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Assessing the Effectiveness of Commercial Banks Capital Financing in Enhancing the Performance of Small and Medium Enterprises (SMEs) in Zambia: A Case Study of Lusaka District

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Abstract

The paper assesses the effectiveness of commercial banks' capital financing in the performance of SMEs in the Lusaka district. A structured questionnaire and a semi-structured interview guide were used to collect data from 99 randomly sampled SMEs in the Lusaka district and 1 purposively sampled respondent from Zambia National Commercial Bank. With the aid of the data analysis tools, the data generated from the respondents were analyzed. Among others, the results of the analysis reveal that SMEs and commercial banks both play an important role in the economic development of a country. The study also reveals that SMEs and commercial banks are highly indifferent to the loan facilities; strict collateral requirements, high interest rates, and the nature of requirements for guarantors dissuade SMEs from accessing loans. Thus, the study concludes that commercial banks' capital financing is key to increased production and growth in profits for SMEs. As such, SMEs should be sensitized about the many products and services that Commercial Banks offer. Therefore, this paper recommends that Banks should formulate inclusive policies and programs that can benefit SMEs, ranging from financial literacy programs, business development programs, business leadership programs, financial markets, trade, and investment among others for us to have a stable and sustainable business community. This paper also recommends policy reforms to reduce interest rates, collateral, and guarantor requirements to allow more SMEs to access loans and grow their business.

Keywords: Commercial Bank, Interest Rate, Loans, Profit, SMEs, Credit Terms

1. Introduction

Small and medium-sized enterprises (SMEs) are acknowledged as the drivers of economic growth in developed and developing nations due to their significant contribution to the creation of jobs and the expansion of the Gross Domestic Product. According to the Organization for Economic Cooperation & Development, SMEs make up the majority of business establishments in most countries. In addition, small and medium enterprises (SMEs) play a major role in economic and social development in all countries of the world, especially developing countries, these SMEs are considered to be the backbone of the private sector, accounting for 90% of private sector establishments and employing 50-60% of the labor force (Magablh and Al-Mahroq, 2007) [18].

The importance of SMEs is acknowledged by the various developmental stages of countries. They play a vital role in the creation of jobs and contribute to the growth of the economy through their participation in various projects and programs. In the European Union for example, SMEs account for 99.9 percent of the 11.6 million businesses created in the bloc (World Bank, 2006) [28]. In the United States of America, SMEs create over 75 percent of the new jobs contributing 40 percent of GDP and 80 percent of the population get their first employment in the SMEs according to World Bank (2010) [29].

The continued existence of SMEs is considered critical to the growth of any economy in the world. Available records show that SMEs occupy 60 to 80% of the global economy (Nnanna, 2002) [23]. The success of SMEs in countries of South Asia is a very good example of the importance of SMEs to the economy. Some of these Asian countries like Malaysia, Taiwan, Thailand, Indonesia, and Singapore whose economies were in muddles for the past three decades, are now among the fastest-growing economies in the world because of their viable SMEs. Global statistical records show that SMEs account for 98 % of

all private companies in the global market contribute not less than 30 % of the global GDP and are responsible for 50% of the global labor force (*ibid*).

For instance, Kenya's small and micro enterprises have contributed greatly to the country's economic growth through employment opportunities, training entrepreneurs, generating income for households. They account for approximately 14% of the gross domestic product (Kombo, *et al* 2011) [16].

In Nigeria the sector has made some contribution to the economic development of the nation, but the contribution is far below the level achieved by countries like India, Malaysia, Indonesia, and the United States of America. Despite that, SMEs in Nigeria employ about 60 % of the labor force, they contribute only 35 % of industrial output and account for 10 % of industrial exports (Nnana, 2002) [23]. The formal financial system in Nigeria provides service to 35% of the economically active population while the remaining 65% are excluded from access to financial services. These 65% are often served by the informal financial sector (CBN, 2005) [8]. Thus, access to finance has remained a major problem for SMEs in Nigeria.

