

EFFECT OF FINANCIAL STRUCTURE ON FINANCIAL PERFORMANCE OF SMES IN JINJA DISTRICT, UGANDA

^{1*} **Beatrice Nakiranda**

beatriceblessed@gmail.com

¹ *MBA Student, Mount Kenya University*

² *Senior Lecture, Mount Kenya University, Kenya*

^{2**} **Martin Onsiro Ronald**

mnsiro@mku.ac.ke

Abstract: *Despite the great entrepreneurial spirit, there is still a high mortality rate of Small and Medium-sized Entrepreneurs (SMEs) in Uganda which is particularly associated to the financial structure. This research therefore sought to analyze the effect of financial structure on financial performance of SMEs in Jinja District, Uganda. The study adopted Modigliani-Miller, trade-off and pecking order theories. A descriptive research design was adopted with a target of 340 owners of in Jinja district, Uganda. 181 SMEs were sampled of which 87% responded to the questionnaires. Data was collected using a questionnaire and analyzed using both descriptive and inferential statistics. Multiple regression analysis was used to draw inferences from the findings. All factors were found to be statistically significant ($p,0.05$) except data on borrowings and increase in cash to pay off liabilities. From the findings, owners' savings, contributions from loved ones, retained earnings, and borrowings have a positive but weak impact on financial performance of SMEs in Jinja District, Uganda. The study recommended for; maintenance of reserve levels for business continuity, the use of either long-term or short-term borrowings in addition to the use of cash, and hands-on training for entrepreneurs in financial matters such as credit management.*

Keywords: *Financial performance, Financial Structure, SMEs*

INTRODUCTION

Sustainable Development Goals (SDGs) have been a key focus among large corporations in the recent years but yet the contribution of SMEs to achievement of these SDGs cannot be under looked. This can be achieved by advancing inclusive and sustainable financial development, giving business and jobs, promoting supportable industrialization, and encouraging innovation, and decreasing income disparities (Organization for Economic Corporation and Development [OECD], 2017).

Additionally, SMEs are significant drivers of economies and social health for both financially advanced nations, economically emerging and developing nations. This is generally credited to their capacity to tackle joblessness issues through creation of employment opportunities for their citizens.

SMEs in the United States of America (USA) contribute to 52 % of the private work power and 51% of Gross Domestic Product (GDP) as indicated by Longenecker, Carlos and Petty (2012). As suggested by Sham (2014), the greater part of China's GDP is commanded by SMEs. In the United Kingdom (UK), 9.9% of all private sector business are SMEs with a combined annual turnover of 1.8 trillion pounds and overall, 47% of all private sector turnover (Small & Medium Enterprises (SME's), n.d.).

In developing economies such as Africa, SMEs make up the largest share of enterprises ranging from Agriculture to Information Communication and Technology (ICT) and tend to employ inferior sections of

women and youth. Definitely, African entrepreneurs and their private ventures are effectively adding to supply and production chains that will expand manufacturing base and kick start huge industrialization (Elumelu, 2017).

In East Africa, SMEs are likewise a critical driving force for economic development and growth. For instance, in Kenya, SMEs contribute to 50% of GDP (Kihimbo, Ayako, Omoka and Otuyo, 2012 and Ernst and Young, 2011). In Tanzania, the GDP contribution by SMEs is estimated at 33% (Ernst and Young, 2011). MSMEs in Rwanda 98%. Micro Small Medium Enterprises in Rwanda, n.d.).

In Uganda SMEs are considered the foundation of the economy providing substantial percentage of jobs especially for the young people as well as play contribute to government revenue through taxes (UMTIC, 2015).

Despite the potential contribution of SMEs to global economies, they face high failure rates in both advanced countries and those that are emerging for example on the African continent, the death rate is above 75% in the first year (Badagawa, 2011), In Uganda, about 40% fail within their first year of operation while 80% collapse after 5 years of operation (Ssempala, 2018). A number of factors that affect SME performance have been identified among which include but not limited access to financing, poor governance such as leadership styles, organization culture.

