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DEDICATIONS.

I dedicate this work with profound love to my dear parents, for their unconditional love, to my siblings for their support, to my relatives for their trust in me, and to my friends, classmates, and teachers for their invaluable contributions to my studies. With great love, I also dedicate this research work to myself for believing in me, for the hard work and perseverance showcased during the whole study period. I highlight the immeasurable support of my beloved dad, Joomu Moses, and big brother Tusubira Fredrick Decent for their undivided availability throughout this journey.

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LIST OF ABBREVIATIONS

BOU	Bank of Uganda.
SMEs	Small and Medium-sized Enterprises.
SMIs	Small and Medium-sized Industries.
UBOS	Uganda Bureau of Statistics.
CRB	Credit Reference Bureau.
SACCO's	Savings and Credit Cooperatives.
GDP	Gross Domestic Product.
UIA	Uganda Investment Authority.
OECD	Organisation for Economic Co-operation and Development
EAC	East African Community.
EC	European Commission
UDBL	Uganda Development Bank Limited.
LC	Letter of Credit.
UGX	Uganda Shillings

GENERAL INTRODUCTION

1. Background

Small and Medium Enterprises (SMEs) play a pivotal role in the economic development of Uganda, much like in many other developing countries. They are essential for generating employment, fostering innovation, and contributing significantly to GDP. According to the Uganda Investment Authority, SMEs account for over 90% of the private sector, contribute 20% of the GDP, and employ more than 80% of the workforce outside agriculture. However, despite their critical importance, SMEs face numerous challenges that impede their growth and sustainability, particularly regarding access to finance.

Access to finance is frequently cited as the most significant constraint for SMEs in Uganda. Financing is essential for SMEs to start operations, maintain their activities, and expand their businesses. However, the World Bank (2020) reports that a considerable number of SMEs in Uganda are either underfinanced or entirely excluded from the formal financial system. This financing gap severely limits their potential for growth and innovation, which are crucial for economic development and competitiveness in the global market.

One of the primary reasons SMEs struggle to access finance is the high-interest rates charged by private banks. According to Beck, Demirguc-Kunt, and Martinez Peria (2008), interest rates in Uganda are among the highest in the region, which makes borrowing costly for SMEs. High-interest rates increase the cost of capital, thereby reducing the profitability and sustainability of these enterprises. This scenario discourages many SMEs from seeking loans, further perpetuating the cycle of limited access to capital.

Collateral requirements also pose a significant challenge for SMEs seeking bank financing. Many SMEs lack the substantial physical assets that banks typically require as collateral. A study by Menkhoff, Neuberger, and Rungruxsirivorn (2012) found that collateral requirements are a major barrier for SMEs in developing countries, including Uganda. Without sufficient collateral, SMEs are often deemed high-risk borrowers, making it difficult for them to secure loans. This situation is exacerbated by the lack of alternative financing mechanisms and the underdevelopment of financial markets in Uganda.

The issue of credit profiling and the lack of robust credit histories further complicates access to finance for SMEs. Credit profiling involves assessing the creditworthiness of a borrower based on their financial history. However, many SMEs in Uganda operate informally and do not maintain detailed financial records, making it challenging for banks to assess their creditworthiness. According to Nanyondo et al. (2014), the absence of a comprehensive credit history often results in higher risk perceptions among lenders, thereby reducing the likelihood of loan approvals for SMEs.

The performance of SMEs also plays a crucial role in their ability to access finance. Banks are more inclined to lend to businesses that demonstrate consistent financial performance and stability. However, many SMEs in Uganda face operational challenges that affect their performance, such as inadequate management skills, limited market access, and competition from larger firms. As highlighted by Kira and Zhongzhi (2012), the perceived risk associated with lending to SMEs with inconsistent performance further restricts their access to necessary financial resources.

The Ugandan government and various development partners have recognized these challenges and are implementing several initiatives to improve access to finance for SMEs. Programs aimed at financial literacy, capacity building, and the development of alternative financing mechanisms are in place to support SMEs. The introduction of credit guarantee schemes is one such initiative designed to reduce the risk for banks by providing guarantees for loans to SMEs. However, despite these efforts, the financing gap remains significant, and more needs to be done to address the systemic issues that hinder SME access to finance.

In summary, SMEs are vital to Uganda's economic growth and development. However, their potential is significantly hampered by limited access to finance. High-interest rates, stringent collateral requirements, lack of credit history, and inconsistent performance are some of the primary barriers that need to be addressed. This study aims to provide a comprehensive analysis of these challenges and propose strategies to enhance SME access to bank financing in Uganda, particularly focusing on private banks. By addressing these issues, the study seeks to contribute to the broader goal of fostering a more inclusive and supportive financial environment for SMEs in Uganda.

Access to finance is a critical issue for SMEs in Uganda. Despite numerous initiatives and policies aimed at improving financial inclusion, many SMEs still struggle to secure the funding they need to start, operate, and expand their businesses. This problem is particularly acute in the private banking sector, where stringent collateral requirements, high-interest rates, and limited credit histories often exclude SMEs from obtaining necessary loans and financial services.

The key challenges faced by SMEs in Uganda regarding access to bank financing can be categorized into several areas. First, high-interest rates make loans prohibitively expensive for many SMEs, reducing their ability to borrow and invest in their businesses. Second, the requirement for substantial collateral often disqualifies SMEs that lack significant physical assets, further limiting their access to finance. Third, credit profiling and the lack of a robust credit history hinder SMEs from securing loans, as many private banks rely heavily on credit scores to assess loan eligibility. Finally, the performance of SMEs themselves is often scrutinized by banks, with those showing inconsistent or poor financial performance finding it more challenging to access financing.

2. Purpose and contribution of the study.

The primary purpose of this study is to investigate the challenges faced by Small and Medium Enterprises (SMEs) in Uganda in accessing bank financing, focusing on the role of private banks. By examining barriers such as high-interest rates, stringent collateral requirements, lack of comprehensive credit histories, and performance inconsistencies, the study aims to provide a detailed understanding of the financial constraints impeding SME growth. This analysis is crucial for policymakers, financial institutions, and development partners to design targeted interventions. Additionally, the study contributes to the academic literature on SME financing in developing countries, particularly Uganda, by incorporating empirical data and case studies. Practical recommendations derived from this study aim to improve access to bank financing for SMEs and inform the creation of a more supportive financial environment. The findings are expected to impact policy development, supporting

3. Problem statement

Access to finance is a critical determinant of the growth and sustainability of Small and Medium Enterprises (SMEs). In Uganda, SMEs account for a significant portion of economic activities and employment. However, despite their importance, SMEs face substantial challenges in accessing financing from private banks. The hurdles are multifaceted, encompassing high-interest rates, stringent collateral requirements, inadequate credit profiles, and operational inefficiencies. These financial constraints hinder the ability of SMEs to expand, innovate, and contribute optimally to economic growth.

One of the key issues is the high cost of borrowing. Interest rates in Uganda are relatively high, making loans expensive for SMEs. This financial burden limits their ability to secure the necessary capital for growth and operational needs. Furthermore, private banks often demand substantial collateral, which many SMEs cannot provide. This requirement effectively excludes a significant number of SMEs from accessing formal credit, thereby stifling their growth potential.

Another critical challenge is the inadequacy of credit profiles among SMEs. Many SMEs have limited or no credit history, making it difficult for banks to assess their creditworthiness. The absence of reliable financial records and audited statements further exacerbates this issue, leading to a higher perceived risk by lenders. As a result, private banks are reluctant to extend credit to these enterprises, leaving them to rely on informal and often more expensive sources of finance.

Performance inconsistencies among SMEs also play a role in limiting their access to finance. Financial institutions typically evaluate the past performance of businesses to gauge their ability to repay loans. SMEs with fluctuating revenues and profitability are seen as high-risk borrowers, making it harder for them to secure bank financing. This situation creates a vicious cycle where lack of access to finance hampers performance, and poor performance, in turn, limits access to finance.

Given these challenges, this perplexity leads us to a pivotal inquiry that forms the fundamental essence of our research, **What are the key challenges faced by Small and Medium Enterprises (SMEs) in Uganda** regarding **access to bank financing, specifically within the domain of private banks?** In addition, this central question is then accompanied by the following secondary questions:

- ⇒ What specific factors contribute to the difficulty SMEs face in accessing bank financing in Uganda?
- ⇒ How do private banks in Uganda perceive the risks associated with lending to SMEs, and what criteria do they use to assess loan applications?
- ⇒ What role do financial statements and the quality of financial reporting play in SMEs' access to bank financing in Uganda
- ⇒ How does the age and performance of an SME influence its likelihood of obtaining bank financing in Uganda?

By addressing these secondary questions, the study aims to provide a comprehensive analysis of the challenges and opportunities associated with SME financing in Uganda, ultimately contributing to more effective strategies and policies to enhance financial inclusion for these enterprises.:

4. Research hypotheses:

H1. High-interest rates significantly reduce the likelihood of SMEs obtaining financing from private banks in Uganda.
H2. Stringent collateral requirements are a major barrier to SME access to bank financing.
H3. Inadequate credit profiles and lack of financial records significantly hinder SME access to bank financing.
H4. The inconsistent performance of SMEs negatively impacts their ability to secure financing from private banks.

5. Methodology Announcement

This study employs a mixed-methods approach, combining both quantitative and qualitative research methods to provide a comprehensive understanding of the factors affecting SME access to bank financing in Uganda. The mixed-methods approach ensures robustness and depth in the findings by enabling the triangulation of data. The quantitative aspect involves the administration of structured surveys to a representative sample of SMEs across various sectors in Uganda. These surveys gather detailed information on the financial characteristics of SMEs, their experiences with accessing bank financing, and the specific challenges they face. Key variables include interest rates, collateral requirements, credit profiles, performance metrics, and the impact of these factors on their ability to secure financing.

In addition to surveys, the qualitative component consists of in-depth interviews with SME owners, managers, and representatives from private banks. These interviews aim to capture the nuanced perspectives and experiences of both borrowers and lenders. Open-ended questions explore the reasons behind the stringent lending criteria, the perceived risks associated with SME lending, and potential solutions to improve access to finance. This qualitative data provides rich contextual insights that complement the quantitative findings, offering a comprehensive view of the financial landscape for SMEs in Uganda.

A stratified random sampling technique is employed to select SMEs for the survey, ensuring representation from different sectors, sizes, and geographical regions within Uganda. For the qualitative interviews, purposive sampling is used to select participants who have significant experience and insights into SME financing, including bank officials and policymakers. This strategic sampling method ensures that the data collected is both comprehensive and representative, providing a solid foundation for the analysis. By integrating these diverse data sources, the study aims to uncover the multifaceted nature of SME financing challenges.

Quantitative data will be analysed using statistical techniques such as regression analysis to test the hypotheses and identify the key determinants of SME access to bank financing. The qualitative data will be analysed thematically, identifying common themes and patterns that emerge from the interviews. The integration of both data sets provides a holistic understanding of the research problem, offering a nuanced and well-rounded perspective. The study adheres to ethical research standards, ensuring informed consent, confidentiality, and the voluntary participation of all respondents. Ethical approval will be sought from relevant institutional review boards prior to data collection.

6. Structure of the Study.

This study is organized into three chapters, each focusing on a distinct aspect of the research on bank financing for SMEs in Uganda.

The first chapter presents the conceptual framework of SMEs. It begins by defining SMEs, highlighting their importance to Uganda's economy, and reviewing existing literature on SME financing. This chapter also discusses various theoretical frameworks and empirical studies that shed light on the challenges and opportunities faced by SMEs in accessing bank financing.

The second chapter examines the role of private banks in financing SMEs and facilitating international trade in Uganda. It provides an overview of the banking sector in Uganda, describes the types of financing available to SMEs, and explores the specific challenges that SMEs encounter when seeking finance from private banks. This chapter also looks at the tools and strategies used by private banks to mitigate risks and support SMEs in international trade.

The third chapter outlines the research methodology and analysis. It details the research design, data collection methods, and analytical techniques employed to investigate the determinants of SME access to bank financing. This chapter also discusses the variables used in the analysis, the sources of data, and the procedures for ensuring the reliability and validity of the research findings. The analysis is conducted through qualitative and quantitative methods, providing a comprehensive understanding of the factors influencing SME access to bank financing in Uganda. The chapter concludes with the interpretation of the results and their implications for policy and practice.

CHAPTER ONE: CONCEPTUAL FRAMEWORK OF SMALL AND MEDIUM-SIZED ENTERPRISES

I.1 Introduction

Small and Medium Enterprises (SMEs) are vital to Uganda's economic development, driving growth, job creation, and innovation. Despite their significance, SMEs often face significant hurdles in accessing finance, especially from private banks. This chapter establishes a conceptual framework to understand these challenges and the role of private banks in addressing them.

The chapter is structured into three key sections: a literature review, definitions, and an overview of SMEs in Uganda. The literature review examines existing research on SME financing, identifying common barriers and strategies for improvement. The definitions section clarifies key terms and concepts essential for understanding the subsequent analysis. Finally, the section on SMEs in Uganda provides context on their economic role, unique challenges, and the financial landscape they navigate.(HANI)

By exploring these areas, we aim to build a comprehensive understanding of the factors influencing SME financing in Uganda and set the stage for the detailed analysis in the following chapters.

I.2 Literature review

There is no doubt that access to finance is of crucial importance for the ongoing and sustainable growth and profitability of small and medium enterprises sector (SMEs) through its role in facilitating the creation of new businesses and nurturing the innovation process as well as promoting the growth and development of existing businesses, which in turn, boost national economic growth.

This literature review provides a comprehensive examination of the theoretical frameworks, empirical findings, and emerging trends in enterprise studies. By synthesizing existing research from various disciplines, this review aims to shed light on the multifaceted nature of enterprises and contribute to a deeper understanding of their roles in driving economic growth, fostering innovation, and shaping societal outcomes.

For clarity and chronology, it was arranged according to the objectives of the study starting with a theoretical review, conceptual review and empirical review

I.2.1 Theoretical review

This study was guided by two Theories namely the Resource Based Theory and Lifecycle of Consumption. These two Theories were chosen because they contain key constructs that have informed the study in terms of resources and the effect of age in terms of how long the SMEs have been conducting business as a moderating variable on the relationship between financial characteristics and access to finance.

I.2.2 Resource based theory

Resource-Based Theory was advanced by Barney (1991) and Dicksen (1996) who contended that the ownership of strategic resources offers an organization with a golden chance to develop competitive advantages over its rivals. Barney (1991) in his studies explained that the Resource Based Theory explains that an organization is a bundle or a pile of assets and resources that are

both tangible and intangible in nature that if effectively and efficiently utilized, an organization becomes a going concern entity.

Resources are everything that might be thought of as an asset of a given firm, which maybe tangible intangible assets and tangible resources and include financial capital (e.g., liability capital, equity, capital, and retained earnings) and physical capital (cars, land& buildings, machinery,). Intangible resources consist of organizational procedures and reputation, entrepreneurial knowledge, skills, experiences, among others (Barney, 1991). For purposes of this study, the focus was on financial resources particular liability capital

The overall idea of this Theory is that if an entity acquires and effectively controls its rare valuable, non-substitutable resources and capabilities, it can attain sustainable competitive advantage over other competing firms and steady growth and performance, given that it has the ability to absorb and apply these particular resources (Barney 1991). He further proceeds to assert that what separates successful or making organizations from breaking or struggling organizations is the way they deploy their resources for example information, knowledge assets, capacities as well as their organizational processes

Resource Based Theory thus involves the ability of business managers to put emphasis on effective management of current assets of the business (Alvarez &Busenitz, 2001). When current assets are managed effectively, good results are expected to be yielded. The Resource – Based Theory therefore implies that business managers, whose resources are specified, can facilitate and ensure recognition of new opportunities and assembling resources in an effective manner as well as ensuring prompt payment and shortening the recovery period of accounts receivable. This would ultimately have a positive effect in the working capital management and firm profitability.

Conferring to Barney (1991) valuable resource must permit a firm to do things and act in behaviours that lead to low costs, high margins, high sales, or adds financial value to the firm. Therefore, basing on the above explanations and constructs of the Theory, this study was guided by this Theory because these Small and medium-sized enterprises can depend on resources owned by the firm like buildings, land titles, cars, reputation, age to access finance inform of demand deposits, credit, payments, or insurance that in long run help to increase sales growth leading increased profitability levels of the firm.

I.2.3 Life Cycle Theory of Consumption

This Theory was first introduced by Modigliani in the early 1950s and later revised in 1980 by Modigliani and Blumberg (Ando, 2005). The firm life cycle approach defines the development of the firm as a linear sequential process through a number of stages. The number of stages is not standardized. The financial life cycle model integrates elements of agency, trade-off, and pecking order theories, and defines sources of finance as typically advanced by funders at each stage of a firm's development.

The theory points out key aspects being lifecycle hypothesis and its relationship in putting aside earned income / saving so that later the savings can be used to acquire assets. This Theory was mainly advanced toward the relationship between peoples' behaviours towards savings, expenditure and incomes but later advanced to other aspects like business. In business, the Theory points out that firms depending on their age have got different sources of finance. At beginning, the firms have trouble accessing finance due to improper information available and low collateral and inexperience (Fjose, 2010). The most central and commonly-used sources of finance at this stage are finance from friends, family members and personal savings of the firm owner (Gompers, 2010).

Throughout mature and growth stages, personal funding becomes comparatively less important as investment finance is progressively sourced from retained profits. Continuous conducting of business facilitates access to amplified sources and amounts of finance, particularly long-term bank debt financing. Thus, it is common for SMEs to have high levels of short-term debt in their toddler stages (Nofsinger& Wang, 2011).

The Theory assumes that lifecycle planning needs people to look into an undefined future. It also assumes that increases in life- time resources lead to proportionate upsurges in consumption in all periods of life as a result, consumption is proportionate to life time resources. The theory also assumes that a firm has to follow some sort of developmental stages to be able to acquire finance.

However, the Theory holds some criticisms like being difficult for people to learn how to behave financially because the future is uncertain, failing to recognise that there are costs or cost centres on which people or organisations spend on their income and this reduces the saving levels and failing to clearly point out the stages of developments firms have to go through.
Despite the cited criticisms mentioned above, this Theory was key to this study in a way that the length of existence in a business determines access to finance given to the SMEs and also its assumed that SMEs that have been in business for a long time through saving and operation they are able to obtain assets that can be used as security in accessing finance from financial institutions (bank financing).

I.3 Conceptual review

I.3.1 Quality of financial statements

It is challenging on the part of the bank to estimate the degree of risk related with the SME; thus, the banks hesitate to extend finance. Though lenders may wish to screen bad borrowers from good ones, in reality inadequate disclosure may stop them from receiving the relevant information, thus making it difficult to extend finance. Rendering to study conducted by Epstein (2007), quality financial statements ought to serve as an anchor between the bank and SMEs to predict the level of perceived risk. This means that fair presentation of financial statements reflects transparency in the financial position, revenue projections and cash flows of the SMEs to enhance lending parties' informed decisions to extend finance.

I.3.2 Collateral Availability

SME segment faces problems to access external finances for their investment projects because of lack of assets to be pledged as security. In that outlook SMEs fail to grow due to lack of collateral to pledge to access external sources of finance. Coco (2000) recommended that the collateral is the lender's protection in case default occurred by a borrower, in that view collateral is the insurance that lender's contract will be honoured and valued.

