2.2.3 Age of the Firm

Age is a key determinant of financial performance of the firm. The period of operation that a firm has been in operation highly determines the financial performance of the firm. Firms that have a vast experience in the market are able to gain economies of scale from the suppliers and other stakeholders of the firm as a result of good relationships and trust. Such a firm is more likely to perform better than a firm that is new in an environment. The firm might spend a lot of money before it gets adapts to the environment (Santalo & Becerra, 2008).

2.2.4 Liquidity of the Firm

Liquidity of the firm is a key determinant of the firm's financial performance Liquidity risk can be measured by two main methods: liquidity gap and liquidity ratios. The liquidity gap is the difference between assets and liabilities at both present and future dates (Pelg, 2006). Liquidity ratios are various balance sheet ratios which should identify main liquidity trends. These ratios reflect the fact that firm should be sure that appropriate, low cost funding is available in a short time. This might involve holding a portfolio of assets that can be easily sold cash reserves, minimum required reserves or government securities (Santalo & Becerra, 2008).

2.2.5 Debt

Debt is a determinant of financial performance of SME‟s. Debt is funds borrowed from a financial institution at a certain percent of interest rates which should be paid within a specified period of time. It is appropriate for the firm to maintain a proper balance between debt and equity. The firms leverage decisions centers on the allocation between debt and equity on financing a firm (Raheman et al., 2007). The emphasis on long-term finance and on the potentially adverse consequences when it is in short supply is somewhat at odds with recent theoretical contributions that emphasize the fact that the use of short-term debt may be associated with higher quality firms and may have better incentive properties. In particular, the possibility of premature liquidation may act as a discipline device that improves firms' performance (Kashyap, Stein & Wilcox, 1993).

2.3 Empirical Review

This section present review of international, regional as well as national

2.3.1 International

Soumadi & Hayajneh (2012) conducted a study on the relationship between capital structure and corporate performance on Jordanian shareholdings firms. The study used multiple regression models by least squares (OLS) to establish the link between capital structure and corporate performance of firms over a period of 5 years. The results showed that capital structure was associated negatively and statistically with the performance of the firms in the sample. Another finding from the study was that there was there was no significant difference to the impact of financial leverage between high financial leverage firms and low financial leverage firms in their performance. The study also concluded that the relationship between capital structure and firm performance was negative for both high growth firms and low growth firms.

Maritala (2012) examined the optimal level of capital structure which enabled a firm to increase its financial performance. The study found that there was a negative relationship between the firm's debt ratio and financial performance measured by return on assets and return on equity.

Ahmad, Abdullar & Roslan (2012) carried a study in Malaysia which sought to investigate the impact of capital structure on firm performance by analysing the relationship between return on assets (ROA), return on equity (ROE) and short-term debt and total debt. The study established that short-term debt and long-term debt had significant relationship with ROA. It was also established that ROE had significant relationship with short-term debt, long-term debt and total debt. In a study conducted by, Cecchetti et al. (2011) on the effects of debt on firms and concluded that moderate debt level improves welfare and enhances growth but high levels can lead to a decline in growth of the firm. Over borrowing can lead to bankruptcy and financial ruin (Ceccetti et al., 2011). High levels of debt will constrain the firm from undertaking project that are likely to be profitable because of the inability to attract more debt from financial institutions.

However, Rainhart & Rogoff (2009) argued that debt impact positively to the growth of a firm only when it is within certain levels. When the ratio goes beyond certain levels financial crisis is likely to happen. The sentiment was also echoed by Stern Stewart and Company which argues that a high level of debt increases the probability of a firm facing financial distress.

2.3.2 Regional reviews

In a study conducted in Kenya with some scholars have different views. In astudy done by Kinyua (2014) on the role of finance, management skills, macro-environment factors and infrastructure have on the performance of small and medium-sized enterprises, which sought to evaluate the factors affecting the performance of SMEs in the Jua Kali sector in Nakuru town. Found that financing had the potential to positively affect the performance of SMEs.

In yet another study by, Namusonge, Mairura & Karanja (2013) in their survey on the role of financial intermediation in the growth of SMEs in Kenya showed that the financial intermediaries played a significant role by offering banking services and extending credit facilities to SME businesses. Other support offered by financial intermediaries included; advisory services, training and financing the start of businesses. The existing evaluation procedures adopted by financial intermediaries were a big hindrance to credit access because they were stringent and bureaucratic was further revealed by the study. Finally they also found out that evaluation procedures made it difficult for businesses to access support from financial institutions because the procedures wasted a lot of business time and made financial intermediaries' services inaccessible to most businesses

Osoro & Muturi (2013) concludes that accessibility to credit affects financial performance of small and medium enterprises positively. The easier it is to access credit, the higher the financial performance of the Small and medium enterprises. However, they also indicate that access to credit is not that easier from the financial institutions considering the many requirements one has to meet before the credit is approved to the entrepreneur for use in the business? The results showed that as credit becomes more available, the financial performance of business becomes better and hence a chance for business growth (Osoro & Muturi, 2013).

Another study conducted by Atieno (2009) found that SMEs in Kenya that participate in business associations have better access to bank loans. In addition, membership to associations is important for SMEs as they facilitate access to financial services. Thus institutions, such as associations, which support the SME's capacity to access financial services, become an important avenue for strengthening SMEs.

However, Nondi & Achoki (2006), in a survey of financial management problems in small hotels and restaurants in Kenya, found that 26 percent of these establishments reported lack of working capital as the most serious problem they face in their operations. Their findings differ with those of Namusonge, Mairura & Karanja (2013), who also conducted a survey in the same country but on financial intermediaries.

2.3.3 National Review

In a study done by Barungi, F. & Gashija, F. (2017), the purpose of this study was to assess the contribution of the Business Development Fund to the ease of access to finance among Small and Medium Enterprises in Kigali city and the Southern Province. With purposive sampling used to sample the districts and convenience sampling for the SMEs. The study used structured questionnaires and interview guides as the primary data collection tools, their study adopted mixed method approach and found that, Small and medium sized enterprises in Kigali city and the southern Province have easy access to finance. The majorities of the SMEs in these areas are given loan guarantees, and are trained in business investment; however, the minorities do not receive mentorship and business advisory services from BDF. BDF has to some extent contributed to the ease of access to finance among the SMEs at majorly one front; this is the provision of advisory services (investment and business advisory).