Various sources of financing reflect the diversity among SME characteristics and their needs, the choice of financial source is related to the stage the business has reached across the business growth cycle (Business Innovation Skills [BIS], 2012). Therefore, financial capital is an important factor to be considered across the stages of development of any business venture.

STATEMENT OF THE PROBLEM

In spite of the positive impact of SMEs to the economy and standards of living of people, they face a high mortality rate in which for more than 10,000 people who start business every year, about 40% of them fail within the birth year while 80% collapse after 5 years (Ssempala, 2018). This fact has sparked off concerns among various stake holders to determine the cause of this high mortality rate and propose solutions to mitigating it.

In the bid to determine factors contributing to the high mortality rate of SMEs, studies to establish factors that affect SME performance have been conducted for example Lakal (2018) made inquiry into why Ugandan firms avoid equity financing, Sempala (2018) studied the determinants of growth of MSMEs with focus in Rubaga Division, Kampala District, Ntayi (2014) examined the challenges and opportunities of the business environment in Uganda with a situational analysis under the Irish Center for Business Excellence (ICBE) funding, Abaho et al., (2016) studied performance of SMEs in Uganda in relation to their entrepreneurial ability, among others.

A critical reflection on research by Lakal (2018), Abaho et al., (2016) indicate a research gap and the need to carry out future research in other geographical places specifically in Jinja District to verify other studies that have been used to provide a general outlook of SMEs in Uganda. Therefore, this research sought to close the knowledge gap by exploring other factors that affect performance of SME with focus on effect of financial structure on financial performance.

STUDY OBJECTIVES

This research sought to assess effect of financial structure on financial performance and the following objectives guided the study.

- i) To assess effect of owner's savings and contributions from loved ones on financial performance of SMEs in Jinja District, Uganda.
- ii) To examine effect of retained earnings on financial performance of SMEs in Jinja District, Uganda.
- iii) To investigate effect of borrowings on financial performance of SMEs in Jinja District, Uganda.

LITERATURE REVIEW

Theoretical review

This research was informed by the Modigliani-Miller theory, the trading off theory and the pecking order theory. The Modigliani-Miller (MM) Theory was established in 1958 by Franco Modigliani and Merton Miller who proposed a flawless capital market where the market worth of a firm is irrelevant of its financial structure implying that the market value of a firm with a mix of debt and equity forms of financing equals the market value of an unlevered firm given that both firms fall within similar risk of business. The MM theory was of paramount importance to this study because its assumptions of a perfect economy were to be carefully used while explicitly considering a firm's transaction costs, taxation costs, flotation costs, bankruptcy costs so as to determine the relevance of the first and second proposition of MM theory to SMEs. The trade-off Theory conducted by Kraus and Litzenberger (1973) explains the idea that firms select amount of debt and equity finance to be used by balancing costs and benefits. The focus of trade-off theory suggests that the ideal capital mix happens when tax benefits and bankruptcy marginal costs balance. Thus, equity capital is less favored over debt capital by firms especially at the point where the cost of insolvency begins to be substantial. The importance of this theory was to clarify the fact that companies are financed both debt and equity; that debt is the preferred financing position of firms because of its associated tax benefits despite the financial and non-financial expenses that are related to debt. The Pecking Order hypothesis (1984,) was balanced by Stewart C. Myers and Nicolas Majluf, and it expresses that organizations rank their financing options from equity financing to debt financing as per the financing cost, wanting to raise value as a financing method for last resort.

Empirical Literature Review

Various research has been conducted by different scholars with the aim of investigating the effect of financial structure on financial performance of SMEs. Research by SAEED (2009) revealed that owner's money impacts on how SMEs perform while in-depth studies by Zarook, Rahman and Khanam, (2013) and SAEED (2009) demonstrate that, in addition to owner's savings and formal finance and business education is fundamental in SME performance.

Personal savings and Contributions from loved ones and financial performance

Oladele et al (2014) in their research affirm that about 96.4% of the finances necessitated by SMEs proprietors originated from individual savings where by 65.8% percent were personal savings in the banks while 30.6% were savings from daily contributions from loved ones, and these directly influenced performances of their businesses. Chioma and Ngozi (2014) discovered that in the vast majority of the African nations, loved ones steadily support each other's businesses thoughts by giving cash either legitimately to the business vision bearer or indirectly into the business by purchasing goods / services due to existing close relationships in place

while Macharia (2012) likewise articulated that financing of SMEs through family and friends aided entrepreneurs with average contribution of 40% of funds, commercial setups contributed average of 24% while reserves contributed average of 30% of funds. Oladele et al., (2014) also discovered that among the factors that can influence SME's performance, family and companions was the most critical one.