Collateral solves the information asymmetry problems in the evaluation of investment project, the worthiness of the project and risk that might be involved by a borrower as well as the cost related to supervision of borrower's characters. Bougheas, Mizen and Yalcin (2006) pointed out that the prerequisite of collateral is a crucial aspect for SMEs to succeed in approachability of external financing from lenders.

Fatoki (2019), and Barbosa and Moraes (2004), proposed that operators of SMEs have to own more tangible assets that can create higher value on their firm to quicken borrowing security. Since, the higher the value of assets the lower the interest rates of the debt to be secured by those

assets. Consequently, it is hypothetical existence of a strong positive relationship between collateral and access of debt financing by SMEs.

I.3.3 Age of the firm

Age according to Chandler (2009) the longer a firm exists and the bigger it is, the greater it signals that it can weather hard economic conditions. Additionally, by remaining in business, a firm can indicate that it does not adopt opportunistic behaviour. According to Klapper et al. (2006), younger firms (less than 4 years) depend less on bank financing and more on informal financing. This view is also supported by Ngoc & Nguyen (2009) which find that it is frequently difficult and expensive for young SMEs to access bank financing, due in large portion of information asymmetry between the banks and firms. Bougheas et al. (2006) point out that young firms are extra failure prone than older ones. Therefore, it is hypothesized that, there is a positive relationship between the age of the firm and access to finance from commercial banks

I.3.4 Access to finance

The significance of finance has been well recognized in the literature and the firm-financing gap has advanced to be a common terminology, portraying the inadequate access to finance faced particularly by firms (OECD 2006, & IFC, 2010). Inadequate finance is a key hindrance to firm growth (Malhotra etal.,2007) and it has been found that small firms face bigger encounters in obtaining finance as compared to larger firms (Schiffer & Weder, 2001 & Beck & Demirguc-Kunt, 2006)

I.4 Empirical Review of related literature basing on the study objectives

I.4.1 The effect of Quality of financial statements on access to finance

Schoombee (2004) assert that financial institutions tend to consider the quality of financial statement before they extend credit to borrowers, they need to assure themselves of the viability of the loan applicant and thus they need to see audited financial statements accessible in form of statement of comprehensive income statement of financial position, statement of changes in equity and finally statement of cash flows. According to McKenzie and Baker (2011), and Epstein (2007) quality financial statements should serve as an anchor between the bank and small and medium enterprise to predict the level of perceived risk. This means that fair presentation of financial statements reflects transparency in the financial position, cash flows and revenue projections of the SMEs to enhance lending parties make informed decisions to extend finance.

According to Ball (2006), quality financial statements should serve as an anchor to effect access to finance. This is based on the premise that once financial statements reduce the level of information asymmetry this enables the bank to estimate the perceived risk and extend finance to small and medium. Furthermore, Leuz and Verrecchia (2011) argued that a higher financial reporting quality increase expected cash flows by financial statement users.

Bestowing to Meyer (2002), to determine repayment capacity, creditors will normally want small and medium enterprises to provide financial statements reflecting its most recent financial position as well as the 2-3 previous years. For loans or other products financing capital expenditures, creditors will also need medium-term and long-term financial projections that reflect the expected materialization of the business plan that validates the need for the loan or other financing facility which are all reflected in the financial statements (Tweedie, 2012). He

continued to assert that for SMEs to access finance from banks, quality of financial statements is supreme.

Quality financial statements are examined as part of the underwriting process for larger accounts. Research displays that financial information is one of the primary measures used to assess the capacity of a business to effect payment of credit (Kwok, 2002). The quality of financial statements ranks as the favoured measure for lending to small and medium classified as both retail and corporate clients. Using data from financial statements addresses small and medium information asymmetry problems in a cost-effective way, especially for larger financial institutions. Allee and Yohn (2009) found that firms in the United States with audited financial statements are marginally but significantly less likely to be denied credit and those firms with accrual-based financial statements benefit in the form of lower cost of capital.

More so Nanyondo et al. (2014) assert that there is a significant positive relationship between quality of financial statements and access to finance to small and medium enterprises. However, perceived risk is not significantly associated with access to finance. A substantial number of studies have exposed that banks were the most significant external users of small entity financial statements. This discovery is in line with the evidence gained from the study carried out in different countries and found that bank loans were one of main sources of debt finance for SMEs (Beck et.al., 2006)

Dang, Marriott and Marriott (2008) also studied the use of small and mediums quality financial statements by bank lending officers in Vietnam. Comparable to prior studies, bankers converted financial statement information into a standardized form, but they viewed that small entity financial statements were less useful in loan decision making. Place visit and direct communication with clients, for example, were used as alternative sources of information. The results of this study also recommended that the bank's use of quality financial statements from small and medium was affected by the directors' perceptions of the role of accounting, but not by the uses of accounting standards and financial statement audit.

I.4.2 The effect of collateral availability on access to finance.

Coco (2000) proposed that the collateral is the lender's defence in case default happened by a borrower, in that viewpoint collateral is the insurance that lender's contract will be honoured and respected. The security assets should be used to recover the principal in case of default. SMEs in specific provide security in form of properties (cars, houses and whatever that could actually bring back the principal amount) in case of non-payment on loans (Garrett, 2009). Security for loans must really be capable of being sold under the normal circumstances of the market, at a fair market value and also with sensible timeliness.

Menkhoff, Neuberger, and Rungruxsirivorn (2012) found that SME borrowers in less developed economies have lower level of collateralizable assets to pledge as a security by banks and thus, the likelihood of credit rationing is higher for SMEs in the less developed economies. Bougheas et al. (2006) argue that collateral is a significant factor for SMEs in order to access debt finance. Barbosa and Moraes (2004) contend that SME owners-managers that invest deeply in tangible assets tend to have higher financial leverage since they can borrow at lower interest rates if their debt is secured with such assets.

In 2017, the World Bank steered an enterprise survey among 560 small and medium enterprises in Bangladesh to comprehend the collateral necessities by the commercial banks. The survey outcomes showed that 67.14 per cent of SMEs provided land and buildings as security to get access to the bank loans. On the other hand, about 43 per cent SMEs provided individual assets

and about 29 per cent firms provided equipment and machinery as security. However, only 3.39 per cent firms guaranteed accounts receivables as collateral (World Bank Enterprise Survey, 2017). Henceforth, the results recommended that commercial banks in Bangladesh are comfortable to provide SME loans when they are secured with the fixed assets as collateral.

By way of providing collateral an essential role is played in easing SME access to finance, SMEs that have extra fixed assets tend to utilize higher financial leverage (Nofsinger& Wang, 2011) .The motive for this is that these firms can borrow at lower cost of debt finance/interest rates as their loans are protected with these assets serving as collateral. In his examination of the role of collateral and personal guarantees by means of a unique data set from Japan's SME loan market (Fatoki, 2011) found that a positive relationship between the use of collateral and the strength of the borrower-lender lending relationship results in easier SME access to finance.

SME segment faces challenges to access external finances for their investment projects attributed to lack of assets to be promise as collateral. In that outlook SMEs fail to grow due to absence of collateral to pledge to access external sources of finance. Bougheas et al. (2006) pointed out that the requirement of collateral is a central aspect for SMEs to prosper in approachability of external financing from lenders. Barbosa and Moraes (2004) and Fatoki (2011) proposed that operators of SMEs have to own more tangible assets that can create higher worth on their firm to quicken borrowing security. Because, the higher the value of assets the lower the interest rates of the debt to be secured by those assets. Subsequently, it is assumed that there is a strong positive relationship between collateral and access of debt financing by SMEs.

I.4.3 The moderating effect of age on the relationship between quality of financial information and access to finance.

Chandler (2009) proclaims that older firms deliver a resume which lenders can use to device their credit worthiness. Abdul Saleh (2013) also recognised that experience enhances the availability of credit. Similarly, Kamweru (2011) contends that firms that are younger have no traditional credit history that providers of external finance can use to assess their creditworthiness as such they are more inhibited in the use of external financing. Conversely, he opposes that older firms have a deep-rooted credit history and have built a good reputation with providers of external finance as such are less inhibited in the use of external finance.

The charisma and the credit history which older firms create over the years in undertaking business decrease the challenge of information asymmetry in quality of financial statement disclosure and hence aid the firms to easily access external financing (Frazer, 2005). Ssentamu (2016) upholds that being in the business for many years propose that at least the firms are competitive on average. Information that is required by banks to appraise and process loan application may be more presented with older firms than the new firms (Ssentamu, 2016).

I.4.4 The moderating effect of age on the relationship between collateral availability and access to finance.

Age of the firm is a very vital factor of access to credit considered by banks, (Pandula, 2011) revealed that new firms are not probable to meet the collateral obligations of the credit institutions since they have not amassed adequate asset. Additionally, inadequate collateral combine with non-appearance of information on financial record may make it problematic for new firms to access credit.

According to Klapper, Sarria-Allende and Sulla (2002), younger firms (those established less than four years), are more dependent on informal financing and far less on bank financing this is accredited to absence of sufficient collateral. This is reinforced by Quartey (2003) who determined the significant positive effect of firm age on the ability to access external finance. In addition, in their examination of the impact of firm and entrepreneurial characteristics on SME access to debt finance in South Africa (Fatoki & Asah, 2011) detected that SMEs that were put in place more than five years have a far healthier chance to be successful in their credit applications compared with SMEs that were put in place for less than five years.

I.5 Literature summary and gap

This study has reviewed a number of related studies about factors or drivers to access of finance by small and medium enterprises however there is a lot of generalization that's to say in the whole country without particularly focusing on a given area hence there is a contextual gap as conclusions can't be made out of generalization for a particular area. The diversity of factors responsible for suboptimal access to finance identified in literature indicates that the search for efficient factors of access to finance by SMEs is still emerging. Moreover, although empirical studies have been carried out to explain the limited access to finance using different predictor variables (Nanyondo et al., 2014; Mwihaki, 2015 & Ssentamu, 2016). The effect of quality of financial statements, collateral availability has not been excessively studied in the Ugandan setting.

This study therefore argued that the limited access to finance by SMEs could be attributed to quality of financial statements, collateral available as they are moderated by firm age. Finally, there are scanty studies that have analysed the effect of moderating variables like age on the relationship between say financial characteristics and access to finance. Therefore, this study intended to fill both the contextual and conceptual gaps by assessing the effect of financial characteristics on access to finance contingent to age of the firm by small and medium enterprises in Uganda.

I.6 Theoretical framework of SME

I.6.1 Definitions of SME

While there is broad acknowledgement of the role of the SME sector internationally, defining SMEs remains a challenging task. In fact, there is no one generally agreed definition for "small and medium-sized enterprises" applicable in all countries.

The definitions of SME can be subdivided into two distinct approaches according to the reference criteria used: on the one hand, definitions based on criteria endogenous to the company such as the human dimension, turnover. And on the other hand, those using criteria exogenous to the company such as the sector of activity and the legal form.(HANI)

I.6.2 Definition according to criteria endogenous to the company

It should be noted that according to these criteria, we can identify the concept of SME according to two indicators, namely: the descriptive indicator known as a quantitative indicator, and the analytical indicator also called qualitative indicator.

All different in the way of treating the company, the indicators, already cited, are parallel to the neoclassical analyses of the firm. In fact, of course they are distinct but not very far from being complementary. Note that the quantitative indicator is limited to the description of the most visible elements of the company, while the qualitative indicator takes into account the relationship of the company with its environment. In doing so, it is based on a much more managerial and organizational approach. Therefore, distinctive but also complementary, the criteria that these two indicators use are of the same nature. Whether quantitative or qualitative, all within the company.(Islamic Microfinance, 2004)

I.6.2.1 *Quantitative indicators*

According to this approach, which is also known as the “statistical approach” criteria of quantitative nature are used to define SMEs. As such, the size of the firm is determined based on some selected quantitative criteria. In fact, quantitative-based definitions of SMEs are the most popular ones used by researchers as well as policy makers. These indicators are based on a set of criteria which, as a whole, are measurable and quantifiable, namely:
− The number of employees employed;
− Turnover;
− The amount of share capital committed.

I.6.2.2 *Qualitative indicators.*

The qualitative methods for defining SMEs tend to focus on particular characteristics of SMEs that are inherent in their nature. These indicators closely match economic reality. They try to emphasize to a greater or lesser degree the distinctive elements of an SME, and use more or less differentiated criteria. In this context, we will retain the most important ones, namely:
− The human dimension and the quality of company management;
− Management strategies and objectives.
− Others, such as: lack of strong position on the market, difficulties in obtaining credit, inability to resort to financial markets and relatively strong integration into the local community to which the owners and directors belong, as well as a greater or lesser dependence on neighbouring sources of supply.

I.6.3 Definition according to criteria exogenous to the company

The so-called exogenous criteria for the company make it possible to classify SMEs into more or less homogeneous categories, which can be cited as follows:
− The legal nature of the company;
− The type of activity;
− The quality of the sector of activity.

I.6.3.1 *Definition according to the legal framework.*

The forms taken by companies classified according to the legal framework are diverse and varied. There are private companies, public companies and cooperative companies.(HANI)

I.6.3.1.1 *Private companies*

This type of business is legally characterized by the ownership of the capital which belongs to a family, a person or an association of people. This typology allows the following distinction:

The Individual Business: it is easy to set up, but it presents significant risks to the extent that there is no separation between the assets of the business and those of the owner.

The Collective Name Company: it is made up of a group of partners; all liable indefinitely for the company's liabilities, that is to say, they are required to settle the company's debts to its creditors from their own assets, regardless of the amount of their contributions.

The Limited Liability Company: the partners of a limited liability company are liable up to the amount of their contributions. The incapacity or bankruptcy of a partner does not lead to the disappearance of this type of business. Shares are not negotiable and can only be transferred under certain very strict conditions; which brings them closer to companies based on interests. The limited liability company has a minimum of two partners and a maximum of fifty.

The joint stock company: it is a company organized in the form of a commercial company having a capital whose subscription by the partners has been the subject of the issue of securities representing the capital, the shares or shares issued to subscribers or associates, hence called shareholders.

The Single Person Limited Liability Company: It is a particular variant of the limited liability company. It is made up of a single person (natural or legal); and allows the individual entrepreneur not to commit his entire personal assets.
In view of the advantages presented by the last two forms of business in terms of operational flexibility and implicit in the constitution and transfer of shares, they seem to be the preferred choice for the creation of SMEs.

I.6.3.2 *Public companies*

Public companies are companies which belong entirely or in majority (through capital and decision-making power) to a public authority (State, local authority, etc.).

These companies operating in commercial productive activities, and whose number is today tending to be reduced with the implementation of privatization programs, have varied objectives depending on their situation. We distinguish in this context:
Authorities: having no legal personality, they are managed by civil servants.
Public establishments: have a legal personality and an autonomous budget. Led by a board of directors and a general manager. These establishments can be hospitals, universities, schools, etc., and can have the character of a public industrial or commercial establishment.
National companies: which appeared following the nationalization of private companies, are similar to public limited companies with a single shareholder, namely the State; managed by a board of directors bringing together representatives of the state, users and consumers and a CEO appointed by the state from among the members of the board of directors. **Mixed economy**

companies: are limited companies bringing together public and private capital.(Abdulsaleh, 2013)

I.6.3.2.1 *Cooperative enterprises*

Cooperative enterprises can be defined as collective enterprises whose members, associated with equal rights and obligations, pool work and capital to satisfy their needs without depending on the market. Their major objective is not profit maximization, and their activities are carried out in many sectors such as: production, crafts, retail, insurance and construction.(Abdulsaleh, 2013)

Given the advantages offered, namely the simplicity of distinction by the conditions of incorporation and particular strategic objectives, the classification of SMEs according to the legal framework seems to be useful. However, limiting oneself to the legal criterion alone makes this distinction delicate, because of the abstraction made of the specificities of each productive unit.(Abdulsaleh, 2013)

I.6.3.3 *Definition according to the quality of the sector of activity*

At this level, we distinguish two types of distribution: classic distribution and modern distribution of the type of activity.

I.6.3.3.1 *The classic distribution*

Companies can be classified according to this type of distribution into three sectors:

Primary sector: which brings together all agricultural companies or those working in the fields of extraction or logging, in other words it is all companies whose main activity is the extraction or exploitation of natural resources.

Secondary sector: concerns all companies whose main activity consists of producing economic goods considered as outputs of processing operations.

Tertiary sector: it covers all companies whose main function is to provide services to businesses or individuals.

However, given the changes made during the industrial revolution of the 18th century and the progress made throughout the world in recent years, this distinction no longer has much meaning, which has also given rise to a new distribution of activities.(Abitekaniza, 2017)

I.6.3.3.2 *Modern distribution*

This new vision reveals many sectors of economic activity which were neglected by the old method, namely: energy, transport equipment, construction, trade, transport and telecommunications, etc.

I.6.3.4 *Definition according to the quality of the sector of activity*

This classification method is based, as its name indicates, on the quality of the sector of activity. Therefore, it allows the distinction between what we call the traditional sector characterized by the preponderance of the labour factor, the non-modernization of equipment, and the absence of

technological innovations, and the modern sector characterized in turn, by the independence of companies in this case SMEs and the appearance of what is known as subcontracting SMEs.

I.7 Distinction Between SMEs/SMIs and Start-ups

Conceptualizing SMEs/SMIs and start-ups poses challenges, but it is essential to explore the specifics, definitions, and distinctive variables that define them. There is no universal consensus on the definitions of SMEs/SMIs and start-ups, but these entities are often studied due to their global relevance, contributing to diversification and national wealth creation.

The definition of SMEs and start-ups generally relies on qualitative considerations, although precise quantitative criteria are often used for statistical, fiscal purposes, or to determine eligibility for support or financing programs (Niyungeko, 1993). The distinction between the two relies on several criteria, such as the size of the company in terms of the number of employees, turnover, balance sheet, and investments in research and development. These criteria help determine whether a company falls into the category of start-ups or SMEs, thus influencing its eligibility for government support and financing programs.

I.7.1 What is a Startup?

The definition of a Startup is not clearly defined and is subject to a multiplicity of concepts and interpretations. Research tends to attribute to them either an "institutional definition with quantitative terms, or a managerial aspect with qualitative terms" (Dalex, 2020). The term "start-up" is widely used in various fields of economic and social activities, although it does not yet have a precise and uniform definition (Brosia, 2016).

I.7.1.1 *The Quantitative Aspect of Start-ups*

In reference to research in the field of innovation, start-ups are institutionally classified based on the innovative activities declared by various national and international organizations. Table 0.1 below presents some quantitative aspects attributed to these so-called "innovative" young companies

Table 0.1:Quantitative Definitions of Start-ups

Organization/Institution	Definition attributed to startups
OECD	A firm engaged in technological innovation of product and process for a period of one year.
European Commission EC	Young Innovative Companies (YIC) under 6 years of existence, having less than 250 employees, and allocating at least 15% of their budget to R&D.
Main European Countries	To qualify as a startup, the company must simultaneously meet five conditions in accordance with Article 44 sexies-0 A of the

	General Tax Code:

Source: Table created based on the work of (Dalex, 2020).