2.4 Conceptual Framework:

The study adopted a conceptual framework that explained the effects of influence of microfinance credit on the financial performance of MSMEs in Muhanga District, Rwanda. There are independent variables and dependent variables.

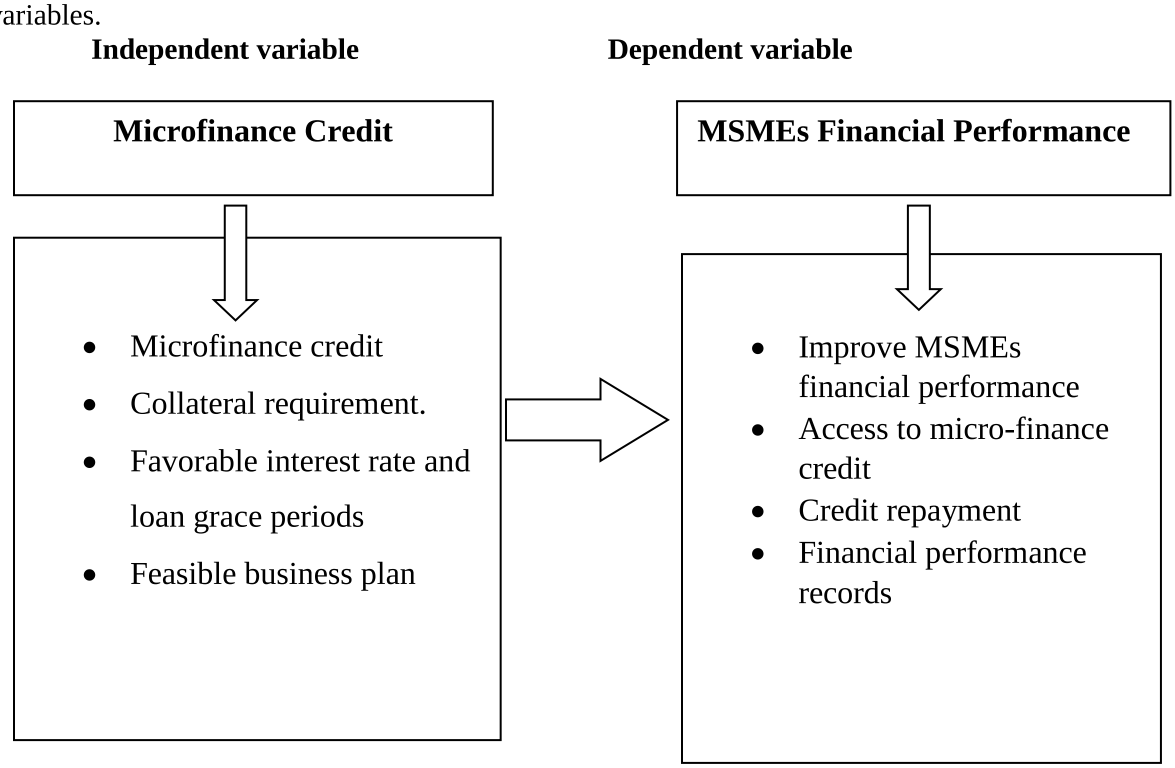


FIGURE 2. 1: **CONCEPTUAL FRAMEWORK**
Source: *Researcher, (2018)*

RESEARCH METHODOLOGY

3.1 Research Design

This study was guided by an ex-post facto design. This research design was employed because it was not possible to ethically or physically control the variables and it was not also possible to conduct an experimental design on this study. The design was used to ascertain the relationship between microfinance credit on the financial performance of Micro Small and medium enterprises in Muhanga district, Rwanda.

3.2 Study Population

According to Frankel & Wallen (2000), a population refers to the group to which the results of the research are intended to apply. They stated that a population is usually the individuals who possess certain characteristics or a set of features a study seeks to examine and analyze. Kumekpor (2002), emphasized this by defining a population as the total number of all units of the issue or phenomenon to be investigated into which is "all possible observations of the same kind" Target population for this study will be 58 MSMEs from micro, small and medium enterprises with probability sampling procedures on 50 MSMEs in Muhanga district, Rwanda. The target population is chosen because they are the key informant who will be able to give information which will guide the researcher in making informed conclusion on the relationship between microfinance credit on the financial performance of Micro Small and medium enterprises in Muhanga district, Rwanda.

TABLE 3. 1: POPULATION AND SAMPLE SIZE

Population category	Population size	Sample size
Tailoring	15	14
Welders	5	4
Mechanics	5	4
Carpenters	8	7
Hairdressers	10	9
Vegetables Sellers	10	9
Restaurant	5	4
Total	**58**	**50**

Source: *Researcher, (2018)*

3.3 Sampling

Purposive sampling was used to get data from MSMEs in Muhanga district because they were deemed to be key informants for the study. In purposive sampling techniques, subjects are selected based on the judgment of the researcher. The study therefore consisted of a sample size of 50 respondents.

3.4 Data Collection Methods and Tools

3.4.1 Primary data source

Primary data were collected using observation guide and questionnaire which were both closed ended and open ended with two parts part one has section A which is contain background information such as age of respondent, gender, level of education and number of year of experience. Part two has section B to E which is be based on research question, this part was in form of a Likert scale anchored by a five- point rating ranging from strongly disagree=1 to strongly agree=5, 10 MSMEs were interviewed because they couldn't answered the questionnaire.

3.4.2 Secondary data Source

Secondly data were collected by use of document analysis that were obtained from literature sources or data collected by other sources for example county annual work plan (AWP), and annual county budgets which is give information regarding the county plan on development in the county and the county estimated revenue and expenditure.