Despite these contributions highlighted, just as in many other countries, Zambian entrepreneurs have continued to face stiff hindrances in raising the required funds for establishing and investing in SMEs. They experience scarcity of funds, limited access to capital markets, and debt funding opportunities. This is because the Zambian financial system contributes poorly to the entrepreneurship and SME sector (CBN, 2010) [9]. The maturity of credits extended to SMEs by the system is often limited to a very short period of repayment with exorbitant interest. With bias in favor of lending to governments due to higher returns and lower risks than SMEs, the system applies tougher screening measures and tends to charge SMEs commissions for assuming risk (*ibid*). It is against this background that this study seeks to add to the existing literature and bridge the gap by assessing the effectiveness of commercial banks capital financing in the performance of SMEs in Zambia; with respect to SMEs in Lusaka district.

1.2 General Objective

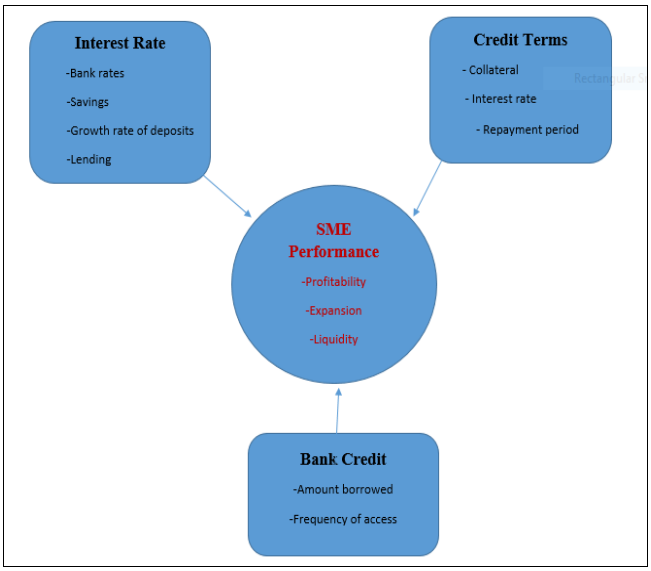
To assess the effectiveness of commercial banks capital financing in enhancing the performance of SMEs in Lusaka district.

1.2.1 Specific Objectives

1. To establish the effects of interest rates on the profitability of SME in Lusaka district.
2. To analyze commercial banks credit on SME performance in Lusaka district.
3. To establish credit terms influence on SME performance in Lusaka district.

1.3 Conceptual Framework

This shows the diagrammatic depiction of the relationship between commercial banks' capital financing and the variables (credit terms, interest rates, bank credit) with their indicators and the performance of SME determinants.



Source: Researcher

Fig 1.1: Conceptual framework for the assessment of commercial banks' capital financing on the performance of SMEs

The conceptual framework depicted in Figure 1.1 shows credit terms, interest rates, and bank credit as independent variables, while SME performance as a dependent variable. The framework shows the effects and relationship of the variables in the study on SME performance. According to Agarwal (2006) [3], credit terms are measured in terms of interest rate, collateral, and repayment period. Bank credit is measured by the amount borrowed/volume and frequency of access which is the number of times one can access credit (Nakiyingi, 2010) [21]. Interest rates are measured by bank rates, saving, lending, and growth rate of deposits (McMahon, 2001) [20]. On the other hand, SME performance is measured by total sales, profitability, and liquidity (Kelley, 2005) [15]. However, credit terms are conditions set by commercial banks in the advancement of credit to meet working capital and short-term liquidity management. They include factors such as interest rate, collateral, and loan repayment periods. Collateral required by commercial banks in developing countries has been a contentious issue in SME financing. Thence, access to bank credit depends on the ability of the business to meet credit terms set by commercial banks. Therefore, improved access to more financial capital can help firms expand more and maintain financial stability, leading to improved SME financial stability (Claessens, 2006) [10].