I.7.1.2 *The Qualitative Aspect of Start-ups*

Beyond recent definitions, which converge towards a quantitative orientation, the conceptualization of start-ups has evolved towards a qualitative perspective, emphasizing the criterion of innovation and the adoption of new technologies.

Key visionaries of these "young sprouts" highlight the diversity of approaches to define these companies. According to (Blank, 2010), a start-up is a temporary entity searching for a scalable business model to enable exponential growth.
This definition suggests that start-ups are ephemeral entities in search of innovative business models to stimulate their growth.

(Ries, 2015), author of "The Lean Start-up," offers another definition: "A start-up is a business structure organized by individuals seeking to design a new product or service under conditions of extreme uncertainty." This definition adds two essential dimensions to the commercial activity of innovative companies: the human dimension, crucial for agile entrepreneurship, and the introduction of the concept of a new product or service as the ultimate goal surrounding the innovative company.

For McClure (2013), a renowned American investor and founder of 500 Startups, an investment fund and incubator, the fundamental principle of uncertainty characterizes the emergence of a start-up. According to McClure, "A start-up is a company that does not clearly know: what is its product? Who are its customers? How to make money? As soon as it discovers these three elements, it ceases to be a start-up and becomes a real company."

I.7.2 Distinctions Between Small and Large Enterprises

Compared to large enterprises, SMEs/SMIs adopt a greater number of management practices focused on flexibility, considered one of their most notable distinctive characteristics. This flexibility is a major advantage, allowing SMEs to respond quickly, innovate, and adapt to changes, according to (Galetic, 2011).

The simplicity of SMEs' internal organization is the source of their increased flexibility, offering them the ability to adjust and react more promptly to market developments. However, faced with the internationalization of the economy, rapid and uncertain changes, increasing competition, the need for constant innovations, and the growing use of information technologies, companies are challenged to improve their competitiveness, diversify their activities, and conquer market shares nationally and internationally.

These challenges are particularly pronounced for SMEs due to their smaller economies of scale and more limited resources compared to large enterprises. It is thus crucial to highlight some common characteristics that distinguish SMEs/SMIs. Generally, these companies stand out for their personalized management of activities. Their decision-making processes are often simple, promoting speed and efficiency. Moreover, they typically exhibit low specialization, with versatile employees. Their internal information systems are simple, facilitating rapid information

dissemination within the company, while their external information systems are also straightforward due to often geographically proximate markets.

A specific classification is given to the legal categories of SMEs/SMIs and their attributes. Hence, the most recent research supports that the effects of laws on entrepreneurship cannot be anticipated a priori using models of universal application. Each country has its own regulatory directives. Deakin S. believes that the legal aspect of SME entrepreneurship has effects that depend on the interaction of legal norms with various national regional, and sectoral conditions, as well as with complementary institutions on financial and product markets" (Deakin, 2011)

I.8 SMEs in Uganda

The first difficulty that any researcher faces when approaching a research object lies in choosing an adequate definition. In fact, several definitions coexist, varying depending on the qualitative or quantitative approach adopted.

A definition can be selected based on its relevance to the specific scope. Thus, a financial researcher will probably favour a definition of SME based on financial criteria such as independence or the family nature of capital. On the other hand, a marketing researcher will look more at criteria such as the extent of the market and the mode of relationship between the manager and his customers. As part of our end-of-study project in monetary and banking economics, the subject of our reflection is of a general nature. Consequently, we will seek to retain a global definition that can serve as a reference within the scientific community specializing in the study of SMEs. And in this context, an important question crosses our minds: what concept of SME to retain in this statement?(Berger, 1998)

Regarding the case of Uganda, Small and Medium-sized Enterprises (SMEs) in Uganda, according to the Uganda Investment Authority (UIA) and the Ministry of Finance, Planning, and Economic Development, was based on the number of employees, annual turnover, and annual balance sheet total.

As per the Uganda Investment Authority (UIA) and the Ministry of Finance, Planning, and Economic Development in Uganda, the classification of SMEs is typically as follows:

1. Micro Enterprises:
    - Employees: Up to 5
    - Annual Turnover: Up to UGX 10 million

2. Small Enterprises:
    - Employees: 6 to 50
    - Annual Turnover: UGX 10 million to UGX 100 million

3. Medium Enterprises:
    - Employees: 51 to 100
    - Annual Turnover: UGX 100 million to UGX 360 million

Table 0.2: Ranking of SMEs according to size

Size	Number of staff	Turnover

Micro enterprise	Up to 5	10 millionugx
Small enterprise	6 to 50	10 to 100 million
Medium enterprise	51 to 100	100 to 360 million

Source; (Doing Business Report , 2015)

I.8.1 Start-ups in Uganda

The start-up ecosystem in Uganda has been experiencing remarkable growth over the past decade. With a youthful population, increasing access to technology, and supportive government policies, Uganda has become a fertile ground for entrepreneurial ventures. This section explores the key sectors, notable start-ups, support ecosystem, challenges, and opportunities in Uganda's start-up landscape.

I.8.1.1 ***Key Sectors***

Technology and Innovation**.** The technology sector in Uganda is vibrant, with start-ups leveraging innovations to solve local problems and enhance efficiencies. Fintech is a leading sub-sector, driven by the widespread adoption of mobile money services pioneered by companies like MTN Mobile Money and Airtel Money. These platforms have transformed financial transactions, enabling millions of Ugandans to access financial services.(Berger, A More Complete Conceptual Framework for SME Finance., 2006)

Agritech is another growing area, with start-ups such as EzyAgric providing technological solutions to farmers. These solutions include mobile applications that offer weather forecasts, market prices, and access to agricultural inputs, helping farmers increase productivity and market access.

Healthtech startups are also making significant strides. For instance, the development of telemedicine platforms and health management systems aims to improve healthcare delivery and access, particularly in rural areas.

Agriculture. Agriculture remains the backbone of Uganda's economy, and startups in this sector are leveraging technology to enhance farming practices and supply chains. Startups like Akorion and Ensibuuko are providing digital platforms that connect farmers to markets, offer financial services, and provide data-driven agricultural advice.

Education The education sector has seen the emergence of edtech startups creating online learning platforms, digital educational content, and tools for skills development. Companies such as KAINOafrica are transforming education by making quality learning resources accessible to students and educators across the country.

Renewable Energy With a significant portion of the population lacking access to reliable electricity, renewable energy startups are crucial in bridging this gap. Companies like SolarNow and Fenix International offer affordable solar energy solutions, providing sustainable power to off-grid communities and promoting environmental conservation.(Alfo, 2006)

I.8.1.2 *NotableStartups*

SafeBodaSafeBoda is a motorcycle taxi service that prioritizes safety and reliability. It connects riders with professionally trained drivers through a mobile application, enhancing the safety and efficiency of urban transportation. SafeBoda has expanded its operations beyond Uganda, demonstrating the scalability of Ugandan startups.
Kuda. Kuda offers digital banking services aimed at enhancing financial inclusion. By providing an accessible, user-friendly banking platform, Kuda enables individuals and small businesses to manage their finances more effectively and securely.
SolarNow. SolarNow provides solar energy solutions to rural and peri-urban communities. Their products include solar home systems, solar water pumps, and solar refrigerators, which contribute to improving the quality of life and economic activities in underserved areas.
EzyAgric. EzyAgric is an agritech startup that offers a comprehensive platform for farmers. It provides services such as access to agricultural inputs, real-time market information, and financial services. EzyAgric's innovative approach helps farmers increase productivity and profitability.(Allen, 1995)

I.8.1.3 *Challenges and opportunities.*

Despite the positive trends, startups in Uganda face several challenges:
Access to Capital Securing initial and growth-stage funding can be difficult for many startups. Limited access to capital hinders the ability of startups to invest in research, development, and expansion.

Regulatory Environment Navigating the regulatory landscape can be complex and bureaucratic. Startups often encounter challenges in complying with regulatory requirements, which can impede their growth and operational efficiency.
Infrastructure Inadequate infrastructure, particularly in rural areas, poses significant challenges for startups. Issues such as unreliable electricity, poor internet connectivity, and inadequate transportation networks can limit the scalability and reach of startups.
Market Access Reaching a broader market beyond local boundaries can be challenging. Startups need to develop strategies to expand their customer base and enter new markets, both regionally and internationally.(Atieno, 2001)

I.8.1.4 *Opportunities*

Digital Transformation The increasing internet penetration and smartphone usage in Uganda present vast opportunities for digital businesses. Startups can leverage digital platforms to reach wider audiences, offer innovative solutions, and enhance operational efficiencies.
Youth Demographics Uganda's young, tech-savvy population drives demand for innovative products and services. Startups that cater to the needs and preferences of this demographic have significant growth potential.
Regional Expansion.The East African Community (EAC) provides opportunities for Ugandan startups to expand their operations to neighbouring countries. The EAC's common market and trade policies facilitate cross-border business activities, enabling startups to tap into new markets and scale their operations.

The startup ecosystem in Uganda is characterized by vibrant entrepreneurial activity, driven by a dynamic youth population, technological advancements, and supportive policies. While challenges such as access to capital, regulatory complexities, and infrastructure limitations

persist, the opportunities for growth and impact are substantial. By leveraging the supportive ecosystem and addressing the existing challenges, Ugandan startups have the potential to drive economic development, create jobs, and contribute to sustainable growth.(HANI)

I.8.2 The General roles of SMEs in the Ugandan Economy

Employment Generations are a major source of employment in Uganda, significantly contributing to job creation across various sectors. They provide opportunities for both skilled and unskilled labour, thereby reducing unemployment rates and enhancing livelihoods. According to a report by the Uganda Bureau of Statistics, SMEs employ approximately 90% of the total non-farm private sector workers, highlighting their critical role in the labour market.

Economic Growth, SMEs contribute significantly to Uganda's GDP by stimulating local economies through diverse business activities. These enterprises drive economic growth by fostering innovation, enhancing productivity, and promoting economic diversification. According to the Uganda Investment Authority, SMEs account for over 20% of the GDP and are crucial in driving economic resilience.

Innovation and Entrepreneurship, SMEs are often at the forefront of innovation, introducing new products and services to the market. They cultivate an entrepreneurial culture, encouraging creativity and the development of novel business ideas. This innovation meets local demands and opens new markets, both domestically and internationally. For instance, Techno Brain, an SME in Uganda, has developed innovative IT solutions that are now used across Africa.

Income Distribution, by providing employment and entrepreneurial opportunities, SMEs help in the equitable distribution of income. They enable a broad segment of the population to engage in economic activities, which is crucial for reducing income inequality and poverty. The role of SMEs in income distribution is particularly evident in rural areas, where they offer alternative livelihoods to agriculture.

Export Promotion, SMEs in Uganda contribute to export promotion by producing goods for regional and international markets. Sectors such as agribusiness, handicrafts, and manufacturing have seen significant SME involvement in exports, boosting foreign exchange earnings and improving the trade balance. An example is Mukwano Industries, which started as an SME and now exports products to several countries in East Africa.

Industrialization and Urbanization, SMEs support the processes of industrialization and urbanization by establishing small-scale industries and businesses in urban and peri-urban areas. They contribute to infrastructure development and urban growth, generating demand for urban services and goods. In Kampala, the capital city, SMEs are pivotal in the development of local industries and the urban economy.

Supply Chain Development, SMEs play a critical role in supply chain development by acting as suppliers and distributors for larger firms. They provide essential goods and services, creating a symbiotic relationship that enhances overall economic efficiency. For example, in the agricultural sector, SMEs supply inputs and services vital for larger agribusiness operations.

Social Stability, by providing economic opportunities and reducing unemployment, SMEs contribute significantly to social stability. The economic engagement of a larger segment of the population helps mitigate risks of social unrest and promotes peace. This role is particularly

important in post-conflict areas of Uganda, where economic revitalization is essential for long-term stability.

Government Revenue, SMEs contribute to government revenue through taxes, business licenses, and other regulatory fees. This revenue is crucial for funding public services and infrastructure projects, further supporting economic development. The fiscal contributions of SMEs are vital for the government's budget, particularly in sectors such as healthcare and education.

The multifaceted roles of SMEs in the Ugandan economy underscore their importance as engines of growth, innovation, and social stability. Understanding these roles provides a foundation for analysing the financial challenges SMEs face and the strategies private banks can adopt to support their development.(Amito, 2023)

I.8.3 Challenges and Opportunities by SMEs in Uganda

I.8.3.1 *Challenges*

Access to Finance, Access to finance remains the most significant challenge for SMEs in Uganda. Many SMEs struggle to secure loans from private banks due to stringent collateral requirements, high-interest rates, and a lack of credit history. This financial barrier limits their ability to grow, invest in new technologies, and expand operations.

Regulatory and Compliance Issues, SMEs in Uganda face complex regulatory and compliance challenges. Navigating the bureaucratic requirements for business registration, taxation, and obtaining necessary permits can be overwhelming for small business owners. Additionally, regulatory changes and corruption further complicate these processes, impeding business operations and growth.

Market Access, Limited market access is another major challenge for Ugandan SMEs. High transportation costs, competition from larger firms, and inadequate market information restrict their ability to reach both local and international markets. SMEs often lack the marketing expertise and resources needed to effectively promote their products and services, limiting their market reach.(Garrafa)

I.8.3.2 *Opportunities*

Expanding Financial Services, Innovations in financial technology (fintech) and the growth of mobile banking present significant opportunities to improve access to finance for SMEs in Uganda. Mobile money services and digital lending platforms can provide alternative financing options for SMEs that lack access to traditional banking services.

Government Support Programs, The Ugandan government offers various support programs aimed at fostering SME growth. These include grants, subsidies, and business development services provided through agencies like the Uganda Investment Authority and the Uganda Development Corporation. Strengthening and expanding these programs can provide much-needed support to SMEs.

Market Expansion through Regional Integration, The East African Community (EAC) integration presents a valuable opportunity for Ugandan SMEs to access larger regional markets. This regional integration can lead to increased trade and business expansion beyond national borders, offering new growth avenues for SMEs.

While access to finance, regulatory and compliance issues, and limited market access are major challenges for SMEs in Uganda, significant opportunities exist to overcome these barriers. Expanding financial services through fintech, leveraging government support programs, and capitalizing on regional market integration can enhance the growth and sustainability of SMEs. Addressing these challenges and harnessing these opportunities will be crucial for maximizing the contribution of SMEs to Uganda's economic development.(Garrafa)

I.9 Conclusion

In conclusion, SMEs are the backbone of Uganda's economy, playing a crucial role in driving growth, job creation, and innovation. Despite their significant contributions, these enterprises face considerable challenges in accessing finance from private banks, primarily due to stringent collateral requirements, high-interest rates, and limited credit history. The theoretical frameworks, including the Resource-Based Theory and the Life Cycle Theory of Consumption, underscore the importance of financial resources and developmental stages in shaping access to finance. Empirical evidence supports that quality financial statements, available collateral, and firm age significantly influence banks' willingness to extend credit to SMEs. Addressing these financial barriers is essential for unlocking the potential of SMEs to contribute more effectively to Uganda's economic resilience and growth.

However, there are significant opportunities to enhance SME financing through innovations in financial technology, government support programs, and regional market integration. Fintech solutions, such as mobile money services and digital lending platforms, offer alternative financing options for SMEs lacking access to traditional banking services. Government initiatives, including grants and business development services, provide essential support to foster SME growth. Moreover, regional integration within the East African Community presents valuable opportunities for market expansion and increased trade. By leveraging these opportunities and addressing existing challenges, private banks and other stakeholders can support the sustainable development of SMEs, ensuring their continued impact on Uganda's economic development and social stability

CHAPTER TWO: THE ROLE OF PRIVATE BANKS IN FINANCING SMES AND FACILITATING INTERNATIONAL TRADE IN UGANDA.

Chapter two: the role of private banks in financing Smes and facilitating international trade in Uganda

II.1 Introduction

Private banks in Uganda play a crucial role in financing SMEs, which are vital to the country's economic growth and employment. This chapter explores the banking sector in Uganda with a focus on private banks, the methods and types of financing they provide to SMEs, and their role in facilitating international trade.
First, we provide an overview of the banking sector, highlighting the structure and key players. Next, we examine the various financing options available to SMEs, including traditional loans, microfinance, and innovative financial products. Finally, we discuss how private banks support SMEs in international trade through trade finance, letters of credit, and other financial instruments.
By understanding these roles, we gain insights into how private banks can better support the growth and sustainability of SMEs in Uganda.

II.2 The Banking Sector in Uganda

II.2.1 Overview of the Banking Sector

The banking sector in Uganda has been through colorful transitions which have led to its prevailing state moment characterized by a large number of fiscal institutions with different power structures and a full range of fiscal services. ultramodern formal banking in Uganda dates back to 1903 when Standard Chartered Bank opened its doors in Kampala. Barclays Bank followed in 1927, and by 1966 a modest aggregate of 41 marketable bank branches were in operation- countrywide. By 1972, 12 locally possessed marketable banks was and the expatriation of Asian possessed businesses by President Idi Amin in 1972 led to the unknown indigenization and nationalization of the banking sector. By the 1980s, the deteriorating political and profitable climate had an accumulative impact on the banking sector.

This combined with poor bank supervision and regulation, and the liberalization of fiscal requests, led to a period of habitual insecurity characterized by the collapse of several marketable banks and the loss of public confidence in the banking system. Reforms since 1986 have been geared towards rehabilitating and resuscitating the fiscal sector so that it effectively contributes to the process of profitable development. The first imperative was the restoration of macroeconomic stability that was lost in the 1970s. posterior achievement of this thing has created a conducive provident terrain within which the fiscal sector would be suitable to contribute to posterior development pretensions and also realize that it was vital to the success of all other development strategies. The preface of the Structural Adjustment Programs (SAPs) and Economic Recovery Programs (ERPs) was accompanied by financial and financial programs aimed at liberating interest rates, strengthening the external value of the currency, and correction of the financial protuberance and affectation in the frugality. These primary programs were gradationally unfolded over a period of about ten times from 1986 to the liberalization of the frugality in 1996. The liberalization of the frugality and fiscal sector is regarded as a mixed blessing but it has offered the fiscal sector openings and challenges. moment, the Bank of

Uganda (BoU) is confident that the current position of fiscal reforms, profitable and political stability combined with the nonsupervisory and administrative frame will insure a vibrant and healthy fiscal sector that's suitable to support the public ideal of poverty eradication and the development of Uganda into a middle- income status country.

II.2.2 Types of Banks in Uganda

Representative services of foreign banks; These are legal realities representing a bank or fiscal institution from another country, furnishing guests with information on products and services of the head office and promoting the conclusion of deals, but not furnishing fiscal services or similar services are limited or banned by legislation.

Foreign marketable banks; These are banks incorporated outside Uganda but operating through a branch and attachment. moment there are a number of foreign banks substantially from the West. Credit Institutions A credit institution is a company that has as its top business the provision of credit installations to the public or a section of the public.

Credit institutions, have an accreditation to rally savings and give credit, especially to the pastoral population and growers. A good illustration moment in Uganda of a credit institution is a microfinance. Credit institutions are certified under the Financial Institutions Act.

Marketable banks. A marketable bank is any bank that's incorporated under the Companies Act. These are the largest number of banks in Uganda moment. Only marketable banks are authorized to take part in plutocrat creation through deposit multiplier. A marketable bank is a fiscal conciliator that accepts deposits from savours and, in turn, makes loans to borrowers. They make a profit by the difference between the interest rates on the loans and the interest rates paid out on the deposits.