Retained earnings and financial performance

Findings of Timoshenko (2012) and Chepkemoi (2013), Wang (2013) and Kinyua (2014). Timoshenko (2012) revealed that firms that survived the primary growth period regularly switched funding options from personal savings to retained earnings. The primary role for this shift was to encourage business expansion and ultimately create business independence. Chepkemoi (2013) research also stated that SMEs in Kenya seriously depended on retained earnings to fund their interests in their early stages of inception. This was due to the fact that they were still young and had not established sufficient collateral to qualify for external financing. Wang's research conducted in 2013 states that SMEs in Taizhou, China previously financed their operations by obtaining funds from micro-finance setups. However, micro-financing kept losing popularity as SMEs resorted to usage of retained earnings (Wang, 2013).

Retained earnings and financial performance

Literature reviewed from various research reveals that borrowings can either have undesirable or positive influence on fiscal performance of a firm. Conclusions from research conducted by Ombongi and Long (2018), evidence that bank credit has positive effect on overall performance of a firm since personal savings, retained earnings are not enough to move SMEs from one level of growth to another. On the contrary, research by Karanja (2014) shows that debt capital negatively affects SME performance probably due to interest the business is obliged to pay to the lender despite of the profitability levels the business. It is therefore important for every firm to obtain a good asset base in order to improve its ability to obtain and pay back its credit. Kinyua (2014) however, indicates that financial performance of a firm is positively improved with debt capital particularly when equity capital is not adequate to acquire fixed assets of the firm which certainly improves financial performance.

Quality of information

Information is said to consist of facts and data, which are organized for a particular purpose; information quality is a major criterion for measuring the success of an information system, and decision quality is a function of information quality (Jung, 2004). Information quality attributes can also be regarded to include both the objective and subjective elements of accuracy, reliability, validity, comprehensiveness, currency, credibility, expertise, trust, thoroughness, transparency, and an awareness of bias.

Financial performance of SMEs

Several analysts have recommended that sales growth is the most significant performance measure in SME performance because it is progressively precise and effectively available compared with other accounting measures. Among these researchers include Matovu (2015), Haber and Reicher (2005), Orser and Hogarth (2002) and Gundry and Welsch (2001). According to Matovu (2015), SME performance fairly relies on sales and profitability with sales being the greatest contributing factor followed by profitability. Furthermore, the performance of SMEs is above average indicating that SMEs can sustain themselves in the market through profitability and sales. The current ratio, cash ratio and quick ratio which are by far the most proportions of liquidity can be utilized evaluate the capacity of association to change over resources into money. However, liquidity measures calculated from financial statements don't show the readiness of a firm to access credit

capital. Therefore, extensive literature review found a research gap, which is the relationship between financial structure and financial performance from the perspective of SMEs in Jinja District, Uganda.

RESEARCH METHODOLOGY

Both qualitative and quantitative research methods were used to collect and analyze research data. The study also adopted descriptive survey research design with purpose of aiding analysis in the various features of the study variables of financial structure and SME financial performance. The relationship between financial structure and the level of performance in SMEs were investigated using explanatory research design.

The research target 340 proprietors of SMEs in Jinja District, Uganda however since the target population was large, stratified random sampling technique was used to sample it and the total sample size of 181 SMEs were selected using the Krejcie and Morgan (1970) table.

A questionnaire was used to collect primary data from respondents owing to the fact that it didn't require presence of the researcher and as a result, a lot of time was saved. The questionnaire was designed using a 4-point likert scale.

The tool was pretested for validity using the content validity index (CVI) and a CVI of 0.8 was obtained which confirmed the research instrument as valid for use. For further validation of the questionnaire, a pilot test was conducted by issuing questionnaires to 10 percent of the sample population in a focused discussion to iron out any ambiguity and misinterpretations of questions in the questionnaire. The tool's reliability for internal consistency was pretested using Cronbach alpha technique obtaining a value of 0.75 which was within acceptable range.