Questionnaire was administered to: Tailoring, welders, Mechanics, Carpenters and hairdressers, while observation guide was used to vegetables sellers because a researcher observed what happen on the ground and document analysis was used to Restaurant. This research is quantitative in nature; the data were collected for period of two Months.

3.4.3 Validity and reliability of the research instruments

3.4.3.1 Validity of the research instruments

To measure validity of research instrument the researcher used expert judgments; this is by relying on groups of individuals with specialist skill set, training or experience in the subject matter relevant to the activity being performed.

3.4.3.2 Reliability of the Research Instrument

The researcher is enhance the reliability of the data collected by ensuring that the questionnaires are pretested before being administered to the sample group. The instrument was piloted using 8 business owners who are not be part of the sample before they are administered. From the piloted instruments, reliability is be determined. Data reliability, which is a measure of internal consistency and average correlation, is measured using Cronbach's alpha coefficient that ranges between zero and one (Kipkebut, 2010) .Higher alpha coefficient values means there is consistency among the items in measuring the concept of interest. As a rule of thumb acceptable alpha should be at least 0.60 and above (Hair *et al*., 2006).

3.5 Data processing

The data collection techniques that were employed for the research included the use of structured questionnaires. The questionnaires were used for the collection of data from the entrepreneurs from MSMEs in Muhanga District. The questionnaire embodied both open and closed-ended questions for randomly selected members of the various groups. A survey questionnaire is designed to apply to a heterogeneous sample selected from the large population of SMEs according to (Burns, 2000). A questionnaire is defined as a formalized schedule or form which contains an assembly of carefully formulated questions for information gathering as noted by (Wong, 1999). The questionnaire was structured in three broad areas that included general information, a rating on the effect of MFIs credit on the MSMEs capital, To what extent does the microfinance credit improve the financial performance of MSMEs, Effect of micro finance credit to the growth of MSMEs. The variables on the key objectives of the study will be measured in interval scales on a five point Liker scale (1-representing strongly agree to 5– strongly disagree) to determine respondents agreement with the concepts under investigation. Data were processed using the SPSS version 20.

3.6 Data analysis

To ensure easy analysis, the questionnaires were coded according to each variable of the study. This study used descriptive and inferential statistics. According to McDanile & Gates (2001), descriptive analysis involves a process of transforming a mass of raw data into tables, charts, with frequency distribution and percentages, which are a vital part of making sense of the data. In this study, the descriptive statistics such as percentages and frequency distribution were used to analyze the demographic profile of the participants.

FINDINGS

The aim of this study was to find out the effect of microfinance credit on MSMEs financial performance.

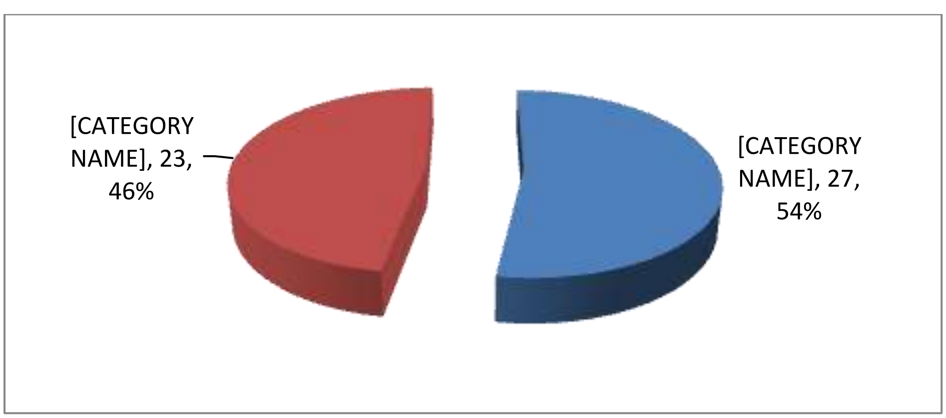
4.1 Demographic Data of the Respondents

The entrepreneurs were asked to indicate their gender, age bracket, educational background and work experience on the questionnaire.

4.1.1 Gender of the respondents

In order to know the population of the research demographic presentation were used, the Results showed that 27(54%) of the entrepreneurs were male, while 23 (46%) were female. The low number of female entrepreneurs is attributed to the attitude of the locals towards access to credit.

FIGURE4. 1: GENDER OF RESPONDENTS



Source: Primary data, February 2018

4.1.2 Age bracket of the respondents

Results also showed that entrepreneurs 14(28%) were less than 30 years, 24 (48%) were 30-40 years, 9 (18%) were 41-50 years, while only 3 (6%) reported to be 51 years and above. This implies that all categories of entrepreneurs were involved in answering the study research questions.

TABLE 4. 1: Age bracket of the respondents

Category	Frequency	Percent
Less than 30 years	14	28.0
30-40 Years	24	48.0
41-50 Years	9	18.0
51 years and above	3	6.0
Total	**50**	**100.0**

Source: Primary data, February 2018

4.1.3 Marital status of the respondents

The results showed that 29(58%) of the respondents are married, 16 (32%) are single, 0(0%) are divorced none of respondents is divorced, 5(10%) are widows (ers). This shows that most of entrepreneurs are married in this study.

TABLE 4. 2: MARITAL STATUS OF THE RESPONDENTS

Category	Frequency	Percent
Married	29	58.0
Single	16	32.0
Divorced	0	0.0
Widow(er)	5	10.0
Total	**50**	**100.0**

Source: Primary data, February 2018

4.1.4 Academic qualifications of the respondents

The findings showed that the respondents are divided into 4 categories such as primary level, secondary level, bachelor’s degree and others. Hence 7(14%) have primary level, 31(62%) have secondary level, 9(18%) have bachelor’s degree, and 3(6%) have other level, this implies that most entrepreneurs have secondary level in this study.

TABLE 4. 3: ACADEMIC QUALIFICATIONS OF THE RESPONDENTS

Category	Frequency	Percent
Primary level	7	14.0
Secondary level	31	62.0
Bachelor’s degree	9	18.0
Others	3	6.0
Total	**50**	**100.0**

Source: Primary data, February 2018

4.2 Analysis of the results

This part concerns the analysis of the results on the effect of microfinance credit on the financial performance of MSMEs in Muhanga district, Rwanda.