There are colorful types of banks in Uganda, which can all be distributed according to the law and regulation under which they were certified and the type of power. piecemeal from the central bank that's the Bank of Uganda, there are four orders of banks in Uganda presently offering banking services to the public. They include marketable banks, credit institutions, foreign marketable banks, and representative services of foreign banks.(Procedure, 2012)

II.2.3 Role of the Central Bank

The central bank, often regarded as the cornerstone of a country's financial system, plays a pivotal role in maintaining monetary stability, regulating financial institutions, and fostering economic growth. As the primary monetary authority, the central bank wields significant influence over key economic indicators such as inflation, interest rates, and exchange rates. Through its monetary policy tools and regulatory oversight, the central bank aims to ensure price stability, promote a sound and stable financial system, and support sustainable economic development. With its mandate to safeguard the integrity and stability of the financial sector, the central bank serves as a guardian of financial stability and a linchpin of the national economy.

Through enforcing a stable environment of macroeconomic conditions, such as low and stable inflation rates and stable exchange rates, the central bank fosters confidence in the economy both from within and from foreign investors. This, in turn, promotes sustained investment, growth, employment, and poverty reduction in Uganda.

To build a strong and competitive economy, the central bank implements policies aimed at creating stable economic conditions and an environment conducive to sustained economic growth and development. It works to create a suitable mixture of a conducive private sector to ensure efficiency and democracy in the economy. This is done through monitoring the exchange rate and promoting economic growth, high growth of potential output, and increasing employment in the economy.

A sound financial system is one that is able to mobilize resources and allocate them efficiently towards high investment and growth in the economy. The central bank implements monetary policies with the objective of fostering price stability and a sound financial system. It does this by regulating the inflationary pressures on the economy.

The central bank (Bank of Uganda) was established by the Bank of Uganda Act, 1966. It started operating on the 15th of August 1966. Prior to its establishment, the functions of a central bank were carried out by the East African Currency Board. According to the Bank of Uganda charter, the roles of the central bank are to foster price stability and a sound financial system.(Procedure, 2012)

II.2.4 Key players

II.2.4.1 *Commercial Banks.*

The Ugandan commercial banking sector plays a pivotal role in the country's financial system. It comprises licensed commercial banks that offer a range of financial services to individuals, businesses, and government entities. For example, Stanbic bank, Centenary bank, Post bank, KCB bank, Bank of Africa, Equity bank among others.
Clearly! The part of marketable banks in Uganda is multifaceted and pivotal for the country's frugality. Let's explore their functions.

Financial Intermediation. Commercial banks act as interposers between depositors (individualities and businesses) and borrowers. They accept deposits from the public and give loans to individualities, businesses, and government realities. By easing lending and borrowing, they contribute to profitable growth and development.

Monetary Policy, perpetration marketable banks play a vital part in enforcing the central bank's financial policy. They acclimate interest rates, manage liquidity, and influence credit vacuity grounded on the central bank's directives. Through open market operations, they buy or vend government securities to regulate plutocrat force.

Payment Services marketable, banks offer colourful payment services, including Checking accounts Easing day- to- day deals. Electronic finances transfers Enabling flawless plutocrat transfers. Credit and disbenefit cards Supporting cashless deals. ATMs furnishing accessible access to cash. Credit Provision They extend credit to individualities and businesses for

colourful purposes Working capital loans to finance diurnal operations. Business expansion loans for growth and investment. Consumer loans similar as particular loans and mortgages.
Risk Management; Commercial banks assess and manage pitfalls associated with lending. They estimate borrowers' creditworthiness, collateral, and prepayment capacity. Effective threat operation ensures stability and minimizes losses.

Foreign Exchange Services Banks grease foreign exchange deals, including buying and dealing currencies. They issue letters of credit, handle transnational trade payments, and offer foreign exchange services to businesses.

Information Banks marketable banks collect profitable, statistical, and fiscal data related to trade, commerce, and assiduity. This information aids decision- making by businesses, policymakers, and investors. Merchant Services numerous marketable banks give trafficker services, including credit card processing, mobile payment results, gift cards, and electronic check services.

In summary, marketable banks in Uganda serve as critical pillars of the fiscal system, supporting profitable conditioning, managing pitfalls, and promoting fiscal addition.(Beck, 2005)

II.2.4.2 ***The micro finance Sector.***

The microfinance sector in Uganda is critical in providing financial services to micro-entrepreneurs, small enterprises, and low-income individuals who may have limited access to standard banking services. Of financial services tailored to the needs of their clients. These services may include; Small loans provided to micro-entrepreneurs and small businesses for working capital, asset acquisition, or business expansion, Deposit accounts designed to mobilize savings from low-income individuals, often with low minimum balance requirements and flexible withdrawal options, Insurance products designed to protect clients against risks such as illness, death, crop failure, or property damage, Capacity-building initiatives to enhance clients' financial literacy, business skills, and knowledge of financial products and services, Facilitation of remittances and payment services to enable clients to send and receive money securely and efficiently.

Microfinance institutions play a crucial role in poverty alleviation, economic empowerment, and financial inclusion by providing access to finance and promoting entrepreneurship and self-employment. Despite its growth and impact, the microfinance sector in Uganda faces several challenges, including limited access to capital, high operating costs, governance issues, and inadequate infrastructure. However, there are also opportunities for innovation and growth, including leveraging technology, developing new products and delivery channels, and strengthening regulatory oversight and consumer protection mechanisms.

Overall, the microfinance sector in Uganda continues to evolve and expand, playing a vital role in promoting inclusive economic growth, poverty reduction, and sustainable development. With the support of stakeholders, including policymakers, regulators, donors, and development partners, the sector has the potential to further deepen financial inclusion and empower marginalized communities across the country.(Beck, 2005)

II.2.4.3 ***The Development Bank***

Uganda Development Bank Limited (UDBL) is the country's only national development bank. The bank has a mandate of contributing to the policy of poverty eradication through sustainable socio-economic growth and development. It does this by providing financial support to projects that have a high developmental impact, or those that simply put, have a high likelihood of creating employment, adding value to domestic raw materials, and/or exporting goods and services. UDBL provides finance to its customers at competitive interest rates as well as financial and technical advice on how to run a business and management of the project. This is done to ensure that the projects undertaken by UDBL's customers are sustainable and are not likely to fail due to poor management.

The UDB was created to facilitate the economic and social development of Uganda with a view to improving the living standards of the people of Uganda. More specifically, the bank is to accelerate the industrial and economic development of Uganda by stimulating and supporting projects which are of a highly developmental nature, increasing the availability of loan capital and the terms on which it is available for investment in Uganda, and providing such advisory and other services as are deemed appropriate in the circumstances. UDB aims to support economically and socially viable projects, thereby contributing to the sustainable economic recovery and growth in Uganda. The Ugandan economy has over the years had a very low public and private investment rate. UDB is to reverse this trend by increasing the investment rate in the economy through investment in projects with both a short-term and long-term effect on the economy. In the short run, UDB will finance projects which are essentially rehabilitation in nature but in essence will contribute to productivity and income notably. An example of such a project would be the financing of a biogas project. In the long run, UDB will finance projects which will contribute to productive employment while raising income levels and quality of life for Ugandans. UDB will also guide its clients in the preparation and implementation of projects, fostering a good economic and financial understanding in the management of the project and transferring UDB's skills and experience to the clients and other financial institutions in Uganda.

The organisational structure of UDB is designed to efficiently fulfil its mandate and is currently based on a functional framework. The bank is a statutory body governed by a board of directors, currently chaired by Mr. Patrick Bitature, and a management team led by the Managing Director, Dr. Martin Aliker. The highest policy-making and oversight body is the board, which is responsible for setting the bank's corporate strategy. It guides and monitors the management team in the implementation of that strategy. The board itself is divided into several subcommittees, which focus on different aspects of the bank's activities and operations. The current management team is small, in order to contain costs, and this has necessitated a relatively flat line of command at UDB. All staff members are expected to be acquainted with the bank's operations at all levels and to perform several tasks outside the scope of their specific roles. This is seen as important in the continual development of staff skills and knowledge and also to ensure operational flexibility. Each of the UDB's functional units is headed by a manager, reporting to the head of operations, who in turn reports directly to the Managing Director. Currently, there are five functional units and five support units. Functional units are Business Development (which deals with the actual implementation of the bank's lending activities), Credit (which determines the bank's lending criteria and conducts risk analysis), Finance and Administration, Internal Audit, and Legal services. Support units are Human Resources, Information and Technology (IT), Strategic Planning and Research, Corporate Affairs, and Quality Assurance.(Laeven, 2006)

II.2.5 Challenges and opportunities

II.2.5.1 *Challenges*

High Cost-to-Income Ratio: Many banks in Uganda struggle with a high cost-to-income ratio, averaging around 68%. This inefficiency affects profitability and hampers their ability to provide cost-effective services.

Case Backlogs and Capital Paralysis: Approximately UGX 730 billion (Ugandan shillings) is tied up in court cases and processes, rendering it inaccessible to the wider economy. Addressing this challenge could unlock significant capital for investment and growth.

Limited Financial Inclusion: Despite growth in the number of accounts, Uganda's banking sector still lags behind mobile phone accounts. With nearly 40 million people, there are only 12.1 million bank accounts, highlighting the need for greater financial inclusion.(Laeven, 2006)

II.2.5.2 *Opportunities:*

Digital Payments Evolution: The payments landscape is shifting from paper-based transactions to digital or e-payments. Customers demand secure, integrated, and 24/7 payment experiences. Collaboration with fintech companies and telecom aggregators can enhance cost-effective financial services.

Agent Banking: Technology-driven agent banking can reduce costs while providing convenience to customers. By expanding agent networks, banks can reach underserved areas and improve financial access.

National Payments Policy: The Central Bank of Uganda is drafting a National Payments Policy to regulate digital payments, ensuring safety, efficiency, and flexibility for financial services players and the public.(Stiglitz, 1981)

II.2.5.3 *The Future Outlook of the Banking sector in Uganda*

The Ugandan banking sector is poised for growth and development. Key trends include a surge in digital banking services, with mobile and online banking gaining popularity due to their convenience and accessibility. Traditional banks are expected to dominate the market, with projected net interest income reaching US$3.19 billion in 2024. Additionally, there's a notable shift towards sustainable and socially responsible banking practices, as more Ugandan banks incorporate environmental and social considerations into their strategies. The country's high level of mobile penetration also influences the market dynamics.
In summary, expect continued expansion, increased digitalization, and a focus on responsible banking practices in Uganda's financial landscape.

II.3 Banking Innovations for SME Financing.

II.3.1 Methods of financing SMEs

II.3.1.1 *Banking and SMEs*

Banks play a vital role in providing financial services to SMEs such as line of credit financing and financial advice.
However, SMEs' access to bank financing can be complex due to various factors such as the size of the company, its financial stability and its ability to provide guarantees.
SMEs often rely on banks to obtain funds necessary for growth, investment and day-to-day management of operations.
Modes of Financing: This term typically refers to the broad categories or channels through which financing is obtained. It encompasses the overall approach or means by which SMEs acquire funding.(Stiglitz, 1981)

II.3.1.2 *Short-term credits*

The term short-term credits refers to all specialized financing techniques relating to the recovery of needs linked to the operating cycle, and on the other hand, means of financing whose duration is extremely short, ranging from a few days to a few months. To clarify this definition, it is necessary to examine the nature of the operations to which the credit is attached. Thus, depending on the nature of the production and marketing cycle, short-term credit can be relatively long and reach a period of around one year.

Due to the absence of mortgage guarantee and their very short term nature, these loans are particularly risky for banks. They are therefore granted after an in-depth study of the needs to be met and the financial structure of the company. In this context, these credits can be broken down into two categories:
- General operating loans: overdraft, bridging loan, companion loan, etc.;
- Operating credits for a specific purpose: the advance on merchandise, the warrant, intended to cover a particular operation.

II.3.1.3 *Mmedium- and long-term credits.*

Also called investment credits, they are intended to finance the upper part of the company's balance sheet; the repayment of this credit can only be ensured by the profits made. To grant these loans, the bank requires the company to have a minimum amount of equity. On average, the initial contribution is 30% of the amount of the financing need expressed.

II.3.1.4 *Medium-term credits.*

Medium-term loans are by definition loans whose duration is approximately between two and seven years. These credits are generally intended to finance the acquisition of light equipment, that is to say those whose depreciation period is equal to the repayment period of these credits.)

These credits can be mobilized, that is to say they can be financed by a mobilized organization (such as the central bank). This is not the case for non-mobilizable credits. The mobilization of credits is an operation by which the creditor (the bank) finds, from the mobilizing organization, the availability of the sums it has lent to its debtor.
Mobilization quite often requires obtaining, prior to any disbursement, “prior agreement” from the mobilizing organization.

Medium-term loans carry more risk of locking in losses than short-term loans. However, the risk of immobilization is avoided when there is a commitment, rediscounting with the central bank or any other mobilizing body. But this risk can reappear at deadlines if one or more beneficiaries of these credits default and request either the extension of a deadline, or even an adjustment of

several future deadlines. In this case, agreement with the mobilization organizations is difficult and the immobilization often remains the responsibility of the banker.(Coco, 2000)

II.3.1.5 ***Long-term credits.***

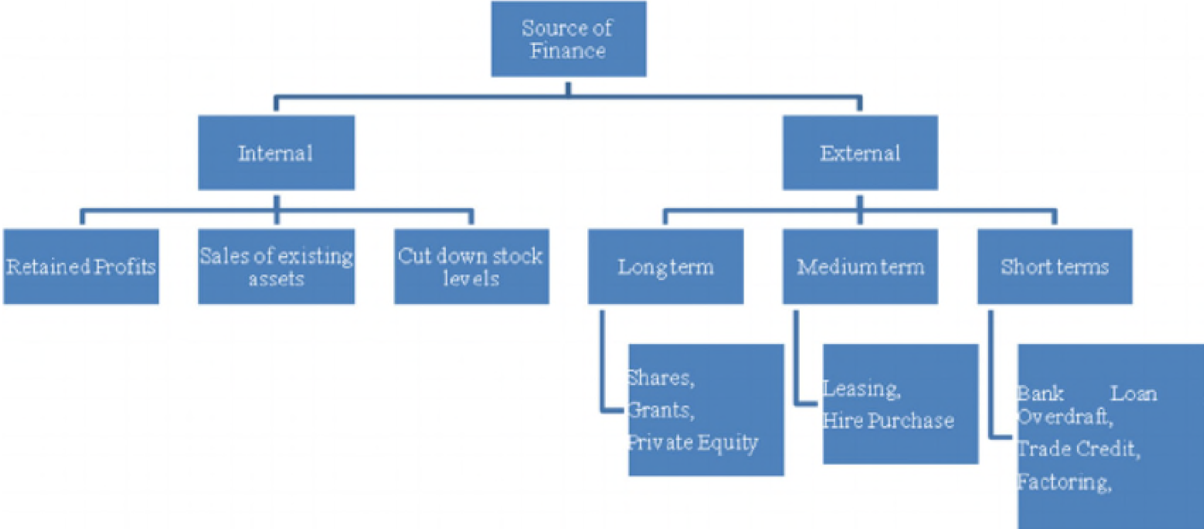
Long-term loans are, by definition, loans whose duration exceeds seven years. They are generally intended to finance major investments, that is to say those whose amortization period goes beyond seven years. Long-term loans are most often granted by specialized financial organizations.

In Uganda, in the era of the planned economy, the financing of planned productive investments on behalf of national companies was ensured for the medium-term part by the primary banks, for the long-term part, by the Uganda DevelopmentBank on public treasury resources.

In total, the risks of loss of credits in the medium and long term are greater because during the duration of the competition, the entrepreneur's business may decline for one reason or another. The banker must therefore carefully examine the repayment program and seek suitable guarantees.

Diagram representing the different financing methods

Figure II.1:Sources of finance.



Source: The impact of corporate characteristics on the financial decisions of companies: evidence on funding decisions by Italian SMEs, figure 2

II.3 Types of Financing for Small-Medium-Sized Enterprises

II.3.1 Equity Financing.

Equity financing is an important part of raising financial resources for the business ventures particularly for SMEs. One of the major challenges facing entrepreneurs is how to raise adequate levels of funding to finance their business concepts. For a relatively small business, it is easy to raise funds from an entrepreneur's savings that it is for a medium to large business start-up. To

this end, it is important that business entrepreneurs conduct feasibility studies to determine the level of financing their might require for their business concepts and how that the capital outlay may affect the type and source of financing (Daskalakis et al., 2013). Equity financing is defined as the capital investment into a business venture without expecting a return on a specific date, and more so, where the owner of the capital is basically investing in the business.

Access to SME financing is one of the most critical aspects of SME survival. Scholars like Birundu (2015); Berger et al., (2009); and Badulescu, (2011) posit that the growth on any SME venture is determined by access to finance at different stages of product and service development. Access to financing is also important in that it enables the business to develop profitable product and service mix for specific niche markets. According to Wanjohi and Mugure (2008) argues that SME financing can be classified in two types: equity and debt financing. Equity in this case refers to owner's capital, while debt financing refers to bank loans, trade credits, leases among others.

According to Vera and Onji (2010), equity capital can be raised internally or externally. Internally, this can be through owner personal savings, or earnings, while external equity is from can be received from business partners, friends, family and relations. In most instances in SME ventures, equity funding is more preferable than debt financing. This is because young SMEs do undergo cash flow challenges making it difficult for them to secure loans with adequate collateral during the founding phase (Bonfim & Daniel, 2012). Similarly, Vera and Onji (2010) argue that equity financing offers SMEs long term financing with very minimum cash outflows unlike the debt financing option. Several scholars agree that equity financing can take different forms and shapes including personal financing, Venture Capital equity, Joint venture equity, and from relatives, family and friends (Kira & Zhongzhi, 2012; Asah, 2011; Kiraithe, 2015)

II.3.1.6 *Personal Financing*

Personal financing is defined as the situation in which the owner of a business venture contributes funds from his or her own savings to fund business activities (Asah, 2011). The importance of personal funding is that it helps SME start-ups mobilize additional resources since owners tend to have more confidence in the business and can invest without expecting an immediate return. In most cases, start-up SMEs are financed by owners since they don't want external interference in the business model they have adopted for the SME (Kiraithe, 2015). A study done by Schäfer, Werwatz, and Zimmerman (2014) among young entrepreneurs in Germany found that risky ventures were hardly financed by debt, but rather personal financing. They further noted that the over-reliance on personal financing by these young entrepreneurs was not out of choice, but rather, most financial institutions were not willing to fund risky ventures, and more so, run by youth.

According to OECD (2012) the challenge inherent in personal financing for most SMEs is lack of adequate personal savings that can effectively finance SME foundational operations. This is particularly the case in South America, and Sub-Saharan Africa where majority of individuals seeking to venture into business are necessity entrepreneurs seeking to escape the trap of unemployment. To this Wangui et al., (2014) and Charbonneau and Menon (2013) this kind of financing is not sustainable since young entrepreneurs in Sub-Saharan Africa do not have adequate savings to invest into business ventures. This notwithstanding, Fatoki and Asah (2011) posits that the best source of new SME financing is through entrepreneurs' own funds. The importance of this form of SME financing is that it is easy to access, easy to use, with no pay

back terms that will require transfer of equity. Similarly, Vera and Onji (2010) contend that personal financing of SMEs is good for start-ups that later needs additional capital since it demonstrates to potential investors that the owner (entrepreneur) is willing to risk his funds, and therefore creates a perception that he can take care of their investments when such a time comes.