All information which was obtained using questionnaires was then coded and categorized for exhaustive description, representation, and analysis. Descriptive statistics of mean and standard deviation were used to analyze quantitative data. Inferential statistics were used to generalize the results from the sample population and enable establish the relationship between variables using regression and correlation analytical techniques. Multiple linear regression analysis was carried out between the two variables of the research while the correlation relationship was analyzed using Karl Pearson's correlation coefficient.

The multiple linear regression model below examined the connection between variable factors and fixed factors of the research. $Y = \alpha + \beta_1X_1 + \beta_2X_2 + \beta_3X_3 + \epsilon$

Given that.

Y – Financial Performance

α – Constant

β_{1-3} – Coefficients

X_1 – Owners' savings and contributions from loved ones

X_2 – Retained earnings

X_3 – Borrowings

ϵ – Error term

RESEARCH FINDINGS AND DISCUSSION

The study response rate was 87% which was sufficient to draw conclusions regarding the effect of financial structure on financial performance of SMEs in Jinja District, Uganda. 59.4% of the responses were from males while 40.6% were from females. Most respondents (36.1%) were within the age group of 26 – 30, followed by the age group of 20 – 25 with 29.7%, and then followed by the age group of 31 – 35 with 22.6%. Next was the age group of 36 – 40 with a 7.7%, and lastly the age group of above 40 with a representation of 3.9% respectively. Majority of the respondents (56.7%) had acquired a diploma as formal level of education, followed by those that had reached certificate level (24.5%). Respondents with Bachelor’s degrees were 12.9% while those with Master’s degrees were 6.5%. Most of the respondents (56.8%) were from the operations department, followed by sales and marketing (16.1%), administration (15.5%) and human resources (11.6%) respectively. 81.3% of SMEs were located in Jinja Central Division. This is followed by Walukuba Masese Division (12.9%) and Kimaka Mpumudde Division (8.3%) respectively. The highest number of respondents were at assistant managerial level (49%), followed by supervisors (26.5%), managers (18.1%) and directors (6.5%) respectively. 64.5% of respondents had been in business operation for a period of 1 to 5 years, 22.6% of respondents had been in operation for a period of below 1 year. 9.7% of the businesses had been operational for a period of 6 to 10 years while 3.2% of the firms had been in operation for more than 10 years. 46.5% of SMEs employed between 21 and 50 people, 35.5% of SMEs employed between 11 and 20 people, 13.5% employed between 1 and 10 people while 4.5% employed above 50 people.

Effect of owner’s savings and contributions from loved ones on financial performance of SMEs in Jinja District, Uganda.

Table 1: Descriptive statistics for owners' savings and contributions from loved ones

	N	Mean	Std. Deviation
Personal cash at bank used as start-up capital	155	3.1290	.63153
Personal cash at hand used as startup capital	155	3.071	.5711
Personal money invested regularly	155	3.0774	.62973
Contribution of loved ones towards startup capital	155	3.0774	.61934
Valid N (listwise)	155		

Source: Obtained from primary research data analysis, 2022

According to table 1 above, there was a mean of 3.129 for personal cash at bank used as start-up capital which implies that respondents agreed to have contributed to start-up capital using their personal savings at bank. The standard deviation of 0.63153 for personal cash at bank used as start-up capital implies that research data collected for this variable was less spread out and therefore consistent and accurate. There was a mean of 3.071 for the use of personal cash at hand as start-up capital which implies that respondents agreed to have contributed to start-up capital using their personal cash at hand. The standard deviation of 0.5711 for personal cash at hand used as start-up capital implies that research data collected for this variable was less spread out and therefore more consistent. For regular investment of personal money into the business, there was a mean of 3.0774 which implies that respondents agreed to have continuously invested personal money into business operations while the standard deviation of 0.62973 for regular investment of personal money into the business implies that research data collected for this variable was less spread out and therefore more consistent. There was a mean

of 3.0774 for the use of contributions of loved ones towards start-up capital which implies that respondents agreed to have their loved ones contribute to start-up capital. The standard deviation of 0.61934 for personal cash at hand used as start-up capital implies that research data collected for this variable was less spread out and therefore more consistent. These findings are in line with the trading order theory as stated by Meyers and Majluf which states that companies rank their financing options based on costs incurred in raising it with preference made to internal funds such as personal contributions. When internal funds are drained, debt options are taken up, and when it is not reasonable to pay any more debt, equity is given.