2. Literature Review

2.1 Effects of interest rates on the profitability of SMEs

The interest rate is a key part of the government's monetary policy. It is a significant determinant of the cost of capital for borrowers and an important measure of reward for savers. Thus, when the interest rate levels in an economy are right, they help to induce savings as well as stimulate investment spending and thereby promote growth. It is common to observe different patterns of interest rate structure in the economic history of a nation. The Interest

rate charged by banks could be regulated to encourage saving mobilization and ensure adequate investment in SMEs for rapid economic growth. The Central Banks of countries utilize regulation of interest rates to increase investment and consumption in the economy. However, according to Amonoo *et al*. (2003) [7], the interest rate is the premium received by the lender after a stated period. From the borrower's point of view, it is the cost of capital at the time of obtaining a loan. Interest rates affect businesses in three significant ways; firstly, rising interest rates increase the total price customers pay to use credits for products and services, therefore, as the interest rate increases the demand for products is likely to decrease. Secondly, most businesses borrow funds to finance their daily business transactions. Therefore, managers must raise the prices of the product to cover the cost of doing business or accept low profit. The third effect of interest rate is on the expansion of a business, and since the firm must sometimes finance new equipment with credits, interest is of great concern to the manager. Therefore, lower interest rates may mean that it is a good time for the business and a higher interest rate will make a manager consider delaying expansion until the cost of borrowing decreases. In the period of rising and falling interest rate, there is a shift in the demand for and the supply of loanable funds, respectively. Demand decreases periodically where large number of business decides to borrow to finance expansion of their operation leading to a rise in the interest rate. Demand also falls after businesses complete their expansion or if they experience widespread of decline in the sales of final goods and services (Aliyu & Bello, 2013) [6].

However, interest rates do not really have an effect on how much people save, because an increased amount of disposable income means that they are more likely to spend it than to save it. When interest rates increase, though, foreign investment can increase because people outside of the country want a larger return for their investment and they are more likely to get it in a state of high interest rates. This causes more demand for the dollar, driving up its value in the international market. The opposite happens, though, when the interest rates are decreased. Although much of it is contained within consumers' perception of the economy and their income, interest rates can drive up consumer spending, investment, and the amount of loans people take out of the bank (Ekpenyong, 1997) [11].

When the economy of a country is not strong, which is a common feature for most developing countries including Zambia, the interest rates on loans are likely to be high. As affirmed by Matala (2014) [19] these rates are even higher on secured loans than on unsecured loans. The rationale behind this is that a secured loan takes more administrative time and personnel than unsecured loans. However, access to bank credit is not just scarce, it is also extremely expensive. The average annual interest rate on loans was 48% in 2005 (the inflation rate was 20%). Large firms and exporters borrow at rates below the average (the prime rate was 20% in 2005). The few small and medium enterprises (SMEs) in Zambia that are able to borrow from banks pay the average annual lending rate or higher. Microfinance institutions lend at rates of around 50-60 per cent. Most loans have a short-term maturity (1-3 months); there are only few loans with a maturity of 1 year or more. The few firms with sources of revenue in foreign currency are able to obtain financing from banks in US dollars at significantly lower interest rates. Bank savings and deposits accounts are not a practical instrument for building savings over time. No interest at all is paid on small savings accounts denominated in Kwacha and only large firms receive positive interest rates on their deposit.

2.2 Analysis of commercial banks credit on SME performance

Firstly, access to finance is a major factor affecting the growth and success of SMEs. The adequate access to financing is critical to enable SMEs to contribute to the economic development of the nation (Hasnah, *et al*, 2013) [13]. Credit financing involves the procurement of interest-bearing instruments, secured by asset-based collateral and have term structures (Nderitu & Githinji, 2015) [22]. The structure could be long-term, short-term or trade credit. To finance working capital, most SMEs rely on internal financing, short-term credit from suppliers, and or specialized financial products like factoring. In the case of capital expenditures, which normally represent larger amounts than working capital needs, SMEs rely on internal financing, often involving fresh capital injections from shareholders (World Bank, 2014) [30]. Long-term funds are not suitable for short-term projects as they burden the firm with the costs of servicing unnecessary debt. Similarly, short-term debts are not appropriate for financing long-term projects since the loan may have to be repaid before the end of the project (Ackah & Vuyor, 2011) [1].