II.3.1.7 *Venture Capital Financing*

Venture capital financing a form of business financing where funds are raised from investors who trade in risk and returns for the business funds' investments (Potter & Porto, 2007; Odit & Gobardhun, 2011). Venture capitalists are the people who provide the financing that entrepreneurs need to effectively run their business. The importance of venture capital financing is that the venture capitals not only invest their money, but also their skills in monitoring and providing advisory services to the business venture (Fatoki & Asah, 2011; Kira & Zhongzhi, 2012). Equally, the importance of having venture capital financing is that by performing monitoring of business start-ups venture capitalist can help the SMEs participate in strategic planning and decision making for the SME (Atherton, 2012).

Venture capitalist does usually include individuals, corporate organizations, and small business investment corporations (Odit and Gobardhun, 2011). The interesting characteristics of venture capitalist is that they invest in SMEs that have asymmetrical information and high intangible assets making their investments high risk, however, with high returns. Therefore, one could argue that the main incentive that draws venture capitalists to SME ventures and investments is the anticipated returns. It is possible to make super normal profits on their equity since they usually hold a stake in addition to the profit sharing (Asah, 2011). According to Daskalakis et al., (2013) SMEs should highly consider using venture capitalist as a way of financing since venture capitalist usually have connections to a network of suppliers and markets that SMEs can sell their products, as well as linkages to long term strategic partners.

II.3.2 Debt Financing

Debt financing is defined as the use of external funds to finance an organizational business activity (Smolarski & Kut, 2011). This means that accessing external funds by SMEs is regarded as debt financing. According to Akim (2011) traditional forms of debt financing for SMEs include bank loans, credit lines, and bank overdrafts. Newer forms of debt financing include asset-based financing, factoring, and trade credit. This study will look at bank loans, asset-based financing, and trade credit as types of debt financing accessible to SMEs.

II.3.2.1 *Bank Loans*

Bank loans are important for SMEs seeking to raise start-up or additional business capital. Bonfim and Daniel (2012) posits that business entrepreneurs that have adequate forms of collateral find it easy to access bank loans compared to entrepreneurs who do not have collateral. As such, Tardieu, (2007) points out that lack of adequate collateral has made it difficult for most SMEs to access bank loans. Disadvantaged groups such as women and youth in Sub-Saharan Africa find it even more difficult to access bank loans (Kiraithe, 2015). The patriarchal society of Sub-Saharan Africa has over the years made it difficult for women and youth to own property, or inherit property, thus, making it difficult for this groups to raise adequate collateral for bank loans (Birundu, 2015)

According to Badulescu (2011), access to credit by SMEs is usually affected by credit rationing behaviour by banks. Lack of adequate collateral and information concerning entrepreneurs credit worthiness do constitute major reasons bank loan declines. Most SMEs, particularly in the start-up stage lack the necessary relationship connections with banks, therefore decreasing the banks willingness to advance credit (Bonfim and Daniel, 2012).

Daskalakis et al., (2013) argues that unlike large corporations that have access to broader choice of selecting financial sources compared to SMEs, tend to gravitate towards commercial banks for short term debt financing that can be reviewed and renewed for long term debt. Abdesamed and Wahab (2014) notes that information asymmetry is acute in SMEs compared to large firm, and thus, the lending relationship between banks and the SMEs are important. SMEs tend to be managed by owners and as a result, the agency cost and agency problems can stand in the way of formulating asymmetrical information exchange between owner and the banks due to different of owners and managers (Tardieu, 2007; De Young et al., 2004). As a result of this argument, it is possible to conclude that agency problem can have adverse impact on accessibility to bank loans by SMEs. SMEs can improve access to these loans through collateral and enhanced relations with the banks.

However, as noted earlier by Kiraithe (2015) and Badulescu (2011), collateral has been one of the major stumbling blocks for SMEs seeking financing in their formative stages. Therefore, it can be 12
counterproductive for banks to keep insisting on collateral on SME start-ups that are not able to raise the collateral. Different approaches can be use by banks to enhance access to bank loan. However, if status quo remains, with all factors constant, SMEs will continue to have difficulties in accessing bank loans for the foreseeable future (Berg et al., 2015; Wangui et al., 2014).

II.3.2.2 ***Asset-Based Financing.***

Asset-based financing is defined as a form of obtaining financing based on the value of an asset one holds, rather than on its own credit standing (OECD, 2012). In this regard, the working capital and term loans are secured by account receivables, inventory, and equipment etcetera (Aabii, 2014). One of the major advantages of asset-based financing by SMEs is that firms can easily access funds under flexible terms than they could have obtained under commercial bank loans. Asset based financing does not consider the nature of future cash flows from the business as banks would. Equally, asset -based financing SMEs that lack credit history can still secure funding through the asset itself, and thus may not be exposed to rigorous credit rating or worthiness compared to traditional bank loans (Alfo& Trovato, 2006; Charbonneau & Menon, 2013) .

According to Aabii (2014) the edge asset-based financing gives SMEs is that the do not generally require personal guarantee from entrepreneurs, nor do they require the entrepreneurs to give up equity. The only challenge associated with asset-based financing for SMEs lies within the determination of the asset value. Asset appraisal may have to be conducted before the value is ascertained and funds advanced against it, which might take time (Ayyagari, Demirgüç-Kunt, & Maksimovic, 2010). Similarly, upfront legal costs may reduce involved in securing asset-based financing may eat into the SMEs profitability. Thus, SMEs have to tread a thin line between using asset-based financing in a way that enhances their firms leverage and profitability compared to alternative traditional bank loans. If they find this not to be the case, then asset-

based financing can still be costly and out of reach for most SME start-ups (Bonfim & Daniel, 2012).

II.3.2.3 *Bank Finance for SMEs*

A large body of the existing literature has documented that banks are the main external capital provider for SMEs sector in both developed and developing countries (Vera & Onji, 2010; Ono &Uesugi, 2009; Zhou, 2009; Wu et al., 2008; Carey & Flynn, 2005; Cole &Wolken 1995). De Bettignies and Brander (2007) assume that bank loans are available for SMEs on competitive and fair basis.

In order to optimize their capital structure, Moro, Lucas, Grimm, & Grassi (2010) suggested that SMEs should only focus on bank financing. Keasey and McGuinness (1990) argued that in spite of the fact that bank financing is more expensive in comparison to other sources of finance, it generates a higher rate of return for SMEs. They further conclude that bank finance can help SMEs accomplish better performance levels than other financing sources can do. The explanation given by them is that SMEs employ the funds more efficiently when they are monitored by, and answerable to banks.

From the perspective of banks, SMEs segment represents a strategic profitable part of bank business. In this regard, de la Torre, Martinez and Schmukler (2009) described the engagement between SMEs and banks as integral. They explained that banks do not only provide the necessary capital for entrepreneurs to establish new SMEs or expand the existing ones they also offer a variety of services and financial products. The findings of Beck, Demirgüç-Kunt and Martinez (2008) have highlighted a number of factors perceived by banks as drivers to finance SMEs. The most important factor is the great potential of profitability associated with the involvement with SMEs as banks perceive this sector as unsaturated with good prospects. Another factor is the possibility to seek SMEs clients through their relations with their large clients. Banks involvement with SMEs is also driven by the intense competition in other sectors such as the large business and retail customers.

The empirical literature on bank financing to SMEs emphasises some mechanisms, techniques and models developed and adopted by banks to lend to SMEs such as relationship lending (e.g., Petersen & Rajan, 1994), factoring (e.g., Soufani, 2002) and scoring (e.g., Frame, Srinivasan, &Woosley,2001) just to mention some.

Relationship lending is a powerful mechanism used to reduce problems related to opaqueness in firms especially SMEs. Under relationship lending, “soft” information is gathered by a financial institution (usually small local bank) through continuous contact with the firm (usually SME) in the provision of financial services (Berger &Udell, 1998, p. 645). The information will be then used to evaluate the creditworthiness of the entrepreneur as a part of the loan process to ensure that the potential loan will be repaid. The strength of the relationship lending, measured by its duration or the breadth of the relationship, was found positively correlated to the availability of funds for SMEs (Petersen & Rajan, 1994). In addition to this, the literature reports other benefits including; lower cost of credit, protection against credit crunches and the provision of implicit interest rate or credit risk insurance (Berger &Udell, 1998). Other study suggested that in order to increase credit supply for SMEs trust-based relationship lending is more effective than the

establishment of longer or more concentrated bank-borrower relationship (Hernández-Cánovas& Martínez-Solano, 2010).

Based mainly on "hard" quantitative information, credit scoring is a lending technology used by financial institutions especially banks to evaluate informationally opaque loans applicants. Unlike the information in relationship lending which need long time to be acquired, the hard data required by credit scoring technology are readily gathered usually from consumer credit bureaus and commercial credit bureaus. It has been evidenced in the literature that credit scoring method increases the credit availability for SMEs. Berger, Frame and Miller (2002) concluded that implementing credit scoring leads to an increase in the supply of credit to SMEs. Additionally, Frame et al. (2001) found that for the banks included in their sample the portfolio share of SMEs increased by 8.4% as a result of adopting credit scoring technology. Moreover, according to Berger and Frame (2007) this increase can be split into; (1) increasing the quantity of credit extended; (2) increasing lending to relatively opaque, risky borrowers; (3) increasing lending within low-income areas; (4) lending over greater distances; and (5) increasing loan maturity.

Another transactions technology employing hard information to lend to opaque SMEs is factoring. Factoring is a method to raise short-term finance whereby clients' account receivables are purchased by a specialized firm or a bank for a pre-agreed fee plus interest (Soufani, 2002). Consequently, the specialized firm or the bank takes the responsibility to control and manage a debtor portfolio of a firm. In simple words, factoring is the process resulting in exchanging the account receivable of a firm for cash. As SMEs usually lack the sufficient collateral to obtain finance, as such, using accounts receivable as collateral, that is factoring, to raise finance is significantly important decision to increase SMEs' liquidity (Soufani, 2002). It was found that factoring as an alternative source of finance can play a crucial role in alleviating financing gaps faced by SMEs (Soufani)

II.4 Enhancing International Trade Through Bank Financing: Insights from Uganda.

Understanding how banking institutions affect countries' and firms' internationalization is central to international business. Banks represent an important category of the global transaction services organizations, which embody important aspects of the institutional environment and are important contributors to the growth of international business. Banks play a critical role in international trade by providing trade finance products that reduce the risk of exporting. They facilitate payments and security of transactions.

No country can exist in isolation, international cooperation and trade antecedent of economic power and growth as well as industrialization. The unequal distributions of resources and globalization have results to interdependency among nations. Because of this, both the developed and developing nations engage in international trade.

However, International trade may result in resources and environmentally detrimental balances and trade shifts. This type of trade may allow one country to partially decouple its domestic economic and ecological systems while consuming goods from other national economic systems. Sometimes, the ideology behind cross nations trade varies. Countries may seek to save their own environmental and resources capacity by shifting away from natural resources and pollutant-intensive activities in the manufacture of their goods. They can do this through importing high

environmentally and resource burdensome products from other regions of the world.(Berger A. N.)

II.4.1 Banks Participation in International Trade.

Local banks support international trade through a wide range of products that help their customers manage their international payments and associated risks, and provide needed working capital. The term “trade finance” is generally reserved for bank products that are specifically linked to underlying international trade transactions (exports or imports). One of the most common and standardized forms of bank-intermediated trade finance is a letter of credit, it reduces payment risk by providing a framework under which a bank makes (or guarantees).

Banks play an important role in an economy of a nation, consequently, they con-tribute to investments, employment creation and the process of economic growth and development. They are the corner stone of an economy of a given nation. Global trading allows the different countries to participate in global economy encouraging the foreign direct investors**.**

In accrediting banks in Uganda for international recognition, the Bank of Uganda plays a major role. For credit lines, this implies that they look at the total amount of credit that is available, and not at the portion that is taken up by the borrower.

II.4.2 Common Trade Finance Instrument by Banks

When an exporter and an importer trade, they have to decide how to settle the transaction under one option, the exporter produces the good and the importer pays upon receipt (open account). Importer and exporter have to decide how to settle the trans-action. The most common trade finance instruments provided by banks are open account, letters of credit, documentary collections, advance payment, export letter of credit, export documentary collection, consignment and guarantee

II.4.2.1 *Documentary collection.*

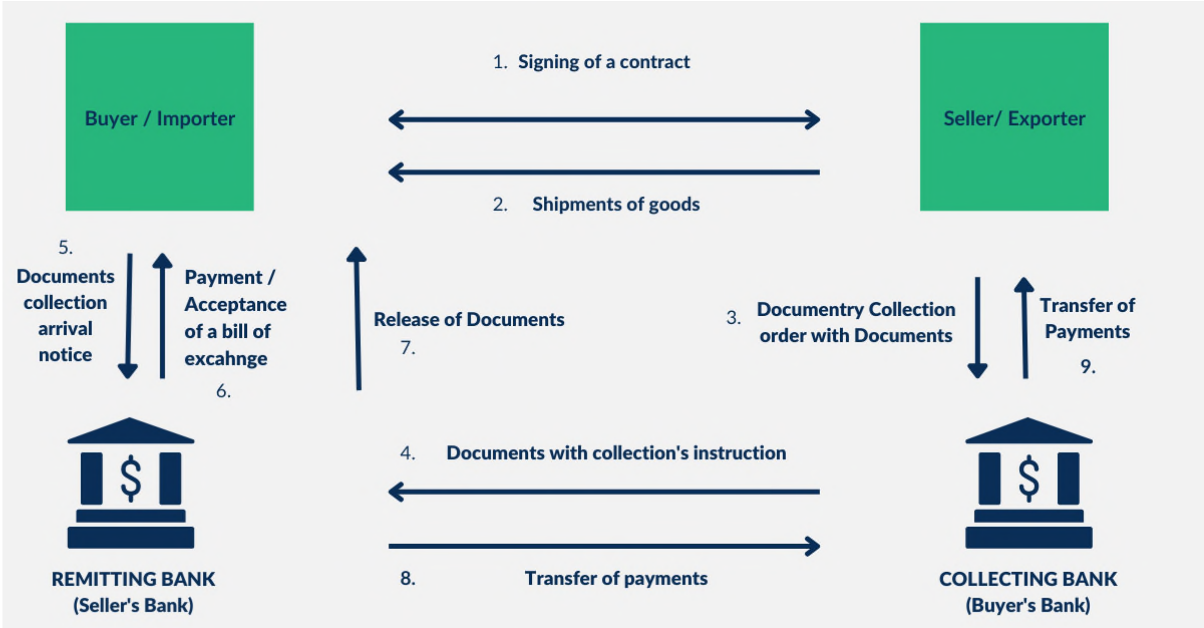
The Uniform Rules for Collection (URC) defines documentary collection as “the handling of documents (financial and or commercial) by banks in accordance with instructions received, in order to: Obtain payment and/or acceptance, or Deliver documents against payment and/or against acceptance, or Deliver documents on other terms and conditions” Therefore: Banks are only agents (of Exporter) in collections, they are bound to follow the instruction of whoever their principal is.

A process governed by international rules by which the supplier is able to collect from an overseas buyer through an intermediary –i.e. banks. It comprises between open account and advance payment and simpler but less secure than letter of credit (URT training manual). The two types of collections are clean collection and Documentary collection (Niepmann, 2015) Clean collection – contain financial documents only It is an alternate of open account where seller ships, sends commercial documents to buyer but sends financial documents I.e. draft through the banks for collection The payment is effected without reservation and conditions by

the principal or his bank. Some element of trust exists between buyer and seller (URT training manual).

Documentary Collection - contain financial and commercial documents Seller ships and then sends all documents (both financial and commercial) through the banks for handling Seller still retains a constructive control over goods through the banks (URT training manual).

Figure II:2 Depiction of the documentary collection process



Source:International Trade and Finance" by Paul R. Krugman

II.4.2.2 *Letter of credit (LC)*

Letter of credit is an undertaking given by a bank to the seller at the request and/or instructions of the buyer to make payment or accept and pay bills of exchange (Draft) drawn by the seller up to a stated sum of money within a prescribed time limit and against stipulated documents, provided that the terms and conditions of the credit are complied with. When a trade is settled with an LC, banks do not only hand over documents to the importer as in a DC but they may also advance the importer's payment. The exporter is paid as soon as it proves that it has delivered the goods. Because banks may incur a loss if the importer does not pay, they screen importers much more actively when they issue an LC than when they engage in a DC. Accordingly, we assume that the share of importers that try to get away without paying decreases by more with an LC than with a DC. At the same time, the fixed fee that the bank charges for an LC to cover screening, monitoring and document handling costs is higher than for a DC.

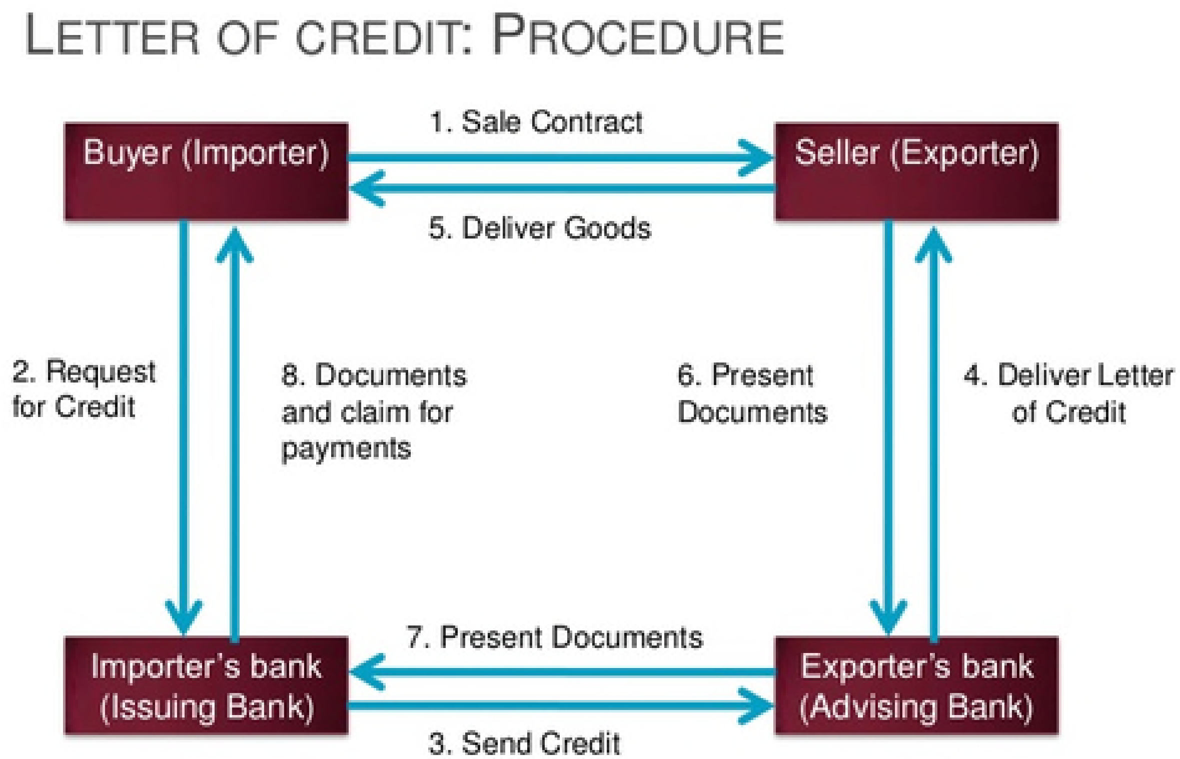
The market for letters of credit is highly concentrated, with a few local banks dominating the issuance of letters of credit in each country. The confirmation of letters of credit is usually done between banks that have long-standing relationships, both in the issuing of letters of credit and

other financial transactions. A number of papers focus on the bank credit channel, while controlling for the international trade finance channel.