4.2.1 Types of the business of the respondents

The Results showed that 4 (8%) of the MSMEs are restaurant, 4 (8%) are welders, 7 (14%) MSMEs are carpentry, 4 (8%) are mechanics, 13 (26%) are Tailoring, 9 (18%) are hairdressers, while 9 (18%) are vegetables sellers. In this study Tailoring, hairdressing and vegetable selling MSMEs had many respondents compared to others MSMEs because in Muhanga district there are many hairdressers and many vegetable sellers.

TABLE 4. 4: TYPES OF THE BUSINESS OF THE RESPONDENTS

Category	Frequency	Percent
Restaurant	4	8.0
Welders	4	8.0
Carpentry	7	14.0
Mechanics	4	8.0
Tailoring	13	26.0
Hairdressers	9	18.0
Vegetable sellers	9	18.0
Total	**50**	**100.0**

Source: Primary data, February 2018

4.2.2 Experience of the Respondents

Results also showed entrepreneurs experience, 15(30%) have less than 2 years of experience, 18 (36%) have 2-5 years of experience, 11(22%) have 6-8 years of experience, while 6 (12%) reported to have above 8 years of experience. This implies that most entrepreneurs have two and above years of experience.

TABLE 4. 5: EXPERIENCE OF THE RESPONDENTS

Category	Frequency	Percent
Less than 2 Years	15	30.0
2 - 5 Years	18	36.0
6 - 8 Years	11	22.0
Above 8 Years	6	12.0
Total	**50**	**100.0**

Source: Primary data, February 2018

4.2.3 Ownership of the Business

The Results showed that 47 (94%) of the entrepreneurs were the owners of the businesses, while 3 (4%) were not the owners, they are employees. In this study the respondents were almost the owners of businesses.

TABLE 4. 6: OWNERSHIP OF THE BUSINESS

Category	Frequency	Percent
Yes	47	94.0
No	3	6.0
Total	**50**	**100.0**

Source: Primary data, February 2018

4.2.4 Knowledge of Microfinance Institutions

The findings indicated that 48 (96%) entrepreneurs knew microfinance institutions, 1(2%) entrepreneur does not knew microfinance institutions, while also 1(2%) is not sure, in this study most of the respondents knew microfinance institutions.

TABLE 4. 7: KNOWLEDGE OF MICROFINANCE INSTITUTIONS

Category	Frequency	Percent
Yes	48	96.0
No	1	2.0
Not sure	1	2.0
Total	**50**	**100.0**

Source: Primary data, February 2018

4.2.5 Having an account in Microfinance Institutions

The findings indicated that 43 (86%) entrepreneurs had an account in microfinance institutions, while 7 (14%) entrepreneurs did not have an account in Microfinance Institutions, they have accounts in commercial banks, but in this study also most of the respondents had an account in microfinance institutions.

TABLE 4. 8: HAVING AN ACCOUNT IN MICROFINANCE INSTITUTIONS

Category	Frequency	Percent
Yes	43	86.0
No	7	14.0
Total	**50**	**100.0**

Source: Primary data, February 2018

4.2.6 Application of a credit in Microfinance Institution

The results showed that 38 (76%) entrepreneurs applied for a credit in microfinance institutions, while 12 (24%) entrepreneurs did not apply for a credit in Microfinance Institutions, seven of them have accounts in commercial while other five entrepreneurs have accounts in Microfinance institution but they didn't apply for a credit, in this study most of the respondents applied for a credit in microfinance institutions.

TABLE 4. 9: APPLICATION OF A CREDIT IN MICROFINANCE INSTITUTION

Category	Frequency	Percent
Yes	38	76.0
No	12	24.0
Total	**50**	**100.0**

Source: Primary data, February 2018

4.2.7 Receiving a credit from Microfinance Institution

The results showed that 36 (72%) MSMEs received a credit from microfinance institutions, while 14 (28%) MSMEs did not receive a credit from Microfinance Institutions, There are two MSMEs who applied but they did not receive a credit because of missing some requirements such us collaterals, security deposit *(dépôts de grantie "French"),* insufficient deposits and repayment capacity.

TABLE 4. 10: RECEIVING A CREDIT FROM MICROFINANCE INSTITUTION

Category	Frequency	Percent
Yes	36	72.0
No	14	28.0
Total	**50**	**100.0**

Source: Primary data, February 2018

4.2.8 How easy was it to access this credit from the Microfinance?

The findings showed that 9(18%) received a credit from microfinance very easy, 21(42%) MSMEs received a credit moderately easy, 4(8%) MSMEs received credit with some difficulties, 2(4%) MSMEs received credits very difficultly, 14(28%) entrepreneurs did not receive credits from Microfinance institutions they did not answer this question but some of them said it is easy but the credit ceiling is a problem. This implies that Microfinance institutions do not complicate the process of credit to MSMEs as it is shown by the findings, when MSMEs have all requirements the process is easy.

TABLE 4. 11: HOW EASY WAS IT TO ACCESS THIS CREDIT FROM THE MICROFINANCE?

Category	Frequency	Percent
Very easy	9	18.0
Moderately easy	21	42.0
With some difficulties	4	8.0
Very difficult	2	4.0
Neutral	14	28.0
Total	**50**	**100.0**

Source: Primary data, February 2018

4.2.9 How long does it take to receive the credit?

The findings showed that 0(0.0%) MSMEs receive microfinance credit in less than 2 weeks, 31(62%) received a credit from microfinance institutions between 2-3 weeks period, 4(8%) entrepreneurs received a credit from microfinance institution in one month, 1(2%) entrepreneur received a credit from microfinance institution in period of over one month, 14(28%) entrepreneurs did not receive credits from Microfinance institutions, this implies that Microfinance institutions credit process is 2-3 weeks to MSMEs. Evidently none of the respondents take less than two weeks to access credit facility from the MFIs; this may be due to the documentation and authentication of documents associated with the accessing of credit facilities such as mortgage registration, notifying contracts, and other certificates.