According to research conducted by the Finnish Bank on the issue of bank loans and advances to SME development, the findings describe that in corporate financing the bank treats both SMEs and big corporations the same when they apply for a loan facility and the bank gives loans to every client who meets the loan requirement without preferential treatment. The bank observes that debt financing is a common financing option for Finnish SMEs. The SMEs mostly apply for start-up capital loans, working capital loan and long-term loans for capital investment. The profitability of the business is considered. The bank focuses on financing profitable and healthy businesses. The bank checks the history of the SME's cash flow, the overall financial condition and financial solvency through the evaluation of the company's financial statements over the period. The bank's credit officer assesses the ability of the company to generate enough cash flow each month to easily make payments of interest and amortization. This is one of the important factors the bank considers when making loan decisions. Commercial bank is a type of financial institution whose activities are based on accepting deposits and granting credit. The commercial bank is considered an intermediary between those who have surplus funds and those who need them (FFB, 2013) [12].

Afolabi (2013) [2] investigated the growth effect of SMEs financing in Nigeria. The result of study revealed that the variables - SMEs output by wholesale and retail trade as a component of GDP, commercial banks credit to SMEs, and exchange rate of naira to the US dollar exert a positive influence on economic development. Similarly, Onyeiwu (2012) [25] reviewed the impact of SME financing on the economic growth of Nigeria Outcome of the study revealed that loans to SMEs and other variables except money supply and deficit financing exerted a positive impact on GDP growth.

Furthermore, business owners require a much faster response for loans or other financial appliances than banks

are generally able to achieve. The average turnaround time for SMEs in Zambia to receive a loan, overdraft, asset finance, or any other form of facility from a financial service provider is 30 days and more, in most cases. However, SMEs tend to be in need of the funds as and whenever they formally apply because their needs are usually urgent. The bureaucratic processes in loan appraisal and approval usually attributes to the delay and by the time facilities are approved, the need for the facility would have already been fulfilled by competitors (ZIPAR, 2013) [31].

2.3 To establish credit terms influence on SME Performance

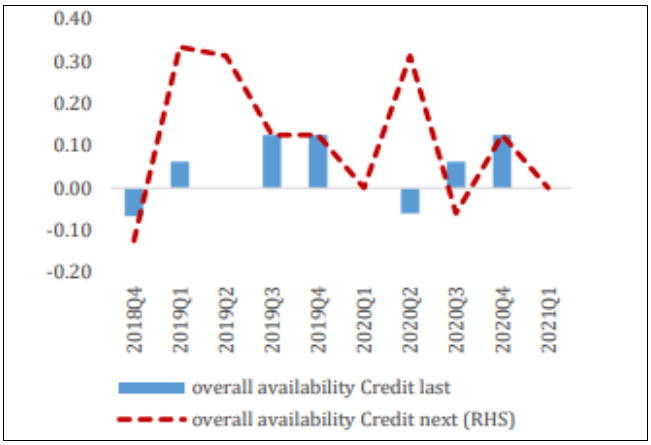
Credit terms refer to standards or negotiated terms (offered by a seller to a buyer) that control the monthly and total credit amount, maximum time allowed for repayment, discount for cash or early payment, and the amount or rate of late payment penalty (Kakuru, 2007) [14]. According to Agarwal (2009) [4], credit terms include factors such as interest rate, collateral and loan repayment periods. Collateral required by commercial banks in developing countries has been a contentious issue in SME financing. However, real-estate collateral provides an incentive and a justification to lend and repay, as well as a means to offset losses in case of default (Otero and Lopez, 2001) in their credit rationing theory argue that in an equilibrium market with problems that are commonly found in financial markets, it would be rational for banks to engage in credit rationing. Due to problems of asymmetric information and agency, banks have difficulty distinguishing good risks from bad risks and monitoring borrowers once funds have been advanced (Organization of Economic Cooperation and Development, 2006).