Although the main objective of a Letter Credit is to reduce financial risk, it comes with a price and so tends not to be used in either the least risky or riskiest situations. This finding can be explained by the optimal contract choice of firms. The basic intuition is that the value of risk mitigation through bank intermediation is offset to a degree by the cost of the intermediation.

A Letter of Credit is therefore a contractual commitment by the foreign buyer's bank to pay once the exporter ships the goods and presents the required documentation to the exporter's bank as proof.

Figure II:3 Process of a Letter of Credit (L/C)



Source:International Trade Finance: A Practical Guide" by Kwai Wing Luk.

II.4.2.3 ***Export letter of credit.***

("Documentary Letter of Credit") shall mean an undertaking given by a bank to the seller at the request and/or instructions of the buyer to make payment or accept and pay bills of exchange (Draft) drawn by the seller up to a stated sum of money within a prescribed time limit and against stipulated documents, provided that the terms and conditions of the credit are complied with. (Commercial bank of Ethiopia Trade Service Process Procedure, 2012)

Consignment Payment It's a method of payment in which the title to the goods remains with the seller until an agent (distributor) in foreign country sells them. Payment is made to the seller if and when the agent (distributor) sells the goods. (Commercial bank of Ethiopia Trade Service Process Procedure, 2012)

Letter of Guarantee It is issued by a bank is a written promise/ irrevocable obligation by the bank to compensate (pay a sum of money) to the beneficiary (local or foreign) in the event that the obligor fails to honour his/her/its obligations in accordance with the terms and conditions.

II.4.3 The Critical Role of Banks in Mitigating Risks in International Trade

Banks play a crucial role in international trade by providing trade finance products that significantly reduce the risks for both exporters and importers. International trade often operates on an open account basis, where goods are shipped before payment is made. This arrangement exposes exporters to the risk of non-payment and importers to the risk of non-receipt of goods after payment. By offering various financial instruments, banks help to mitigate these risks, ensuring smoother and more secure transactions.

One of the most common and effective tools that banks use to mitigate risks in international trade is the Letter of Credit (LC). An LC is a commitment by a bank on behalf of the importer that payment will be made to the exporter, provided the terms and conditions specified in the LC are met. The process involves several steps. First, the importer applies for an LC from their bank. The bank evaluates the importer's creditworthiness, the risk involved in the transaction, and the political risk of the exporting country. Upon approval, the bank issues an LC in favor of the exporter. In some cases, the exporter may require the LC to be confirmed by a bank in their own country. This adds an extra layer of security, ensuring that a local bank guarantees payment even if the importer's bank defaults. After the LC is confirmed, the exporter ships the goods and submits the necessary documents (such as the bill of lading, invoice, and packing list) to their bank, which forwards them to the importer's bank. The LC specifies the documents required and the terms to be met. Once the importer's bank verifies that all conditions of the LC have been fulfilled, it releases the payment to the exporter's bank, ensuring that the exporter receives the payment as agreed. The use of an LC shifts the risk from the importer to the bank. If the importer defaults, the bank assumes the liability, providing assurance to the exporter that they will receive payment. However, if the risk is deemed too high, the bank may refuse to issue an LC.

Another risk mitigation tool is the Advanced Payment Guarantee (APG). This is used when the importer is required to make an advance payment before the goods are shipped. The process involves the importer applying for an APG from their bank. The bank assesses the risk level and the importer's creditworthiness. Upon approval, the bank issues a guarantee to the importer, who then makes the advance payment to the exporter. The bank guarantees that if the exporter fails to ship the goods as agreed, the importer can claim the payment back from the bank. This shifts the risk from the importer to the bank. APGs provide security to the importer, ensuring that their advance payment is protected. This is particularly useful in high-risk transactions where the importer is uncertain about the reliability of the exporter.

In addition to LCs and APGs, banks offer Documentary Collections (DC) as a risk mitigation tool. In a DC, the exporter ships the goods and submits the shipping documents to their bank, which forwards them to the importer's bank. The importer's bank releases the documents to the

importer against payment or acceptance of a bill of exchange. This method, though less secure than an LC, still provides a level of assurance to both parties.

Beyond providing financial instruments, banks also play a critical role in advising their clients on risk assessment and management. They offer services such as country risk analysis, evaluating the political and economic stability of the exporting or importing country, credit risk assessment, analysing the creditworthiness of the trading partner, and market intelligence, providing insights into market conditions and trends. These advisory services help businesses make informed decisions and manage risks more effectively.

In summary, banks are indispensable in facilitating international trade by providing financial instruments and advisory services that mitigate risks for both exporters and importers. Tools such as Letters of Credit, Advanced Payment Guarantees, and Documentary Collections ensure that payments and shipments are secure, fostering trust and confidence in international trade transactions. Through these mechanisms, banks help businesses navigate the complexities of global trade, contributing to the growth and stability of the international trading system.

II.4.4 Trade as a Catalyst for SME Development in Uganda"

Trade, particularly the export of agricultural produce, plays a crucial role in enhancing the standard of living in Uganda. For many small-holder farmers and SMEs, cash crops are the principal means of earning income to purchase goods and services that they cannot produce themselves. This income is essential for covering basic needs such as school fees and medical bills, thus improving their overall welfare. The increase in cash income from export crops can have a multiplier effect on the economy, boosting aggregate demand and supply, and leading to a higher standard of living.

The majority of small-holder farmers grow cash crops to supplement their household food supplies. Despite this, their overall food production throughout the year may not differ significantly from that of farmers who do not grow cash crops. However, their food security is often more precarious due to their dependence on a few cash crops. In the event of crop failure or depressed prices, these farmers are particularly vulnerable, highlighting the risks associated with reliance on cash crops. This situation underscores the importance of diversifying agricultural production and improving market access for small-holder farmers and SMEs.

Uganda's foreign trade pattern reveals a significant reliance on the export of agricultural produce. The country's main agricultural exports include coffee, tea, cotton, tobacco, cut flowers, hides and skins, beans, maize, and fish and fish products. These commodities have been the mainstay of the export sector for a long time, earning substantial foreign exchange and contributing to the national economy. Coffee, in particular, remains a dominant export product, providing livelihoods for millions of Ugandans.

Exporting agricultural produce not only brings in foreign exchange but also creates a market for local farmers and SMEs, enabling them to sell their products at competitive prices. This increased market access can lead to higher incomes and improved living standards for farming communities and small enterprises. The income earned from exports helps farmers and SMEs invest in better farming techniques, purchase inputs like seeds and fertilizers, and improve their productivity. Additionally, the export sector generates employment opportunities, both directly and indirectly, in farming, processing, and logistics.

The positive impact of trade on SME development in Uganda is evident. SMEs, particularly those in the agricultural sector, benefit from the increased demand for their products in international markets. By tapping into global markets, these enterprises can expand their customer base, increase sales, and achieve economies of scale. Exporting also encourages SMEs to adopt international standards and improve the quality of their products, making them more competitive globally.

However, the journey of SMEs to participate in international trade is fraught with challenges. Limited access to finance, inadequate infrastructure, and stringent regulatory requirements often hinders their ability to compete effectively in global markets. To address these challenges, the government and development partners have implemented various initiatives aimed at supporting SMEs. These initiatives include providing financial assistance, improving infrastructure, and simplifying regulatory processes to create a more conducive environment for trade.

The Ugandan government has also established export promotion agencies to assist SMEs in navigating the complexities of international trade. These agencies provide valuable information on market trends, export procedures, and potential trade opportunities. They also organize trade missions and exhibitions, enabling SMEs to showcase their products to international buyers and establish business connections.

Furthermore, the development of trade finance products by banks plays a crucial role in supporting SMEs engaged in international trade. Financial instruments such as letters of credit, export credit insurance, and factoring services help mitigate the risks associated with exporting. These products provide SMEs with the necessary financial security to undertake export transactions confidently.

In addition to financial support, capacity-building programs are essential for enhancing the competitiveness of SMEs in international markets. Training and mentorship programs help SME owners and managers acquire the skills and knowledge needed to succeed in global trade. These programs cover various aspects of export management, including market research, quality standards, packaging, and logistics.

Digital technology also presents significant opportunities for SMEs in Uganda to participate in international trade. E-commerce platforms enable SMEs to reach a wider audience and sell their products online. By leveraging digital tools, SMEs can streamline their operations, reduce costs, and improve their market reach. The adoption of digital technology also facilitates better communication and collaboration with international buyers, enhancing the overall efficiency of trade transactions.

The role of trade in SME development extends beyond the agricultural sector. SMEs in other industries, such as manufacturing and services, also benefit from increased trade opportunities. For instance, the export of manufactured goods such as textiles, leather products, and handicrafts provides additional revenue streams for SMEs. The services sector, including tourism and information technology, also has significant export potential, contributing to the diversification of Uganda's export base.

The impact of trade on SME development is multifaceted. On one hand, it provides economic opportunities and improves living standards for those involved in export activities. On the other

hand, it poses challenges that require concerted efforts from the government, financial institutions, and development partners to address. Ensuring that the benefits of trade are inclusive and reach the most vulnerable segments of society is crucial for sustainable development.

In conclusion, trade is a vital catalyst for SME development in Uganda. The export of agricultural produce and other goods and services significantly contributes to the national economy, improves living standards, and creates employment opportunities. By addressing the challenges faced by SMEs and leveraging the opportunities presented by international trade, Uganda can enhance the competitiveness of its SMEs, foster economic growth, and achieve sustainable development. Through continued support and strategic initiatives, the country can ensure that trade remains a powerful engine for SME development and poverty reduction.

II.5 Conclusion

Private banks in Uganda play a pivotal role in financing SMEs, which are essential for the country's economic growth and employment. Through a variety of financial products and services, including short-term credits, long-term investment loans, and innovative trade finance instruments like Letters of Credit and Advanced Payment Guarantees, private banks provide the necessary resources for SMEs to grow and thrive. Additionally, these banks offer advisory services and capacity-building programs that equip SME owners and managers with the knowledge and skills needed to succeed in both domestic and international markets. The adoption of digital technology further enhances the participation of SMEs in global trade by reducing transaction costs and improving operational efficiency.

Despite the significant contributions of private banks, challenges such as limited access to finance, inadequate infrastructure, and stringent regulatory requirements persist. Addressing these issues requires concerted efforts from the government, financial institutions, and development partners. By creating a more conducive environment for trade, improving infrastructure, and simplifying regulatory processes, Uganda can enhance the growth and sustainability of its SMEs. In summary, private banks are indispensable in supporting the financing needs of SMEs and facilitating their participation in international trade. By leveraging the financial products and services offered by private banks, SMEs in Uganda can overcome challenges, access global markets, and contribute significantly to the country's economic development. Through continued support and strategic initiatives, private banks can ensure that SMEs remain a powerful engine for economic growth, job creation, and poverty reduction in Uganda.

CHAPTER THREE: METHODOLOGY AND RESEARCH ANALYSIS.

III.1 **Introduction.**

This final chapter synthesizes the comprehensive findings and insights from my investigation into the challenges that Small and Medium Enterprises (SMEs) in Uganda encounter when attempting to secure financing from private banks. Despite their crucial role in driving economic growth and creating jobs, SMEs often face significant obstacles that limit their access to essential financial resources. This study probes these barriers within the financial systems, aiming to uncover underlying causes and broader impacts.

The guiding research question focuses on identifying the principal challenges that hinder SMEs' ability to access bank financing, particularly from private sector banks. Through a detailed examination of methodologies, analysis of collected data, and integration with relevant financial theories, this chapter seeks to provide a nuanced understanding of how various factors in the financial landscape influence lending decisions and outcomes.

The conclusions and recommendations section is designed to illuminate the systemic barriers discovered during the research and propose practical strategies for overcoming these challenges. The recommendations are crafted to improve the accessibility and effectiveness of bank financing for SMEs, fostering a supportive financial environment conducive to their growth and sustainability. The findings from this study highlight the need for targeted financial reforms and strategic adaptations within the banking sector to better support the bedrock of Uganda's economy—its small and medium enterprises.

III.2 **METHODOLOGY**

III.2.1 Introduction

This chapter explains the approach that was followed in data collection in order to achieve the set objectives. The chapter focused on the research design that was used, the study population, sample size and selection, the sampling techniques, the procedure of data collection and data collection methods, validity and reliability concerns, data analysis methods, measurement of the study variables as well as ethical consideration and limitations of the study.

III.2.2 Research Design

In order to give the answer to my question "What are the key challenges faced by Small and Medium Enterprises (SMEs) in Uganda regarding access to bank financing, specifically within the domain of private banks?", I adopted a cross-sectional survey design using both quantitative and qualitative data collection techniques. A cross-sectional study is a type of observational study that analyses data from a population, or a representative subset, at a specific point in time. It's a type of research design in which you collect data from many different individuals at a

single point in time. This design was deemed appropriate for obtaining data to create population characteristics and finding correlations between variables (Sileyew, 2019). The benefit of a cross-sectional study design is that it allows researchers to compare many different variables at the same time (Creswell, 2013). This design choice was considered appropriate for investigating the factors that influence SMEs' access to finance in Uganda.

III.2.3 Target Population

A target population refers to a given researcher's study area that has a shared and noticeable trait (Garg, 2016). Before selecting a study population, a researcher must ensure that the study problem affects the given population directly or indirectly (Garg, 2016). Out of Uganda's 1.1 million small and medium sized enterprises, the study focused on at least five from each of the five regions in Uganda (East, West, South, Central and the Northern part of Uganda), but mainly focus on those from the capital (Kampala), those SMES with county business permits from the county governments.

III.2.4 Sampling Technique

Sampling is the process through which a researcher can pick a representative sample from an entire population used in a study Creswell (2013). Probabilistic sampling technique was employed in selecting a sample from the SMES. Probabilistic sampling technique helped in eliminating any form of biases Creswell (2013). The method used in choosing the participants was stratified random sampling selected from the registered SMEs in the county governments.

A sample is a subset or section of the population that is being studied. The goal of sampling is to get insights and understanding about certain qualities or attributes of the total population (Zikmund, 2010).

III.2.5 Instrumentation

According to Jenn (2010), a questionnaire is considered one of the most convenient methods for efficiently collecting information from numerous participants within a limited timeframe. Therefore, careful design of the questionnaire is crucial to ensure the collection of accurate data. The goal is to create a questionnaire that produces interpretable and generalizable results, allowing for meaningful analysis and drawing valid conclusions from the data gathered. A poorly designed questionnaire can lead to the gathering of erroneous data that can provide wrong findings. The study used close-ended questions, which was based on a five-point Likert scale ranging from 1 (Strongly Agree) to 5(Strongly Disagree).

Designing the questionnaire was based on the conceptual framework. The framework offers all the variables and sub-variables to be studied (Jenn, 2010). This questionnaire employed both open and close-ended questions. Open questions ensured that they allowed a respondent to provide in-depth feedback on a given question as they are not restricted to any options. However, for the close-ended questions, they were used to provide answers to the already known questions

III.2.5.1 *Ethical Considerations*

Privacy and Confidentiality

Privacy and confidentiality refer to the protection of a participant's identity. This meant that as a researcher, one should treat any information given by a participant as secret as possible and not divulge it to others without their permission. The research ensured that it did not share personal information such as names, phone numbers, email addresses, or Sacco membership identification numbers. All personal information was coded. Random letters and numbers were assigned to each participant's information, appearing in the published document.

III.2.5.2 ***Data Collection Procedures***

The study included both primary and secondary data. Presumptions, facts, or other information gathered by a researcher directly from the field are referred to as primary data.

The questionnaire served as the main tool for collecting data for the study since it was a simple and affordable way to do so (Regmi et al., 2017). The questionnaire was accompanied with a letter of introduction outlining the objectives of the study, a link was therefore forwarded to each of the respondents. Each participant had two weeks to make sure they submitted the completed questionnaire.

Operational Definition of Variables

Table III.1: Operational Definition of Variables

Objective	Variables	Indicator	Measurement Scale	Methods of data Analysis
To investigate the effect of interest rates in SMEs access to finance in Uganda	Interest rates (Independent)	-BOU interest rate caps -Financial Institutions interest rates	Ordinal	Descriptive
To access the effect of SMEs credit profile on SMEs access to Uganda.	Credit profile (Independent)	-CRB rating -Credit Performance	Ordinal	Descriptive
To examine the effect of SMEs financial performance on SMEs access to finance in Uganda.	SME's financial performance (independent)	-Return on assets -Return on equity	Ordinal	Descriptive
To determine the effect of collateral requirements on SMEs access to finance in Uganda.	Collateral requirements (Independent)	-Value/ Percentage of collateral -Level of collateral ownership	Ordinal	Descriptive

Source: Constructed by me, the author, to guide me during the survey

III.2.5.3 ***Data Analysis***

In this study, we employed a descriptive analysis approach to elucidate the survey data. By categorizing responses and noting trends across various questions, we were able to construct a comprehensive picture of the challenges faced by SMEs in accessing financing from private banks in Uganda. Additionally, comparative analysis was utilized to highlight differences and similarities across different types of SMEs, providing a nuanced understanding of the factors that influence access to finance. This methodological approach allowed for an in-depth exploration of the data, enabling the identification of key themes and insights relevant to our research question.

III.3 RESULTS AND ANALYSIS

III.3.1 Introduction

The analysis of the study's conclusions based on the information obtained from the respondents is presented in this section. Descriptive as well as inferential analysis were performed. Different charts such as tables and graphs were all employed in the study to present the results.

III.3.2 Response Rate

The study sought to establish the response rate of the research and results are presented in Table III.2 below.

Table III.2: Response Rate

	Frequency	Percentage%
Successful	32	78%
Unsuccessful	9	22%
Total	41	100

Source: Elaborated by me from the data obtained

The study, which concentrated on small and medium sized businesses, was carried out in the different regions of Uganda. The respondents received a total of 41 questionnaires, and 32 of them were fully completed when they were returned. This translates to a satisfactory response rate for the research of 78%. Mugenda & Mugenda (2013) indicate that a response rate of sixty percent is deemed adequate, while a rate of seventy percent is deemed exceptional and suitable for analysis. Table 2.1 provides more information on the response rate.

III.3.3 Demographic Characteristics of Respondents.

In the study, respondents' gender, age, educational attainment, number of workers, years in business, and years of operation and the business ownership category they were involved with were analysed. This information was necessary to shed more light on the demographic constitution of respondents. To guarantee a balanced distribution of participants and provide equal representation of their opinions, efforts were made to ensure fairness in selecting respondents. This was done to ensure that every participant had an equal opportunity to be included and that their views were represented fairly.