Effect of retained earnings on financial performance of SMEs in Jinja District, Uganda.

Table 2: Descriptive statistics on retained earnings

	N	Mean	Std. Deviation
Reserve levels are maintained to ensure continuity	155	3.0581	.56106
Reserve levels are reinvested to boost sales	155	3.1097	.61967
Re-invested money generates profits	155	3.1290	.63153
Reserves are used to cater for business liabilities	155	3.1613	.61880
Valid N (listwise)	155		

Source: Obtained from primary research data analysis, 2022

Table 2 showed a mean of 3.058 for maintenance of reserve levels to ensure business continuity which implies that average respondents agree to have maintained reserve levels to ensure business continuity while a standard deviation of 0.56106 revealed that the data collected for this variable was less spread out and therefore consistent with the study objectives.

The mean of 3.1097 for reserve levels boost sales imply that average respondents agree to have used reserve levels to boost sales while the standard deviation of 0.61967 shows that the data collected for this variable was less spread out and therefore more consistent.

For the use of reserve levels to generate profits, there was a mean of 3.1290 which implies that average respondents agreed to have increase in profitability due to maintenance of reserve levels. The standard deviation of 0.6188 reveals that the data was less spread out and therefore more consistent.

Lastly, the mean of 3.1613 reserve levels and catering for business liabilities implies that average respondents agreed to have used reserve levels of their business finance to cater for business liabilities. The standard deviation of 0.6188 being greater than 0.5 reveals that the data was less spread out and therefore more consistent.

These findings concur with the research by Kinyua (2014) whose findings revealed that retained earnings doesn't have significant effect on financial performance of SMEs as compared with equity capital and debt capital. However, retained earnings can be used to expand the business, improve the firm's asset base, and improve the business liquidity. This will facilitate the act of performing financial activities in the right manner, however the researcher concludes that retained earnings have insignificant effect on financial performance of SMEs.

Additionally, these findings are in line with Modigliani and Miller’s hypothesis which proposes that companies do not have an optimum debt to equity ratio but rather, they should have a capital mix of either debt financing or equity financing or both depending on the goal they want to achieve.

Effect of borrowings on financial performance of SMEs in Jinja District, Uganda.

Table 3: Descriptive statistics for borrowings

	N	Mean	Std. Deviation
Borrowed money used as start-up capital	155	3.3290	.71268
Borrowed money increased liquidity	155	3.4839	.69651
Borrowed money increased cash to pay for liabilities	155	3.5161	1.70696
Valid N (listwise)	155		