These terms help in assessing credit worthiness of borrowers and hedge against the risk of loss in case of non-repayment. They include collateral, interest rate, and repayment period (Nyangoma, 2012) [24]. Collateral is a security in the form of an asset that one pledges to access loans. According to Shave (1983, p.38), the mortgage on property or chattel, floating charge on other assets, and personal guarantees will serve as security for a loan. More often than not, SMEs fail to get financial assistance from institutions due to lack of collateral. According to KPMG *et al* (2000) [17] lack of collateral has been repeatedly raised as being one of the most difficult hurdles of entrepreneurs to overcome when trying to obtain loans. This problem is exacerbated by the fact that in many countries the SMEs sector has only existed for just about 10 years and business have not had sufficient time to build up a good equity base.

Nyangoma (2012) [24] found that collateral demanded in Uganda was as high as 150% of the loan making it unfavorable to most SMEs. According to OECD (2006), a suitable financing source remains an obstacle, especially for the growth of innovative SMEs, a problem known as the "SME financing gap". Consequently, small firms rely proportionally more on non-bank sources of financing such as internal funds (savings, retained earnings, family network) and informal sector (money lender), as a result of their inability to produce the collateral requested by commercial banks.

In their study, Agyapong and Darfor (2011) [5] analyzed the criteria for assessing SMEs borrowers in Ghana. The study findings pointed out that when credit managers are deciding on whether to accept or reject a loan application from SMEs, the purpose of the loan, previous loan repayment history, repayment schedule, type of business activity involved, loan size relative to the business size and the provided collateral, ranked highest on their criteria list. The study revealed that lenders took a meticulous interest in risk while dealing with SMEs.

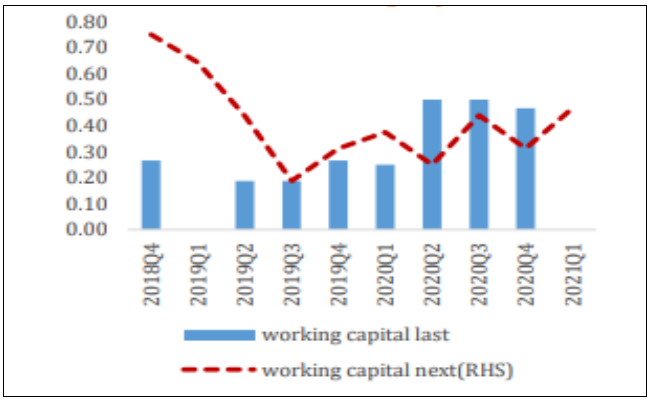
Furthermore, according to the Credit Conditions Survey Report, Fourth Quarter 2020 by the Bank of Zambia, it posits that most banks reported tight credit conditions for SMEs largely due to weak macroeconomic conditions that prompted them to adopt strict criteria in reviewing credit applications (Chart 8). Commercial banks expect tight credit conditions for SMEs to continue in the first quarter of 2021 mainly on account of tight lending requirements driven by the rising default risk.