III.3.3.1 *Gender.*

The gender distribution of the respondents is shown in Table III.3 below

Table III.3: Gender Distribution

Gender	Frequency	Percentage
Male	22	68.8
Female	10	31.2
Total	32	100

Source: Constructed by me using results from the Survey

According to the findings, there were 68.8% male participants and 31.2% female participants. This shows that the respondents' genders were properly distributed, showing that there was no obvious gender imbalance in the study. You can refer to Table 2.2 for a visual representation of this information.

III.3.3.2 ***Education Level.***

The education background of respondents is presented in table III.4 below.

Table III.4: Education Level

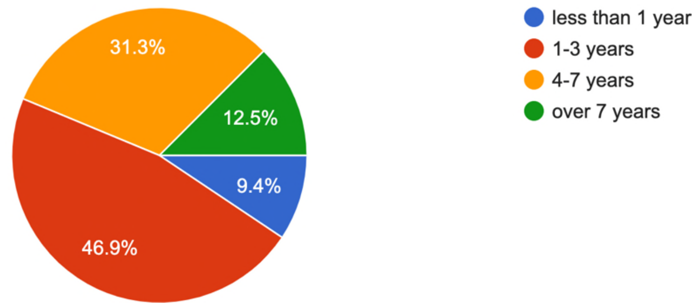
Years	Frequency	Percentage (%)
Post Graduate	2	6.25
Degree	18	56.25
Diploma	7	21.88
Certificate	5	15.62
Total	32	100

Source: Constructed by the author using results obtained from the survey

III.3.3.3 ***Years of Operation .***

The purpose of the study was to determine the number of years that the respondents to the study had been in business. The results are presented in Figure III.1 below

Figure III.1: Years of Operation.



Source: Prepared by me using the data obtained from the survey

Based on the findings, 9.4% of those who took part in the survey stated that they had been in business for less than one year. Additionally, 46.9% stated that they had been in business for one to three years, while 31.3% reported a business tenure of 4-7 years. Furthermore, 12.5% of the respondents said they have been in operation for at least seven years. These results highlight the varying durations of business experience among the participants. This indicated that the respondents had enough knowledge and experience in their business to respond in a satisfactory manner to the questions of the study.

III.3.3.4 ***Number of Employees***

The study sought to investigate the number of employees employed by each business. The findings of the study were presented in Table III.5 below.

Table III.5:Number of Employees.

Number of Employees	Frequency	Percentage (%)
Less than 5 Employees	17	53.1
6 – 50 Employees	12	37.5
51 – 100 Employees	0	0
101 and Above Employees	3	9.4
Total	32	100

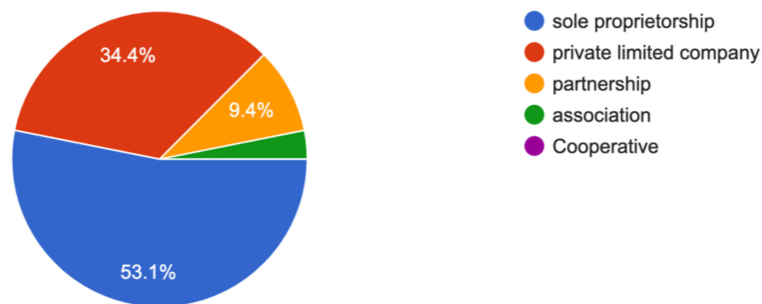
Source: Constructed by author using data obtained from the survey

Findings indicate that 53.1% of respondents had employed less than five staff, a further 37.5% had employed 6-50 workers, and none of the respondents had employed 51-100 employees. Only 9.4% of the respondents had employed above 101 workers in their businesses. This indicated that majority of the businesses had employed less than five employees which is an indicator that the size of their businesses was small.

III.3.3.5 ***Business Ownership.***

The researcher sought to find out the business ownership categories that the respondents of the study were involved in. Findings are presented in figure III.2 below.

Figure III.2: Business Ownership category



Source: Prepared by author using data obtained from the survey

The majority of the companies, representing 53.1%, are categorized as private limited companies, making this the most common form of ownership among the respondents. Sole proprietorships account for 34.4%, indicating a significant number of smaller or individual-owned businesses. Partnerships and associations are less common, with 9.4% and 3.1% respectively, and cooperatives are the least represented category at 0%. This distribution suggests a dominance of private limited structures and individual ownerships (solely proprietor businesses) in this survey sample, with less emphasis on cooperative and associative models.

III.3.4 Descriptive Statistics Analysis

For each of the study's four variables, descriptive statistics are provided in this section. Illustrative measurements and rates, were utilized to sum up and depict these factors. The scale utilized for the factors went from 1 to 5, with 1 specifying "strongly agreed" (SA), 2 indicating

"agreed" (A), 3 indicating "neutral" (N), 4 indicating "disagreed" (D), and 5 indicating "strongly disagreed" (SD).

III.3.4.1 ***Interest Rates***

The responses to the survey, which were asked to share their thoughts on the following statements about interest rates, are shown in table III.6 below.

Table III.6: Statistics for Interest Rates

Statements	SA%	A%	N%	D%	SD%
The majority of SME enterprises in Uganda pay significantly high interest rates to banking institutions.	62.5	31.25	0	3.125	3.125
Many SMEs are deterred from seeking banking institutions for lending facilities by the high-interest rates.	34.375	50	6.25	6.25	3.125
The prevailing lending rates offered by financial institutions have had a discouraging effect on many SME owners, leading them to hesitate in seeking both short-term and long-term loans for their businesses.	56.25	31.25	9.375	0	3.125
Financial institutions tend to exhibit bias when assessing SMEs for loans or credit, in contrast to large corporates.	21.875	40.625	28.125	6.25	3.125

Source: Constructed by the author using information obtained from the research.

The research examined whether banking firms in Uganda charged high interest rates for SME businesses. The findings indicated that 93.75% agreed that the interest rates were relatively high. A small percentage (6.25%) disagreed and none remained neutral out of the 32. This suggests that the interest rates charged by financial institutions were indeed high for SME businesses in Uganda.

Additionally, the study investigated whether these high interest rates discouraged SMEs from seeking credit facilities from banking companies. The findings showed that 84.375% of participants agreed that the high interest rates discouraged them from approaching financial institutions. A small percentage (6.25%) remained neutral, while the statement was contradicted by 9.375% of respondents. This indicates that the higher interest rates in banks had a discouraging effect on SMEs, making them to secure loans from lenders.

In relation to the impact of current lending rates on SMEs' willingness to seek loans, the research established that 87.5% of participants agreed that the higher lending rates had discouraged them from pursuing both short-term and long-term loans for their businesses Only a small percentage (3.125%) disagreed with this statement, and 9.375% remained neutral. This suggests that the higher lending rates indeed discouraged many SME owners from obtaining loans for their businesses.

Regarding bias in loan evaluation between SMEs and large corporates, 62.5% agreed that financial institutions exhibited bias when assessing SMEs for loans or credit, perceiving them to be riskier. A small percentage (28.125%) remained neutral on this statement, while 9.375% disagreed. This implies that there is a perceived bias in the evaluation process, where SMEs are considered riskier compared to large corporates.

These statements were in agreement with those of Maalim and Gikandi (2016) who conducted a study that focused on assessing the influence of interest rates on the accessibility of credit for small businesses in Garissa County and established that interest rates are an important determinant of the credit demand in financial institutions. The study was also in agreement with that of Chilembo (2021) who conducted a study to investigate the elements affecting SMEs ability to acquire financing in Zambia, and established that there was a link between interest rates and lack of collateral assets and increased risk of loan refusal.

III.3.4.2 ***Credit Profile.***

Respondents were asked to provide their feedback on various statements regarding their credit profile, and the results are presented in table III.7 below

Table III.7: Statistics for Credit Profile

Statements	SA%	A%	N%	D%	SD%
Poor credit rating has led to challenges in accessing finance from financial institutions.	40.625	50	9.375	0	0
Previous credit facilities limit access to current credit.	37.5	25	25	12.5	0
Borrowers not having a credit history are deemed to be risky.	56.25	15.625	12.5	15.625	0
Listing by mobile apps prevents SME’s from accessing credit from financial institutions	41.25	38.125	15	5.625	0
There is not enough credit available to invest in expanding new businesses.	25	37.5	31.25	6.25	0

Source: Constructed by author using data obtained from the survey

The study investigated whether poor credit rating had led to challenges to access funds from banks. The findings indicated that 90.625.0% of the participants agreed with the statement, while 9.375% remained neutral and 0% disagreed. This suggests that the poor credit rating of the respondents had indeed posed challenges in utilizing banks to obtain funding.

In addition, the study examined whether previous credit facilities limited access to current credit. The findings indicated that 62.5% agreed with the statement, while 25% remained neutral and 12.5% disagreed. This indicates that previous credit facilities indeed constrained access to current credit.

Furthermore, the study investigated whether borrowers without a credit history were considered risky. The results indicated that 71.87% agreed while 12.5% remained neutral and 0% disagreed. This suggests that financial institutions deemed borrowers without a credit history to be risky.

In terms of listing by mobile apps and its impact on SMEs' access to credit from banks, 79.375% agreed, while 15% remained neutral and 5.625% disagreed. This suggests that listing by mobile apps indeed hindered most SMEs from accessing credit from financial institutions.

Additionally, the study examined whether there was inadequate credit available for investing in new business expansion. The findings indicated that 62.5% agreed with the statement, while 31.25% remained neutral and 6.25% disagreed. This implies that many businesses faced a lack of sufficient funds and credit to invest in new ventures and expand their existing businesses.

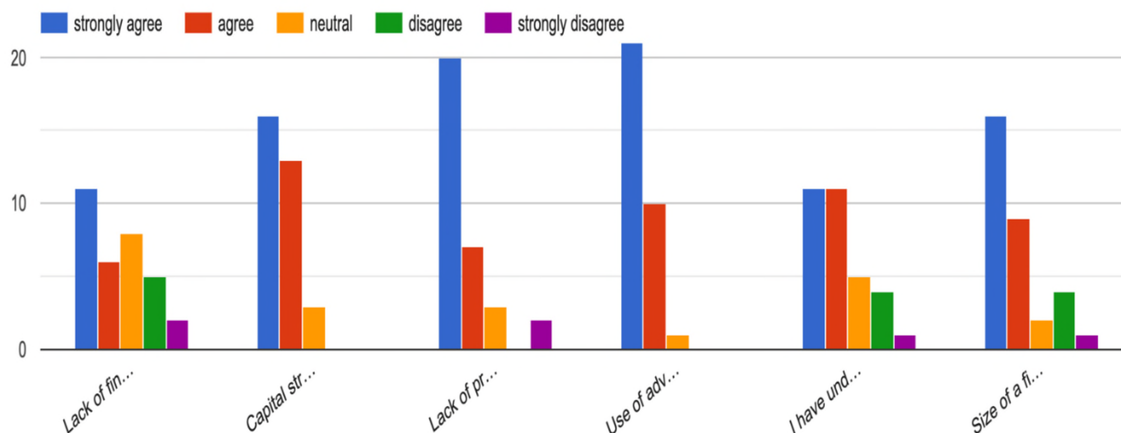
These findings were in agreement with those of Bigsten (2014) whose study on financial institutions revealed that most financial institutions reject loan applications from around 90% of SMEs due to reasons such as a lack of collateral security, poor financial performance, unfavourable credit profiles, and high interest rates on loans. Similarly, the findings agree with those of Mwangi's (2015) whose research revealed that approximately 95% of SME’s rely on loans obtained from friends and family as well as personal savings as their primary sources of funding since they have unfavourable credit profiles.

III.3.4.3 ***SME’s Performance.***

The respondents were asked to express their opinions on specific statements related to the performance of SMEs, and their views are presented in figure III.3

Figure III.3: Statistics for Financial Performance

Kindly tick appropriately whether you agree with the statements relating to the effect of performance on credit access from financial institutions, where (SA-strongly A-agree, N-Neutral, D-Disagree, SD-strongly disagree).



Source: Elaborated by me using data and results obtained from the survey

The study's goal was to determine how financial institutions' shortage of funding affects company performance. The results revealed that 53.125% agreed with the statement. In addition, 25% had no opinion, while 21.875% disputed the assertion. This implies that the performance of firms has actually been impacted by the absence of funding from financial institutions.

Additionally, the study investigated the connection between capital structure and organizational performance. According to the respondents' responses, the majority of them agreed with the statement, making up 90.625%. In contrast, none (0%) disagreed while 9.375% of respondents were indifferent. This shows that the majority of respondents thought the capital structure was important. This suggests that undergoing training on credit management was perceived to be beneficial in effectively managing the business.

In addition, the survey looked at whether the respondents had enough funds to operate their firms in light of the scarce sources of funding. The results showed that 68.75% of respondents, or a majority, agreed with the assertion. 15.625% disagreed and still another 15.625% of them were indifferent. This suggests that the restricted sources of finance had an impact on the capital that was available to run their firms.

The study also aimed to determine whether a firm's size affected its ability to get loans and, subsequently, its performance. The findings indicated that 78.125% of respondents, agreed with the statement. In addition, 15.625% disagreed while 6.25% of the respondent enterprises remained indifferent. This implies that the size of the firm had an impact on its access to credit and ultimately affected its performance.

These findings were in agreement with those of Fowowe (2017) who analysed data from 10,888 African enterprises and found that SME’s performance was a major determinant on access to finance. Firms with less credit constraints grow at a quicker rate than those without it. These

findings supported the concept that financing is critical to company growth and justify the many actions and activities being taken to increase the availability of funding for African firms.

Overall, the survey responses suggest that capital strength, lack of proper documentation, and the use of advanced analytics by financial institutions are perceived as the most significant factors influencing credit access. The lack of financial information and the size of the firm are also seen as important, though there's more variability in responses regarding the understanding of financial products. These insights can be crucial for financial institutions aiming to enhance their credit accessibility strategies.

III.3.4.4 *Collateral Requirements.*

Respondents were requested to indicate their views on the following statements in relation to collateral requirements and their views were presented in table III.8 below.

Table III.8: Statistics for Collateral Requirements

Statements	SA%	A%	N%	D%	SD%
The limited ability of SMEs to provide tangible assets as security hinders their access to credit facilities.	71.875	9.375	18.75	0	0
The absence of fixed assets poses a challenge for many SMEs in accessing credit.	56.25	25	15.625	0	3.125
Borrowing by SMEs is discouraged due to the costs associated with the collateralization process, such as legal fees, stamp duty, valuation, insurance, and others.	31.25	43.75	18.75	6.25	0
SMEs are discouraged from borrowing due to the lengthy process involved in registering and creating a charge on the security they pledge to financial institutions.	21.875	46.875	15.625	12.5	3.125
Potential borrowers are discouraged from borrowing due to the strict and demanding credit terms imposed by financial institutions.	62.5	12.5	18.75	3.125	3.125

Source: Prepared by me, the author using the data obtained from the survey

According to the findings in table III.8, SMEs' access to credit facilities is severely hampered by their inability to provide visible security. A large majority of the respondents, 81.25%, agreed with this statement, while 18.75% were neutral, and none of the respondents (0%) disagreed. This suggests that the lack of tangible security greatly affects SMEs' ability to obtain credit.

Furthermore, the study examined whether the absence of fixed assets poses a barrier to accessing credit for many SMEs. The findings indicated that 81.25% agreed, 15.625% were neutral, and 3.125% disagreed. This indicates that the lack of fixed assets is a significant obstacle for SMEs in obtaining credit from financial institutions.

The study further examined the impact of costs associated with the collateralization process on borrowing by SMEs. The findings indicated that 75.0%, agreed that these costs, including legal fees, stamp duty, valuation, insurance, etc., discouraged borrowing. Additionally, 18.75% were neutral, and 6.25% disagreed with the statement. This suggests that the high costs associated with collateralization pose a significant obstacle to accessing finance and discourage borrowing by SMEs.

Furthermore, the study investigated whether the duration taken to register and create a charge on the security pledged to a financial institution discouraged SMEs from borrowing. The findings indicated 68.75%, agreed that the lengthy registration process for the charge on pledged security discouraged borrowing. Additionally, 15.625% were neutral, and another 15.625% of them also disagreed. This implies that the time-consuming nature of the registration process acts as a deterrent for SMEs seeking loans from financial institutions.

Moreover, the study examined whether the stringent credit terms imposed by financial institutions discourage potential borrowers from seeking credit. The findings indicated that 75.0% agreed that these stringent credit terms discouraged borrowing by SMEs. Additionally, 18.75%% remained neutral, and 6.25% disagreed. This suggests that the strict conditions set by financial institutions discourage SMEs from seeking loans.

These findings were in agreement with those of Mumin (2018), who also sought to determine the factors that impact SME access to Kenyan commercial banks for finance and established that having collateral affects one's ability to get credit in any financial institution. The findings were also in agreement with those of Ndungu (2016) who conducted research to determine the variables that affect how easily SMEs in the county of Murang'a may receive loans. The study's findings indicated that loan interest rates, the quantity of collateral security, and literacy rates were the factors that had the most impact on whether or not SMEs in Murang'a have access to credit.

Overall, the survey responses highlight a strong consensus that collateral requirements significantly impact the ability to secure loans, especially affecting SMEs and those without property to offer as collateral. These insights suggest that collateral requirements can be a major barrier to financial access, particularly for smaller enterprises and those lacking substantial assets.

III.3.4.5 ***Access to Finance***

Respondents were asked to indicate their views on the following statements relating to access to finance and their views presented in table III.9 below.

Table III.9: Statistics for Access to Finance

Statements	SA%	A%	N%	D%	SD%
Poor access to credit has been a result of inadequate or non-existent collateral.	46.875	31.25	15.625	6.25	0
Compared to medium and small enterprises, large enterprises have a higher likelihood of accessing credit easily.	62.5	31.25	6.25	0	0
Loans are completely denied to borrowers who are deemed to be not creditworthy.	46.875	34.375	15.625	3.125	0
Poor access to credit by SMEs is attributed to a lack of awareness on funding opportunities.	25	40.625	18.75	9.375	6.25
Insufficient credit is available for investment in new business expansion.	31.25	31.25	18.75	9.375	9.375

Source: Constructed by me using data obtained from the survey

The views of the respondents on access to finance statements are presented in Table III.9. Regarding the impact of inadequate or non-existent collateral on access to credit, the findings indicated that the majority of respondents, accounting for 78.125%, agreed with the statement. Additionally, 15.625% remained neutral, while 6.25% disagreed with the statement. This suggests that the lack of sufficient collateral was a significant factor contributing to the limited access to credit by SMEs.

The study aimed to investigate whether large enterprises have an easier time accessing credit compared to medium and small enterprises. The results showed that 93.75%, or a majority, were in agreement with the statement. Additionally, none of the respondents disagreed while 6.25% were indifferent. This implies that financial institutions generally perceive large enterprises as less risky and more likely to repay loans, making them more inclined to provide credit to such enterprises compared to medium and small enterprises.