TABLE 4. 12: PERIOD TAKES TO ACCESS CREDIT

Category	Frequency	Percent
Less than 2 weeks	0	0.0
2 - 3 weeks	31	62.0
1 Month	4	8.0
Over one month	1	2.0
Neutral	14	28.0
Total	**50**	**100.0**

Source: Primary data, February 2018

4.2.10 How often do you apply for a credit?

The Results showed that 13(26%) entrepreneurs do not apply for a credit from microfinance institutions often, 16(32%) entrepreneurs apply for a credit from microfinance institutions often, 7(14%) MSMEs apply for a credit from microfinance institutions very often, 14(28%) MSMEs did not apply for credit from Microfinance institutions, this also implies that MSMEs apply for a credit from microfinance institutions often. And those who apply for credit very often they usually use overdraft and short term credits.

TABLE 4. 13: HOW OFTEN DO YOU APPLY FOR A CREDIT?

Category	Frequency	Percent
Not often	13	16.0
Often	16	32.0
Very often	7	14.0
Neutral	14	28.0
Total	**50**	**100.0**

Source: Primary data, February 2018

4.2.11 Amount accessed by MSMEs as a credit over the last five years

The findings showed that in **2013** 14 MSMEs accessed the credit; 5 MSMEs accessed less than 500,000 Rwandan francs credit, 6 MSMEs accessed between 500,000-1,000,000 Rwandan francs credit, one of the MSMEs accessed between 3,000,000-4,000,000 Rwandan francs credit, none of the MSMEs accessed between 2,000,001-3,000,000; 4,000,001 - 5,000,000 and above 5,000,000 credit in **2013**.

In **2014** 16 MSMEs accessed the credit; 3 MSMEs accessed less than 500,000 Rwandan francs credit, 6 MSMEs accessed between 500,000-1,000,000 Rwandan francs credit, 3 MSMEs accessed between 1,000,001 - 2,000,000 Rwandan francs credit, 2 MSMEs accessed between 2,000,001-3,000,000 Rwandan francs credit, 1 of the MSMEs accessed between 3,000,001-4,000,000 Rwandan francs credit, one of the MSMEs accessed between 4,000,001-5,000,000 Rwandan francs credit, none of the MSMEs accessed above 5,000,000 credit in **2014**.

In **2015** 18 MSMEs accessed the credit; 5 MSMEs accessed less than 500,000 Rwandan francs credit, 5 MSMEs accessed between 500,000-1,000,000 Rwandan francs credit, 4 MSMEs accessed between 1,000,001 - 2,000,000 Rwandan francs credit, 3 MSMEs accessed between 2,000,001-3,000,000 Rwandan francs credit, none of the MSMEs accessed between 3,000,001-4,000,000 Rwandan francs credit, one of the MSMEs accessed between 4,000,001-5,000,000 Rwandan francs credit, none of the MSMEs accessed above 5,000,000 credit in **2015.**

In **2016** 23 MSMEs accessed the credit; 4 MSMEs accessed less than 500,000 Rwandan francs credit, 7 MSMEs accessed between 500,000-1,000,000 Rwandan francs credit, 3 MSMEs accessed between 1,000,001 - 2,000,000 Rwandan francs credit, 3 MSMEs accessed between 2,000,001-3,000,000 Rwandan francs credit, 2 of the MSMEs accessed between 3,000,001-4,000,000 Rwandan francs credit, 3 MSMEs accessed between 4,000,001-5,000,000 Rwandan francs credit, one of the MSMEs accessed above 5,000,000 Rwandan francs credit in **2016.**

In **2017** 24 MSMEs accessed the credit; 3 MSMEs accessed less than 500,000 Rwandan francs credit, 9 MSMEs accessed between 500,000-1,000,000 Rwandan francs credit, 5 MSMEs accessed between 1,000,001 - 2,000,000 Rwandan francs credit, 1 of the MSMEs accessed between 2,000,001-3,000,000 Rwandan francs credit, 3 of the MSMEs accessed between 3,000,001-4,000,000 Rwandan francs credit, 1 MSMEs accessed between 4,000,001-5,000,000 Rwandan francs credit, 2 MSMEs accessed above 5,000,000 Rwandan francs credit in **2017.**

From 2013 to 2017 the number of MSMEs accessed credit has increased as it is shown by the table below from 14 MSMEs in 2013 to 24 MSMEs in 2017, over the 5 years; 20 MSMEs accessed less than 500,000 Rwandan Francs credit, 33 MSMEs accessed between 500,000-1,000,000 Rwandan Francs, 17 MSMEs accessed between 1,000,001-2,000,000 Rwandan Francs credit, 9 MSMEs accessed between 2,000,001-3,000,000 Rwandan Francs credit, 7 MSMEs accessed between 3,000,001-4,000,000 Rwandan Francs credit, 6 MSMEs accessed between 4,000,001-5,000,000 Rwandan Francs credit, 3 MSMEs accessed above 5,000,000 Rwandan Francs credit over 5 years. Many MSMEs Accessed between 500,000-1,000,000 as it is shown by the findings, but the amount MSMEs accessed has increased from 2013 to 2017.

TABLE 4. 14: AMOUNT ACCESSED BY MSMES AS A CREDIT OVER THE LAST FIVE YEARS

Category	2013	2014	2015	2016	2017	Total
Less than 500,000	5	3	5	4	3	**20**
500,000 - 1,000,000	6	6	5	7	9	**33**
1,000,001 - 2,000,000	2	3	4	3	5	**17**
2,000,001 - 3,000,000	0	2	3	3	1	**9**
3,000,001 - 4,000,000	1	1	0	2	3	**7**
4,000,001 - 5,000,000	0	1	1	3	1	**6**
Above 5,000,000	0	0	0	1	2	**3**
Total	**14**	**16**	**18**	**23**	**24**	**95**

Source: Primary data, February 2018

4.2.12 Microfinance Credit and return on capital increment

The findings showed that 32(64%) MSMEs strongly agreed that Microfinance credit has increased their capital, while 4(8%) MSME also agreed that Microfinance credit has increased their capital, 14(28%) MSMEs did not receive credits from Microfinance institutions they did not answer this question. This implies that Microfinance credit have a great effect to the financial performance of MSMEs, especially to the return on invested capital increment

TABLE 4. 15: MICROFINANCE CREDIT AND RETURN ON CAPITAL INCREMENT

Category	Frequency	Percent
Strongly agree	32	64.0
Agree	4	62.0
Disagree	0	0.0
Strongly disagree	0	0.0
Neutral	14	28.0
Total	**50**	**100.0**

Source: Primary data, February 2018

4.2.13 Working capital before microfinance finance credit application

Only 4(8%) MSMEs responded that they had enough working capital before they apply for Microfinance credit, 46(92%) MSMEs responded that they did not have enough capital before they apply for Microfinance credit. Most of MSMEs apply for a credit to increase their working capital because they always want money for purchasing Raw materials and the goods to be sold.