Source: Bank of Zambia

Chart 8: SMEs Credit Conditions

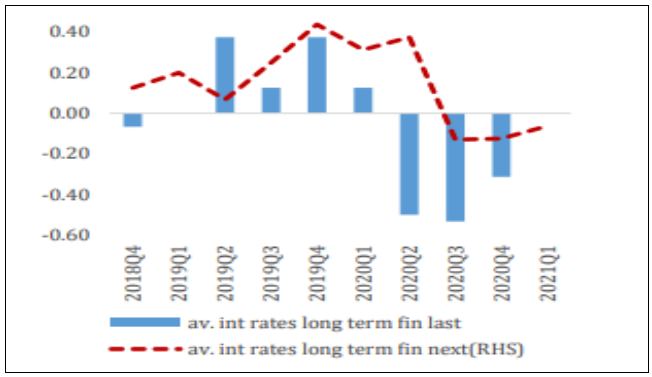
In addition, banks reported a rise in demand for working capital by SMEs for the seventh consecutive quarter consistent with expectations. See chart below:



Source: Bank of Zambia

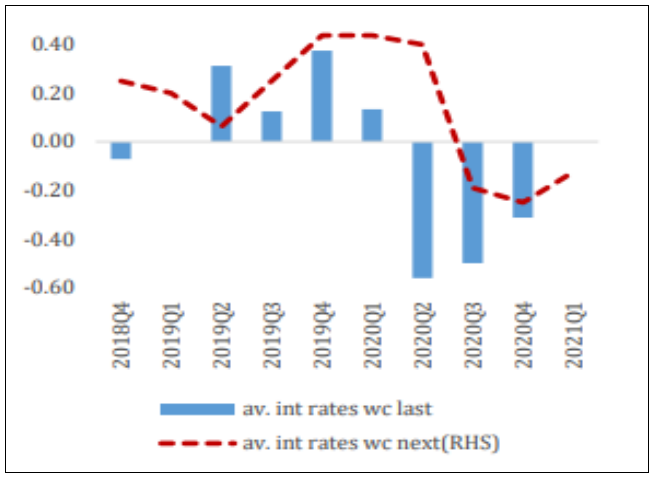
Chart 9: Demand for Working Capital

The rise in demand was due to tight liquidity that led SMEs to seek working capital to support business operations following the partial relaxation of COVID-19 restrictions. Banks expected demand for working capital by SMEs to remain high in the first quarter of 2021 as most of them seek liquidity to stimulate and keep their businesses running in light of rising operating costs. In addition, Lending rates for both working capital and long-term financing were reported to have fallen for the third consecutive quarter. See the charts below:



Source: Bank of Zambia

Chart 12: Intrest Rate - Long- Term Finance



Source: Bank of Zambia

Chart 11: Intrest Rate - Working Capital

The decline in lending rates was mainly attributed to the banks' access to funds under the Bank of Zambia's TMTRF which impacted on the interest rates passed on to SMEs. In the following quarter, commercial banks expected lending rates to remain relatively low as they anticipate the BoZ to maintain an accommodative monetary policy stance in an effort to stimulate economic activity. The tenure for both working capital and long-term financing for SMEs remained relatively long as most banks maintained their existing conditions. In the first quarter of 2021, banks expected to maintain relatively long tenures for both categories of financing. Nevertheless, collateral requirements for both working capital and long-term financing equally remained unchanged as banks rarely revise these requirements. The majority of commercial banks anticipate collateral requirements to remain the same in first quarter of 2021 (Bank of Zambia CCSR, 2020).

2.4 Literature Gap

A lot of research has been carried out locally and internationally reviewing micro and small enterprises. Most of these research studies concentrate on commercial Banks financing SMEs; as such, this shows that there is limited literature on the holistic role of commercial banks in the performance of SMEs. For instance, Kambone (2017) conducted a study focused on the impact of small and medium-scale enterprises in achieving sustainable development growth in Zambia. Sibanda (2018) also researched the assessment of SMEs' financing by commercial banks in Zimbabwe. In the same vein, Uju (2015) conducted research on the role of commercial banks in financing small & medium size enterprises in Nigeria. Ackah & Vuvor (2015) also researched the challenges faced by Small & Medium Enterprises (SMEs) in Obtaining Credit in Ghana. Muyasani (2018) conducted a study on the challenges faced by small & medium enterprises (SMEs) in obtaining credit in Zambia. In the same vein, Nyantakyi & Kyereh (2013) conducted similar research on the challenges behind SMEs' access to debts financing in the Ghanaian financial market. Furthermore, ZIPAR Report (2012) conducted research on the SMEs Access for Finance in Zambia. However, from the researcher's point of view, none of the studies has addressed the holistic effectiveness of commercial banks capital financing on the performance of SMEs. As such, it is from the background that this study is aimed at assessing the effectiveness of commercial banks capital financing on the performance of SMEs in Zambia with special focus on SMEs in Lusaka district.