The study examined whether borrowers considered not creditworthy faced complete loan denial. The findings indicated that 81.25%, agreed. Furthermore, 15.625% remained neutral and 3.125% disagreed. This suggests that financial institutions tend to cease lending to borrowers deemed as not creditworthy.
Another aspect investigated was the impact of a lack of awareness about funding opportunities on access to credit by SMEs. The findings revealed that the majority of the respondents, comprising 65.625%, agreed with the statement. Additionally, 18.75% remained neutral and another 15.75% disagreed. This implies that the insufficient awareness about funding opportunities contributes to the limited access to credit by SMEs.

The study also explored whether there is insufficient credit available for investment in new business expansion. The findings indicated that 62.5%, agreed with the statement. Additionally, 18.75% remained neutral and another 18.75% of them disagreed. This implies that many SMEs

face challenges in expanding their businesses due to a lack of adequate credit for investment in new ventures and expansion.

These findings were in agreement with those of Kung'u (2011) who conducted a survey in Westlands town, Kenya to examine factor affecting credit access to SMEs and established that start up business were faced with credit access setbacks due to lack of collateral and information. He concluded that there is positive relationship between business information, collateral and access to credit.

III.3.5 Discussion of Research Findings.

Results of the inferential statistics indicated that interest rates had a negative and significant effect on access to finance by SMEs in Uganda. These findings agree with those of Gideon (2019) who described interest rates as being capital returns for lenders and thus lead to high lending rates, which discouraged SMEs from borrowing and reducing their creditworthiness. The present study's findings align with the research conducted by Rahman et al. (2017) regarding the link between company size and access to finance for SMEs. Specifically, both studies concluded that company size influences access to finance.

The findings indicate a negative connection between company size and access to finance for SMEs, implying that larger SMEs have better access to financial resources. On the other hand, for micro firms, the link between company size and access to finance is negative, as evidenced by a big number of the respondents who voted against it. This indicates that micro firms are facing even more challenges when attempting to secure financing from commercial banks. Based on the findings of the current study, SACCOs can access credit more easily if certain policies are implemented. Both studies found that the cost of credit rating policies, cost-to-penalty policies, and penalty-to-penalty policies adversely affected SACCOs' access to credit.

Results of the inferential statistics also indicated that credit profile had a positive and significant effect on access to finance by SMEs in Uganda. These findings agreed with those of Yoshino and Taghizadeh-Hesary (2015) whose study indicated that credit-reporting systems limit the influence of asymmetric information on credit markets by assisting lenders in better screening borrowers and avoiding adverse selection, as well as by providing an incentive for borrowers to repay their debts, hence minimizing moral hazard. The majority of SMEs require more capital than microfinances and banks can give. The findings also agree with those of OECD (2018) whose study indicated that many SMEs and entrepreneurs rely heavily on debt to fund their start-up, cashflow, and investment needs. However, SMEs typically face challenges in obtaining debt financing compared to large corporations due to the lack of expertise and skills in financial reporting, under collateralized, have limited credit histories, and lack access to credit due to asymmetric information and agency issues.

Findings also indicated that SME’s performance had a positive and significant effect on access to finance by SMEs in Uganda. These findings were in agreement with those of Wafula and Miroga (2020) whose study on relationship between SME’s performance and the credit terms set by banks found that the performance of small and medium businesses in Bungoma County was affected by the amount of collateral offered, the interest rate, and the length of time given for repayment. In addition, Fowowe (2017) carried research similar to the current study. Both studies concluded that firms with fewer credit constraints experience faster growth compared to

those facing significant constraints. This suggests that improved access to financial resources positively influences the performance and growth of organizations. Similarly, the findings align with the research conducted by Murigi (2014) regarding the impact of access to financial resources on the performance of SMEs in Mukuru slums. Both studies revealed a favourable and significant effect of access to finance on SME performance, indicating that SMEs with better access to financial resources tend to perform better.

In addition, the results of this study show that collateral requirements have a negative and positive effect on SME financing in Uganda. These findings are consistent with research by Mathea (2014), which shows that banks often use a risk-negative approach when evaluating loan repayments for arrears. Therefore, financial needs have become an important factor affecting the financing of SMEs. Despite the improvement in loans to SMEs, banks are still cautious due to lack of assets and records for most of these businesses. The findings are also consistent with the findings of Mumin (2018), who found that financial institutions require certain documents before issuing loans. It was also determined that most of the applicants were denied loan applications because they did not have sufficient capital. The study concluded that the SME profile has an impact on access to credit, just as the age of the owner or manager before purchasing loan money has an impact on access to finance.

III.4 **SUMMARY, CONCLUSION, AND RECOMMENDATION.**

III.4.1 Introduction.

This section provides a concise overview of the key findings, draw conclusions based on those findings, and offer recommendations that align with the topic and objectives of the study

III.4.2 Summary of the Findings

This study's research strategy was a descriptive survey method, coupled with the application of multiple regression analysis for data investigation and analysis. Access to finance was measured by interest rate, credit profile, SME's performance, and collateral requirements. The study's conclusions showed that these characteristics had a favourable and statistically significant influence on the availability of credit.

III.4.2.1 ***Effects of Interests Rates on SME's Access to Finance***

This study's main goal was to investigate how interest rates affect SMEs' access to financing in Uganda. The results showed a notable link between interest rates and the ability of SMEs to access finance in Uganda. Aspects of interest rates such as BOU interest rate caps and interest changed by banks raises the interest charged on loans making them more expensive for SME's.

III.4.2.2 ***Effect of credit profile on SMEs access to finance***

In addition to examining the impact of interest rates, this study also sought to investigate the influence of credit profile on the access to finance for SMEs in Uganda. The findings revealed a notable and positive correlation between credit profile and the ability of SMEs to access finance in the country. Various aspects of credit profile such as CRB rating and listing prevents most SME’s from accessing loans from most financial institutions where the rating is a determinant to accessing finance.

III.4.2.3 ***Effect of SME’s Performance on SME’s Access to Finance***

Examining the effect of SMEs' performance on their ability to acquire financing in Uganda was another goal of this study. Results showed that the effectiveness of an SME had a substantial impact on SME’s access to finance in the different regions of Uganda. Various aspects of performance such as return on assets affected SME’s performance and was a big determinant to access to finance by SMEs in Uganda.

III.4.2.4 ***Effect of Collateral Requirements on SME’s Access to Finance***

The goal of the study was to determine how collateral restrictions affected SMEs' ability to get financing in Uganda. The results showed a negative and statistically significant correlation between the need for collateral and SMEs' ability to receive financing in the country. Factors such as the value and level of collateral were identified as influential in determining SMEs' ability to access finance.

III.4.3 Key Insights.

The facts above lead to the conclusion that interest rates have a considerable negative influence on SMEs' access to financing in Uganda . Interest rates make finance or loans from financial institutions more expensive and most SMEs cannot afford to pay the high interest rates charged on loans.

The study also concluded that credit profiles significantly impacted SME's access to finance in Uganda. Listing of most SMEs on Credit Reference Bureau (CRB) denies them an opportunity to access funds and finances from other lending institutions and this denies them a chance to access resources that they can use to expand their businesses.

SMEs’ performance significantly affected their access to finance in Uganda. Most financial institutions use performance to gauge how well an SME performs and their access to finance is pegged on their performance. SME’s performance therefore plays a key role in their access to finance.

Finally, the study concluded that collateral requirements had a negative but significant effect on SME’s access to finance in Uganda. Inability of SMEs to pledge tangible securities is a hindrance to their access to credit facilities. The study also came to the conclusion that the expenditures of the collateralization procedure, including legal fees, stamp duty, appraisal, and insurance act as deterrents for SMEs seeking to borrow funds. These additional expenses discourage SMEs from accessing finance.

III.4.4 Recommendations

The study recommends a review of the interest rates that banks and other financial organizations charge to allow more SMEs to access funds to expand their businesses. Leaders should legislate and develop laws that evaluate and harmonize the interest rates charged by various financial institutions to make funding more accessible.

Alternative collateral securities must be sought because the majority of SME's do not own titles and logbooks that are majorly required by financial institutions as securities to access funds. This could be through the SME’s guaranteeing each other using their businesses to access funds from financial institutions.

Credit rating policies should be made more accommodative to the SMEs to enable them access to finance that translates to SME’s operating viable businesses.

Government should develop alternative collateral guarantee arrangement through legislation that would serve as a substitute for lending institutions for SMEs to access finance to expand their businesses.

III.5 Conclusion

This research has comprehensively examined the multifaceted barriers to credit access experienced by individuals and small to medium-sized enterprises (SMEs) within the financial landscape. Through a detailed analysis of survey data, it has become evident that factors such as high interest rates, stringent collateral requirements, limited financial literacy, and inadequate financial resources significantly hinder credit acquisition from financial institutions. The findings underscore a crucial disconnect between the financial needs of borrowers and the services offered by financial institutions.

The implications of these barriers are profound, not only limiting individual and business growth but also impacting broader economic development. Particularly, SMEs—often heralded as the backbone of economic growth—face disproportionate challenges that stymie their potential for expansion and innovation. Moreover, the survey responses illuminate a pressing need for financial institutions to adopt more inclusive and adaptive practices to meet the diverse needs of their clientele.

As the financial sector continues to evolve, it is imperative that both policy makers and financial institutions take active steps to reform current practices. Emphasizing financial education, revising collateral requirements, regulating interest rates, and leveraging advanced analytics to enhance credit assessment processes can significantly ameliorate the issues identified. Such reforms not only aid in bridging the existing credit gap but also foster an inclusive financial environment conducive to sustainable economic growth.

In conclusion, this research advocates for a more enlightened approach to lending, one that is attuned to the realities of the borrowers' financial environments and designed to support rather

than impede their financial aspirations. By implementing strategic reforms based on the insights gleaned from this research, financial institutions can enhance their operational effectiveness and contribute positive.

GENERAL CONCLUSION

The study on bank financing for SMEs in Uganda, particularly within the realm of private banks, underscores the crucial role these financial institutions play in nurturing the growth and sustainability of small and medium enterprises. SMEs are the backbone of Uganda's economy, driving employment, innovation, and economic diversification. Despite their significance, these enterprises face substantial challenges in accessing necessary financial resources, including high interest rates, stringent collateral requirements, limited credit histories, and performance-related barriers.

The research findings highlight the considerable negative impact of high interest rates on SMEs' access to financing. Elevated interest rates make loans from financial institutions prohibitively expensive, deterring many SMEs from seeking external funding. Additionally, the study reveals that credit profiles significantly influence SMEs' access to finance. Many SMEs are listed on Credit Reference Bureaus, which limits their ability to obtain loans from other financial institutions, thus stifling their growth potential. The inability to secure affordable financing restricts SMEs from investing in new technologies, expanding operations, and enhancing their overall competitiveness.

Performance metrics also play a critical role in determining SMEs' access to finance. Financial institutions often gauge the viability and stability of SMEs based on their performance records. SMEs with robust financial performance are more likely to secure financing, while those with weaker performance face significant hurdles. The requirement for collateral poses another substantial barrier. Many SMEs lack sufficient tangible assets to pledge as security, making it difficult for them to meet the collateral requirements set by banks. The additional costs associated with the collateralization process, including legal fees and appraisal costs, further deter SMEs from seeking bank loans.

The study employed a mixed-methods approach, combining quantitative surveys and qualitative interviews, to provide a comprehensive understanding of these challenges. The integration of both data sets offers a nuanced perspective on the multifaceted nature of SME financing issues. The findings underscore the need for financial institutions and policymakers to develop targeted strategies that address these barriers. Such strategies may include offering lower interest rates, reducing collateral requirements, and providing tailored financial products that meet the unique needs of SMEs.

In conclusion, improving access to bank financing for SMEs in Uganda requires a concerted effort from both financial institutions and policymakers. By addressing the identified challenges, private banks can play a pivotal role in unlocking the growth potential of SMEs, thereby contributing to broader economic development and poverty reduction in Uganda. The study's insights pave the way for future research and policy interventions aimed at enhancing the financial inclusion and sustainability of SMEs in Uganda. Future research should also consider exploring the impact of digital financial services and alternative financing mechanisms to further support SME growth in the region.

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APPENDICES.

APPENDIX 1: INTRODUCTION LETTER

Joomu Kenneth,

Po Box 06000,
Amizour, Algeria
University of Bejaia.

Dear Sir/Madam,

RE: Request to Conduct Research,

I am currently enrolled as a student pursuing a Master's Degree in Economics at University of Bejaia, Algeria. As part of my academic requirements, I am conducting research focused on the challenges faced by SMEs in accessing bank financing in Uganda. Enclosed with this message is a questionnaire, and I kindly ask for your participation in completing the questions. You can trust that all the information you provide will be handled with the highest level of confidentiality. If you express interest in the research findings, I will gladly share them with you upon request. Your cooperation and contribution to this study would be greatly appreciated. Thank you for your valuable support.

Sincerely,

Joomu Kenneth
Amizour, Bejaia

APPENDIX 1 : QUESTIONNAIRE

SECTION A: GENERAL INFORMATION OF THE ENTERPRISE.

1. Gender*?* Male { }

Female { }

2. Education Level?

Post Graduate { } Degree { }

Diploma { }Secondary Certificate { }

Any other (Specify) ……………………

3. Years of operation for this business?

Less than 1year { }1 -3 years { }

4 -7 years { }Over 7 years { }

4. How many employees have you employed?

Less than 5{ } 6-50 { }

51-100 { } 101 and above{ }

5. Under what type of category ownership is the company?

Sole proprietorship. ( )

Private limited liability ()

Partnership()

Association()

Cooperative. ( )or

NGO ()

SECTION B: INTEREST RATES

Kindly tick appropriately whether you agree with the statements relating to the effect of interest rates on credit access from financial institutions, where (SA-strongly agree, N-Neutral, D-Disagree, SD-strongly disagree).

Statements	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
Interest rates charged by financial institutions are relatively high for most SME businesses in Uganda.					
Many SMEs are deterred from seeking banking institutions for lending facilities by the high interest rates.					
The prevailing lending rates offered by financial institutions have had a discouraging effect on many SME owners, leading them to hesitate in seeking both short-term and long-term loans for their businesses.					
Financial institutions tend to exhibit bias when assessing SMEs for loans or credit, in contrast to large corporates					

C: CREDIT PROFILE

Kindly tick appropriately whether you agree with the statements relating to the effect of credit profile on credit access from financial institutions, where (SA-strongly Agree, N-Neutral, D-Disagree, SD-strongly disagree).

Statements	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
Poor credit rating has led to challenges in accessing finance from financial institutions.					
Previous credit facilities limit access to current credit.					
Borrowers not having a credit history are deemed to be risky.					
Listing by mobile apps prevents SME's from accessing credit from financial institutions					
Credit is not available in sufficient amounts to finance new business growth.					

SECTION D: PERFORMANCE

Kindly tick appropriately whether you agree with the statements relating to the effect of performance on credit access from financial institutions, where (SA-strongly A-agree, N-Neutral, D-Disagree, SD-strongly disagree).

Statement	**Strongly Agree**	**Agree**	**Neutral**	**Disagree**	**Strongly Disagree**
Lack of finance from financial institutions has affected my business performance.					
Capital structure affects performance of an organization					
Lack of proper management skills in my business affects performance					
Use of advanced technology increase performance					
I have undergone training on credit management that has helped me to run the business effectively.					
Size of a firm affects its access to credit and ultimately its performance.					

SECTION E: COLLATERAL REQUIREMENTS

Indicate the implications of collateral restrictions on obtaining loans from financial institutions where (SA-strongly A-agree, N-Neutral, D-Disagree, SD-strongly disagree) by checking the applicable boxes

Statement	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
The limited ability of SMEs to provide tangible assets as security hinders their access to credit facilities					
The absence of fixed assets poses a challenge for many SMEs in accessing credit					
Borrowing by SMEs is discouraged due to the costs associated with the collateralization process, such as legal fees, stamp duty, valuation, insurance, and others.					
SMEs are discouraged from borrowing due to the lengthy process involved in registering and creating a charge on the security they pledge to financial institutions.					
Potential borrowers are discouraged from borrowing due to the strict and demanding credit terms imposed by financial institutions					

SECTION F: ACCESS TO FINANCE

Tick the boxes that best describe how Access to Finance has affected your ability to obtain credit from financial institutions: SA-strongly Agree, N-neutral, D-disagree, SD-strongly Agree.

Statements	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
Poor access to credit has been a result of inadequate or non-existent collateral.					
Compared to medium and small enterprises, large enterprises have a higher likelihood of accessing credit easily.					
Loans are completely denied to borrowers who are deemed to be not creditworthy.					
Poor access to credit by SMEs is attributed to a lack of awareness on funding opportunities.					
Insufficient credit is available for investment in new business expansion.					

THANK YOU

ABSTRACT

This study investigates the challenges faced by Small and Medium Enterprises (SMEs) in accessing bank financing from private banks in Uganda. SMEs are critical to Uganda's economic growth, contributing significantly to GDP and employment. However, access to finance remains a major obstacle, limiting their potential for growth and innovation.
The primary objective is to analyse the key factors that hinder SMEs in Uganda from securing bank financing, focusing on private banks' lending practices and criteria. The study aims to provide insights into the high-interest rates, collateral requirements, credit profiling issues, and performance inconsistencies that affect SME financing.

A mixed-methods approach is employed, combining quantitative surveys and qualitative interviews. Quantitative data is gathered from a representative sample of SMEs across various sectors, while qualitative data is collected through in-depth interviews with SME owners, managers, and private bank representatives. Addressing the financial challenges faced by SMEs in Uganda requires coordinated efforts from policymakers, financial institutions, and development partners. By implementing the recommendations, private banks can play a crucial role in fostering the growth and sustainability of SMEs, thereby contributing to the overall economic development of Uganda.

Key Words: SME financing, private banks, Uganda, high-interest rates, collateral requirements, credit profiles, financial performance.

Resume

Ce travail de recherche examine les defies rencontrés par les petites et moyennesentreprises (PME) pour accéder au financementbancaireauprès des banquesprivéeesenOuganda. Les PME sontessentiellespour la croissanceéconomique de l'Ouganda, contribuant de manière significative au PIB et à l'emploi. Cependant, l'accès au financementreste un obstacle majeur, limitantleurpotentiel de croissance et d'innovation.
L'objectif principal estd'analyser les principauxfacteurs qui empêchent les PME ougandaisesd'obtenir un financementbancaire, en se concentrant sur les pratiques et les critères de prêt des banquesprivées. L'étudevise à fournir un aperçu des tauxd'intérêtélevés, des exigences de garantie, des problèmes de profilage de crédit et des incohérences de performance qui affectent le financement des PME.

Une approche à méthodesmixtesestutilisée, combinantenquêtesquantitatives et entretiensqualitatifs. Les données quantitativessontrecueilliesauprès d'un échantillonreprésentatif de PME dans divers secteurs, tandis que les données qualitativessontcollectées au moyend'entretiensapprofondis avec des propriétaires, des dirigeantsdes PME et des représentants de banquesprivées.
Relever les défis financiers auxquelssontconfrontées les PME enOugandanécessite des efforts coordonnés de la part des décideurs politiques, des institutions financières et des partenaires de développement. En mettantenœuvre les recommandations, les banquesprivéespeuventjouer un rôle crucial enfavorisant la croissance et la durabilité des PME, contribuantainsi au développementéconomique global de l'Ouganda.

Mots clés :financement des PME, banquesprivées, Ouganda, tauxd'intérêtélevés, exigences de garantie, profils de crédit, performance financière.