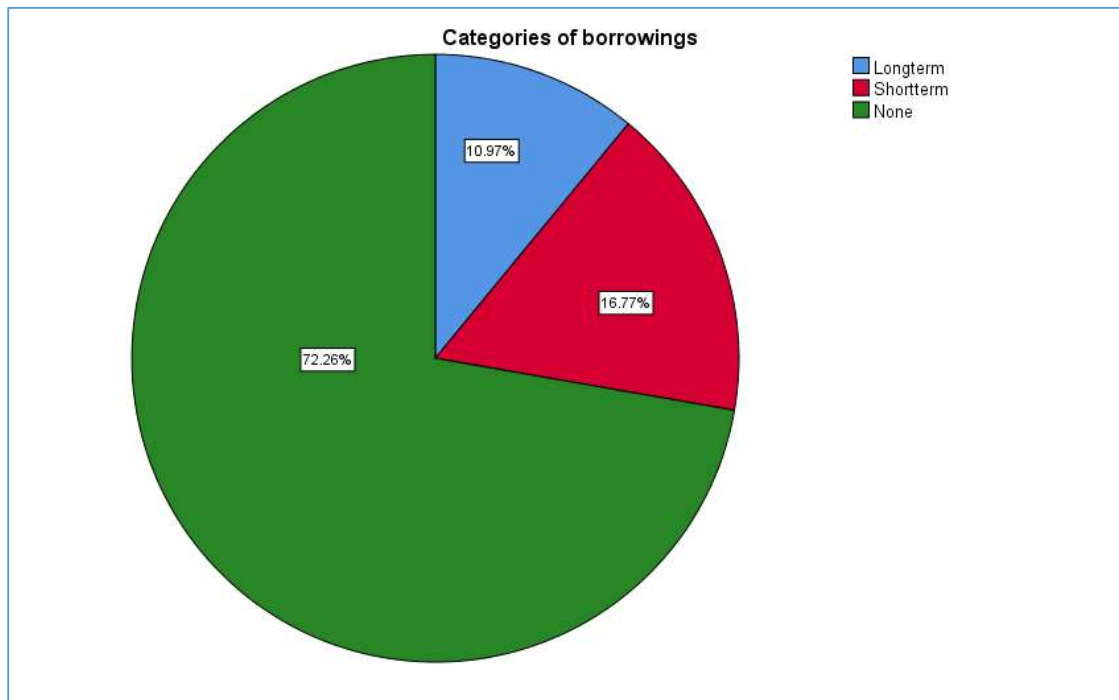
Source: Obtained from primary research data analysis, 2022

Table 3 showed a mean of 3.329 for the use of borrowed money as start-up capital which implies that average respondents agree to have used borrowed funds in order to start their business operations. The standard deviation of 0.71268 reveals that the data used for borrowed money as start-up capital was less spread out and therefore more consistent

There was a mean of 3.4839 for the use of borrowed money to increase liquidity which implies that average respondents agree to have used borrowed funds in order to improve their business liquidity. The standard deviation of 0.69651 reveals that the data used for use of borrowed money to increase liquidity was less spread out and therefore more consistent

For the use borrowed money to pay liabilities, there was a mean of 3.5161 which implies that average respondents agree to have used borrowed funds in order to pay off their liabilities. The standard deviation of 1.70696 reveals that the data used for this variable was overly spread out and therefor inconsistent.

Figure 1: Categories of borrowings



Source: Obtained from primary research data analysis, 2022

According to figure 1 above, 72% of businesses did not borrow to start business operations, 10.97% used long term borrowings to finance business operations while 16.77 % used short term borrowings to start business operations.

These findings are consistent with findings of Chepkemoi (2013) revealed that most of SMEs under her study relied on internal source because external sources of financing particularly debt were more difficult to acquire. Additionally, the study findings are consistent with Pecking Order Theory (2013) which states that in the presence of asymmetric information, a firm will prefer internal finance, but would issue debt if internal finance was exhausted.

These findings are also consistent with the trade-off theory which suggests that the ideal capital mix happens when tax benefits and bankruptcy marginal costs balance. Thus, equity capital is less favored over debt capital by firms especially at the point where the cost of insolvency begins to be substantial.

Analysis of the multiple linear regression model

Lastly, the researcher sought to analyze the multiple linear regression model, $Y = \alpha + \beta_1X_1 + \beta_2X_2 + \beta_3X_3 + \varepsilon$ whereby Y is for financial performance, α is for a constant, β_{1-3} are coefficients, X_1 is for owners' savings and contributions from loved ones, X_2 is for retained earnings, X_3 is for borrowings, and ε is the error term. The findings have been explained in tables 4,5, and 6 next page.

Table 4: Model summary for multiple linear regression

Model Summary^b

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics			Sig. Change	F
					R Square Change	F Change	df1		
1	.543 ^a	.295	.281	.55978	.295	21.040	3	151	.000

a. Predictors: (Constant), Owners’ savings and contributions, Retained earnings, borrowings

b. Dependent Variable: SME Financial performance

Source: Obtained from primary research data analysis, 2022

According to table 4, R square value of 0.295 indicates that the variance of the dependent variable of the model is 29.5% which is statistically significant. This implied that considering the independent variables (owners’ savings and contributions, retained earnings, borrowings) jointly, there is a probability of predicting financial performance of SMEs by 29.5% (R squared = 0.295) while the other probability of 70.5% is beyond the scope of study. Additionally, the analysis revealed that there was an average positive correlation between the owners’ savings, retained earnings and borrowings of 0.543.