TABLE 4. 16: WORKING CAPITAL BEFORE MICROFINANCE FINANCE CREDIT APPLICATION

Category	Frequency	Percent
Yes	4	8.0
No	46	92.0
Total	**50**	**100.0**

Source: Primary data, February 2018

4.2.14 Accessibility to Microfinance credit and its influence to the financial performance of MSMEs

The findings showed that 31(62%) MSMEs accessibility to microfinance credit have influenced their financial performance to the very great extent, 3(6%) MSMEs accessibility to microfinance credit have influenced their financial performance to the great extent, while 2(4%) MSMEs accessibility to microfinance credit have influenced their financial performance to the moderate extent, 14(28%) MSMEs didn't answer this question because they didn't access microfinance credit, this implies that Microfinance credit has a meaningful influence to the financial performance of MSMEs.

TABLE 4. 17: ACCESSIBILITY TO MICROFINANCE CREDIT AND ITS INFLUENCE TO THE FINANCIAL PERFORMANCE OF MSMES

Category	Frequency	Percent
Very great extent	31	62.0
Great extent	3	6.0
Moderate extent	2	4.0
Little extent	0	0.0
Negligible extent	0	0.0
Neutral	14	28.0
Total	**50**	**100.0**

Source: Primary data, February 2018

4.2.15 Product diversification after receiving Microfinance credit

According to the table 19, it is apparent that most MSMEs after receiving the Microfinance credit diversified their products range in stocks. 33(66%) MSMEs indicated that they had actually boosted their business by purchasing different products, while only 17(34%) MSMEs indicated that they did not diversified their products range. This can be attributed to the fact that some MSMEs don't use the loan for its intended purpose and in most cases end up failing to repay the loan.

TABLE 4. 18: PRODUCTS DIVERSIFICATION AFTER RECEIVING MICROFINANCE CREDIT

Category	Frequency	Percent
Yes	33	66.0
No	17	34.0
Total	**50**	**100.0**

Source: Primary data, February 2018

4.2.16 Microfinance credit and improvement of financial performance of MSMEs

The findings showed that 32(64%) MSMEs strongly agreed that Microfinance credit has improved their financial performance, while 4(8%) MSME also agreed that Microfinance credit has improved their financial performance, 14(28%) MSMEs did not receive credits from Microfinance institutions they did not answer this question. This implies that Microfinance credit have a great improvement to the financial performance of MSMEs, especially to the capital increment, profitability, working capital increment and return on investment. One of the respondents replied that "*Mbere tutaramenya iby'inguzanyo ubucuruzi bwacu bwari hasi cyane nta nyungu twabonaga yewe twanaranguraga bitugoye kandi tukarangura utuntu duke kuburyo kunguka byabaga bigoye ariko nyuma yo gufata inguzanyo ibyo ducuruza byariyongerye kandi tubona inyungu nyinshi ihagije*" Before we get microfinance credit our business was not doing well, we didn't make a profit, even purchasing items for resale was very difficult, we purchased few quantities and making a profit was very difficult indeed, however, after receiving microfinance credit we had realized increase in purchasing power and we are now making enough profit.

TABLE 4. 19: MICROFINANCE CREDIT AND IMPROVEMENT OF FINANCIAL PERFORMANCE OF MSMES

Category	Frequency	Percent
Strongly agree	32	64.0
Agree	4	62.0
Disagree	0	0.0
Strongly disagree	0	0.0
Neutral	14	28.0
Total	**50**	**100.0**

Source: Primary data, February 2018

4.2.17 Less popularity of Microfinance credit in Muhanga District

The findings showed that 21(42%) MSMEs responded that Microfinance credit is less popular in Muhanga district because of high interest rate, MFIs interest rate is high it is between 21% and 24% some MSMEs decide to apply for credit in commercial banks where there are fair interest, 11(22%) MSMEs said that Microfinance credit is less popular in Muhanga district because of ceiling level of credit, Microfinance has a ceiling which is between 2 and 10 million Rwandan francs this limits more MSMEs to apply for a credit in MFIs, 2(4%) MSMEs responded that Microfinance credit is less popular in Muhanga district because of complicated credit procedure,
3(6%) MSMEs responded that Microfinance credit is less popular in Muhanga district because of long credit procedure, 13(26%) MSMEs responded that Microfinance credit is less popular in Muhanga district because of reputation of MFIs, some people take MFIs as institutions for low income earners and the institutions of poor services this reputation also has a negative impact to the popularity of Microfinance credit, one of respondents replied that "*abantu ntibakunda ibi bigo by'imali iciriritse kuko bumva ko ari ibyo abakene n'abantu bashaka inguzanyo y'udufaranga duke*" Some people don't like MFIs they take them as institutions of poor people and those who want micro credits.

TABLE 4. 20: LESS POPULARITY OF MICROFINANCE CREDIT IN MUHANGA DISTRICT

Category	Frequency	Percent
High interest rate	21	42.0
Ceiling level of credit	11	22.0
Complicated credit procedure	2	4.0
Long credit Procedure	3	6.0
Reputation	13	26.0
Total	**50**	**100.0**

Source: Primary data, February 2018

4.2.18 level of satisfaction that MFIs services have contributed to the financial performance

Table 22 is showing that 23(46%) MSMEs said that microfinance credit services contributed to their financial performance most satisfactory, 8(16%) MSMEs said that microfinance credit services contributed to their financial performance very satisfactory, 5(10%) MSMEs said that microfinance credit services contributed to their financial performance most satisfactory. This implies that Microfinance credit have a great improvement to the financial performance of MSMEs, especially to the capital increment, profitability, working capital increment, return on investment, and return on assets.

Microfinance saving contribution to the MSMEs, 17(34%) MSMEs said that access to microfinance savings contributed to their financial performance most satisfactory, 12(24%) MSMEs said that access to microfinance savings contributed to their financial performance very satisfactory, 7(14%) MSMEs said that access to microfinance savings contributed to their financial performance satisfactory, this shows how savings is important to MSMEs in order to improve the financial performance, and sustainable development of MSMEs.

Percentage of MSMEs financial performance, 5(10%) MSMEs rated the percentage of their financial performance most satisfactory, 9(18%) MSMEs rated the percentage of their financial performance very satisfactory, 18(36%) MSMEs rated the percentage of their financial performance satisfactory, 4(8%) MSMEs rated the percentage of their financial performance moderately satisfactory. Most MSMEs rated their percentage satisfactory this implies that microfinance credit contributes a lot to the financial performance of MSMEs but it doesn't bring them to the top level as it is shown by the findings. one of respondents said "*Ubu business iragenda neza rwose ntakibazo gusa ntitutagera kurugero twifuza ariko inguzanyo yaradufashije cyane kuko twateye imbere kandi tubasha kubona inyungu tukanishyura neza inguzanyo, imisoro n'ibindi byose"* Now the business is going on well, there is no problem even if the business is not on the level we want but microfinance credit really helped us we have grown now, we are making profit and we are able to pay our credit, taxes, and other expenses.

TABLE 4. 21: LEVEL OF SATISFACTION THAT MFIS SERVICES HAVE CONTRIBUTED TO THE FINANCIAL PERFORMANCE

Note 1 =Less satisfactory; 2=moderately satisfactory; 3= satisfactory; 4=Very satisfactory and 5=Most satisfactory

Category	5	Percent	4	Percent	3	Percent	2	Percent	1	Percent
How satisfied has your access to credit services contributed to your MSMEs financial performance?	23	46.0	8	16.0	5	10.0	0	0.0	0	0.0
How satisfied has your access to savings contributed to your MSMEs financial performance?	17	34.0	12	24.0	7	14.0	0	0.0	0	0.0
What percentage can you Rate your MSMEs Financial Performance?	5	10.0	9	18.0	18	36.0	4	8.0	0	0.0

Source: Primary data, February 2018

4.3 Test of Hypothesis

4.3.1 Microfinance credit and MSMEs Return on Capital

From the model, R means the correlation coefficient. It shows the relation between the independent variable and the dependent variable. A positive coefficient means that when the independent variable increases, it causes an increase in the dependent variable. Also, a negative coefficient means that an increase in the independent variable leads to a decrease in the dependent variable. The results show that all the value in the correlation coefficient (R) is more than zero. With R being 0.514 means that when MSME receive microfinance credit, its capital increases. The results indicate that the predictor variable of microfinance credit has a significant relationship with the MSMEs Return on capital. Consequently, the null hypothesis was rejected since there is a relationship between microfinance credit and the MSMEs capital.

H_1 There is a relationship between microfinance credit and MSMEs capital

TABLE 4. 22: MODEL SUMMARY MSMES RETURN ON CAPITAL

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	0.514[a]	0.478	0.421	0.147

a. Predictors: (Constant), MSMEs capital

Source: Primary data, February 2018

4.3.2 Financial performance of the MSMEs

The results show that the correlation coefficient (R) is greater than zero. With R being 0.879 means that when microfinance credit increases, the financial performance of MSMEs also increases. The results indicate that the predictor variable of microfinance credit has a positive relationship with financial performance of MSMEs. Consequently, the null hypothesis was rejected.

H_2 There is a relationship between microfinance credit and financial performance of MSMEs.

TABLE 4. 23: MODEL SUMMARY FINANCIAL PERFORMANCE OF THE MSMES

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	0.879[a]	0.731	0.711	0.174

a. Predictors: (Constant), Financial performance of the MSMEs,

Source: Primary data, February 2018

4.3.3 Growth of MSMEs

The results show that the correlation coefficient (R) is more than zero. With R being 0.787 means that when microfinance credit increases, the growth of MSMEs also increases. The results indicate that the predictor variable of microfinance credit has a positive relationship with the growth of MSMEs. Consequently, the null hypothesis was rejected.

H_3 There is a relationship between microfinance credit and growth of MSMEs

TABLE 4. 24: MODEL SUMMARY GROWTH OF MSMES

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	0.787[a]	0.746	0.719	0.183

a. Predictors: (Constant), Grow of MSMEs

Source: Primary data, February 2018

4.3.4 Popularity of the microfinance credit

The results show that the correlation coefficient (R) is more than zero. With R being 0.516 means that when microfinance credit increases, the popularity of microfinance credit also increases. The results indicate that the predictor variable of microfinance credit has a strong positive relationship with the popularity of microfinance credit. Consequently, the null hypothesis was rejected

H_4. There is a relationship between microfinance credit and popularity of microfinance credit Muhanga district.

TABLE 4. 25 : MODEL SUMMARY POPULARITY OF MICROFINANCE CREDIT

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	0.516[a]	0.491	0.548	0.224

a. Predictors: (Constant), Popularity of microfinance credit

Source: Primary data, February 2018

RESULTS

Introduction

The general objective of the study was to examine the effects of microfinance credit on the financial performance of micro small and medium enterprise in Muhanga district; therefore, this section provides a summary of the major findings, conclusions and recommendations for future research direction.

5.1 Summary

The potential of using institutional credit and other financial services for poverty alleviation in Rwanda is quite significant. Rwandans are generally living healthier and wealthier lives. One of the fastest growing economies in Central Africa, Rwanda notched up GDP growth of around 8% per year between 2001 and 2014 According to (express the news, September 2017).