Table 5: ANOVA analysis for the multiple linear regression

ANOVA^a

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	19.780	3	6.593	21.040	.000 ^b
	Residual	47.317	151	.313		
	Total	67.097	154			

a. Dependent Variable: SME Financial performance

b. Predictors: (Constant), Owners’ savings and contributions, Retained earnings, Borrowings

Source: Obtained from primary research data analysis, 2022

According to the ANOVA analysis in table 5, the significance value of 0.000 is below 0.05. This implies that the model was a good fit and that there is a significant statistical difference between the effect of owners’ savings on financial performance of SMEs, effect of retained earnings on financial performance of SMEs and effect of borrowings on financial performance of SMEs.

Table 6: Coefficients of the multiple linear regression

Coefficients^a

Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.	Correlations		
		B	Std. Error	Beta			Zero-order	Partial	Part
1	(Constant)	.659	.211		3.127	.002			
	Owners' savings	.038	.081	.036	.469	.640	.270	.038	.032
	Retained earnings	.317	.089	.285	3.577	.000	.436	.279	.244
	Borrowings	.326	.071	.344	4.569	.000	.467	.349	.312

a. Dependent Variable: Financial performance

Source: Obtained from primary research data analysis, 2022

The coefficient for owners' savings and contributions from loved ones (0.36) in table 6 above indicated that as owners' savings and contributions from loved ones increases by one-unit, financial performance would increase by 0.36 units. Therefore, the model was fit to predict financial performance using owners' savings and contributions from loved ones.

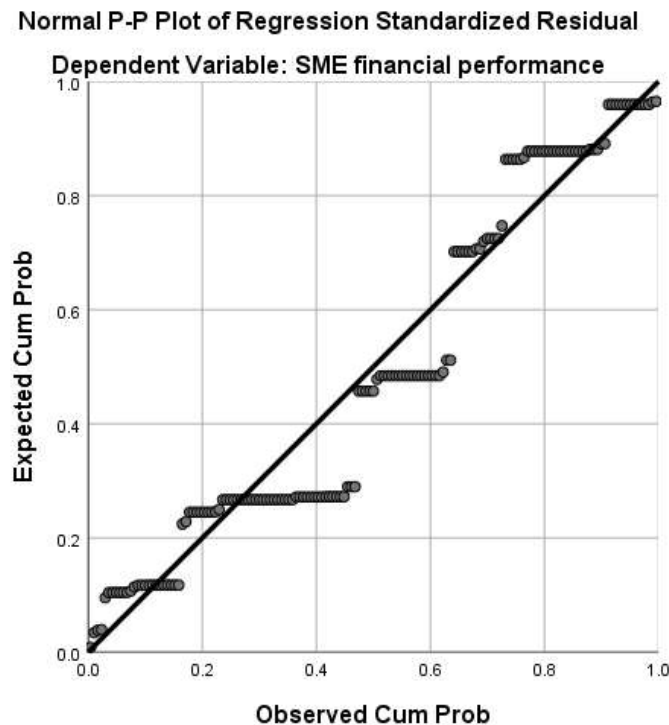
The coefficient for retained earnings (0.285) in table 6 above indicated that as retained earnings increases by one-unit, financial performance would increase by 0.285 units. Therefore, the model was fit to predict financial performance using retained earnings.

The coefficient for borrowings (0.344) in table 6 above indicated that as borrowings increase by one-unit, financial performance would increase by 0.344 units. Therefore, the model was fit to predict financial performance using borrowings.

The standardized coefficients for variables under table 6 show that owners' savings have a greater effect on the financial performance of SMEs, followed by borrowings while retained earnings have the least effect on financial performance. Therefore, the multiple linear regression model obtained from standardized coefficients was as $Y = 0.36X_1 + 0.285X_2 + 0.344X_3$. whereby Y– Financial Performance, α – Constant, β_{1-3} – Coefficients, X_1 – Owners' savings and contributions from loved ones, X_2 – Retained earnings, X_3 – Borrowings.

The findings on the multiple linear regression model agree with findings by Kinyua (2014), in which he indicated that equity capital including owners' savings and retained earnings was a preferred source of capital for most SMEs. Kinyua (2014) study also refuses that high rate of borrowing has negative effect on the financial performance of a firm but rather shows that debt capital has a significant effect on financial performance.

Figure 2: Normal P-P Plot for the multiple linear regression



Source: Obtained from primary research data analysis, 2022

There were scattered points along the plot in the figure 2 above imply that there is no linear relationship between the multiple variables of owner’s savings, retained earnings, and borrowings and financial performance of SMEs.

CONCLUSIONS AND RECOMMENDATIONS

Conclusions

Objective 1: To assess effect of owner’s savings and contributions from loved ones on financial performance of SMEs in Jinja District, Uganda.

The research concludes that owners’ savings including cash at hand, cash at bank and contributions from loved ones are used as startup capital. Both cash at hand, cash at bank and contributions from loved ones have a positive relationship on financial performance of SMEs especially improvement of the cash position. This positive relationship between owners’ savings and financial position of SMEs is however weak.

Objective 2: To assess effect of retained earnings on financial performance of SMEs in Jinja District, Uganda

On average, SMEs maintain reserve levels for business continuity which helps to improve financial performance through boosting of sales, increasing profitability, and meeting business liabilities. However, there is a positive but weak relationship between retained earnings and the ability of the businesses to meet their short-term liabilities. There is also a positive and moderate relationship between retained earnings and sales. Lastly, there is a stronger positive relationship between retained earnings and gross profit over time than it is for net profit.

Objective 3: To investigate effect of borrowings on financial performance of SMEs in Jinja District, Uganda.

Most SMEs do not borrow money to start their business. However, the SMEs that borrow mostly use short-term borrowings compared and less of long-term borrowings. There is a positive slight relationship between borrowings and decrease in liabilities over time. For the average SMEs, borrowed money increase the business capacity to pay its liabilities.

Analysis of the multiple linear regression model

The multiple linear regression model generated reveals that there is no linear relationship between financial performance and owners' savings and contributions from loved ones, retained earnings and borrowings for SMEs in Jinja District.

Recommendations

Business owners should continue to utilize cash options including cash at hand, savings in the bank and contributions from loved ones as startup capital because of its potential to improve their business cash position, meet current liabilities and ensure business continuity especially in the early years of their business operations.

SMEs should endeavor to maintain reserve levels for business continuity. This is because the research has proved that retained earnings have potential to improve financial performance through boosting sales, increasing profitability, and meeting business liabilities.

With increasing pressure on SMEs' performance, owners should embrace other financial structures such as borrowing (for either long-term or short-term) in addition to the traditional options of using cash. They should acquire adequate financial literacy about credit including the merits, demerits, and risks. Through proper risk assessment, SMEs should use appropriate credit channels and clear guidelines for boosting their business operations.

Business owners should develop competencies in keeping accurate, understandable business records so that it can easily be retrieved for better decision making. Having quality information in place will reduce unwillingness to disclose information because they will be sure of what they are disclosing.

The increasing number of survival of SMEs calls for authorities such as City Councils authorities to support SMEs through building appropriate support infrastructure such as good roads, security, probing for support funding, among others.

Education institutions should emphasize hands-on training to its students undertaking entrepreneurial studies on topics such as bookkeeping, credit management, among others so that they can make appropriate financial decisions.

Further research on the effect of non-financial aspects such as marketing on financial performance of SMEs should be conducted. The same applies for measures of financial performance other than sales, profitability, and liquidity. Additionally, further research on the effect of financial structure on financial performance of SMEs in other cities of Uganda including Gulu, Mbarara, Arua, Mbale cities should be conducted. This is to help inform regional SME performance in the country, obtain unique challenges faced by SMEs in the various cities and propose solutions for improvement.

Lastly, further studies on SMEs performance in other countries especially in East Africa should be conducted. This would be to investigate whether SME challenges within the region are similar, there after provide lasting solutions for continuous business improvement.

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