The MSMEs sector in made up of various sub-sectors such as; trade, Service, Manufacturing, agriculture and other artisan bodies. The research shows that the sector is hugely dominated (62%) by trade which is basically buying and selling. This, the researcher believes, is due to the fact that very little capital is needed to begin and operate such businesses and does not require any regulatory processes. Transacting business with MFIs comes with varying expectations from MSMEs.

When respondents were asked of their expectations before transacting with MFIs, it became apparent that, each respondent had his/her own expectation but were all converging to the point of acquiring credit, some of their expectations include: to access prompt credit; to be assured of getting credit on time and as and when needed; to access more funds to expand their business. The study employed an ex-post facto design. The sample was picked from all business categories in Muhanga district, Rwanda. Yamane formula (1973) was used to arrive at a sample of Fifty (50) Micro, Small and Medium Enterprises. Questionnaire was used as the principle tool for collecting primary data whereas the respondents provided financial statements in the case of secondary data. Data was analyzed using descriptive statistics and multiple regression approach. From the analysis the study revealed the following findings. The study found out that all MSMEs borrow to increase their financial performance

5.2 Conclusions

MFIs are concerned with provision of financial services to people who are economically poor and who therefore experience financial exclusion in that they do not have ready access to mainstream, commercial financial services. It is concerned with provision of financial services to poor people using means which are just, fair and sustainable for example they accept social collateral rather than financial collateral, access to larger amounts of loan if repayment is performance is positive, easy way to access finance in not much paper work, and easy and short procedures. A large number of Muhanga district residents derive their livelihood from the MSMEs. However in spite of the importance of this sector, experience shows that provision and delivery of credit services to the sector by formal financial institutions such as commercial banks and MFIs has been below expectation. This means that it is difficult for the poor to move out of poverty due to lack of finance for their productive activities.

Small-scale loans can relieve capital constraints that might otherwise preclude cash-strapped entrepreneurs from investing in profitable businesses, while savings services can create opportunities to accumulate wealth in safe repositories and to manage risk through asset diversification. As MSMEs grow they require funds to finance growth in fixed asset and increase working capital. MSMEs therefore require long-term credit in ever increasing amounts. MSMEs needs funds so that they can purchase raw materials supplies and carry out activities that they need to facilitate the production process.

The study found that all MSMEs borrow investment capital and they use it for the purpose in which they borrowed for, most of them do not have other source of financing other than from micro-finance institutions and they did not have other form of financing before they started receiving financing from microfinance institutions.

This study reveals that MFIs have a positive effect on the growth of the latter, notwithstanding the inherent challenges. It has been noted that, access to credit which is a major challenge in the MSME sector has been reduced to a large extent through the operations of MFIs. MFIs have also contributed largely in the area of mobilizing savings through their saving schemes that make saving more accessible, less costly and ready to receive little amounts. The habit of saving is enhanced as low income earners who were hitherto unable to save with traditional banks are offered an opportunity to save. The practice helps to improve capitalization as most of these saving are ploughed back in their businesses.

It is also critical to highlight the challenges that have the tendency of derailing the efforts of the MFIs in granting credit. Some of these are the inability of clients to repay their loans and the rate of credit misappropriation. It is worth noting that MFIs provide better access to credit than the traditional banks. However, the research reveals that a good number of MFIs require collateral security before loans are granted and this negatively affects the MSMEs as some are unable to provide the collateral requested. High interest rate has also been mentioned as one of the challenges in accessing credit facilities of MFIs. However, amidst these challenges, this research clearly indicates that MFIs have had a positive effect on the growth of MSMEs.

5.3 Policy Recommendations

There is need to provide an enabling environment for MSMEs to grow and thrive, therefore there is a need to develop strategies to enhance increased access to microfinance credit by MSMEs from commercial banks and microfinance institutions. It is important for the government to set up policies that will ease microfinance credit to MSMEs. These policies should be in line with both the owners of MSMEs and financial institutions in order to prevent putting hindrances to potential and credit worthy customers who seek to expand or start up a business. This will create a window for growth and development of the economy as a result of more job opportunities and increased flow of money circulation in the economy.

Financial institutions should ensure that they sensitize the owners of MSMEs on best financial management practices. This will help the owners of MSMEs to account for credit borrowed. Lending institutions should also advise borrowers on how to appraise their projects for viability to ensure that they make wise decisions when investing in projects.

The study recommends that MFIs partners with the government and other stakeholders so as to create awareness of the availability and the process of accessing microfinance credit. Since MFIs have poverty alleviation as its vision they should consider lending startup capital so that the welfare of the business and the borrower can be monitored.

The study recommends central bank should set policies and procedures to prevent barriers that inhibit potential owners and managers of MSMEs from accessing credit facilities. This will create a conducive environment for MSMEs to growth and expand. It will also open up opportunities for jobs and this will enhance economic growth. Financial institutions should also provide financial advisory services to individual proprietors when advancing credit to them; lower lending rates while improving service delivery and train people on risk management and financial management. The Government should also regulate financial institutions to ensure that the owners and managers of MSMEs get access to information in order to make the right investment decisions.

5.4 Suggestions for Further Study

This study focused on MSMEs in Muhanga District, Rwanda and therefore the findings of this study cannot be generalized to all the MSMEs in Rwanda. The study recommends that further research could be conducted on MSMEs countrywide to investigate on the effects of microfinance credit on financial performance of MSMEs to find out whether there are commonalities or unique factors. The concentrated on the MSMEs, it is important to carry out similar study among large enterprises in order to find out the effect of credit on performance of these firms. Further research should also focus on the different aspects of micro financing on the performance of MSMEs;

The role played by government policies on the performance and growth of MSMEs; and The effect of tax administration on performance of MSME's.

For the micro small and micro enterprises sector to grow, small businesses need to link with the rest of the economy. Most of these businesses are so small that creating a link seems almost impossible. Further research should be done in this area to establish the best way of linking Micro, Small and Medium businesses with large companies in the economy.

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