3. Research Methods

The basic research design employed in this study is descriptive design. The type and source of data will be determined by the objectives of the study. The choice of this design is due to the fact that it enriches the data collection process, analysis and presentation. Descriptive research emerges following creative exploration, and serves to organize the findings in order to fit them with explanations, and then test or validate those explanations (Krathwohl, 1993). Quantitative and qualitative study approaches were used. Linear regression analysis and mean estimation were used to establish the relationship between credit terms, bank credit, interest rate and SME performance. The researcher used a survey and field research to gather quantitative and qualitative data respectively.

3.1 Target population

Population is basically the universe of unit from which the sample is to be selected. According to Babbie (1992) a study population is the aggregation of element from which the sample elements actually selected. The population of interest in this study consists of 9124 registered small and medium businesses with PACRA office and Lusaka City Council.

3.2 Sampling design

For this study, the researcher will employ two sampling techniques: Purposive sampling to sample a key informant at Zambia national commercial bank Simple random sampling to sample SMEs in Lusaka district.

3.3 Sample Size determination

Sample size refers to the number of items to be selected from the universe to constitute the sample, and this answers how many sampling units should be surveyed and interviewed, (Kothari 1990). However, to determine the sample size from our given population of nine thousand one hundred and twenty-four (9124), we will use the Taro Yameni formula as follows;

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

Where:

N= population of Study (9124)

n= sample of study
(e)= level of significance
Note (e) = 0.1 (90% confidence level)

$$n = \frac{9124}{1+9124(0.1)^2}$$

$$n = \frac{9124}{1 + 9124(0.01)}$$

$$n = \frac{9124}{1 + 91.24}$$

$$n = \frac{9124}{92.24}$$

$n = 99$

In addition, 1 key informant was selected purposively, therefore making the total sample size of **100** respondents.

3.4 Data collection methods

The main instruments for data collection is the interview guide and a structured questionnaire with both closed and open ended questions. They will both be administered to the respondents at their business premises. The researcher used structured self-administered questionnaires covering all the variables in the study. In these questionnaires, a five point Likert scale was used to ease data processing and analysis. The scale was marked 1-5 where; 1 represented strongly disagree and 5 strongly agree.

The data to be obtained will mainly be primary sourced through the use of questionnaires and interviews. 99 questionnaires will be self-administered with opened ended and closed ended questions to SMEs. Proper guidance will be offered to ensure accurate supply of information. Due to the busy nature of the banking sector, 1 semi-structured questionnaire will be designed to solicit information from a bank official and this will be done face-to-face.

3.5 Data Analysis

3.5.1 Qualitative analysis

The researcher will use thematic analysis as it looks at patterns of meaning in a data set. Thematic analysis takes bodies of data and groups them according to similarities in other words, themes. These themes help us make sense of the content and derive meaning from it.

3.5.2 Quantitative analysis

Quantitative data will be presented using simple descriptive statistic methods including tables, percentages, pie charts, and linear regression analysis. Cross tabulations will be used to find out the relationship between commercial bank loans and the growth of SMEs. The data collected was computerized, sorted, edited, classified and coded. The resultant data was entered using statistical package STATA for analysis. This generated frequency tables for demographic and descriptive data. The relationship between the study variables was established using regression analysis.

4. Findings and Results

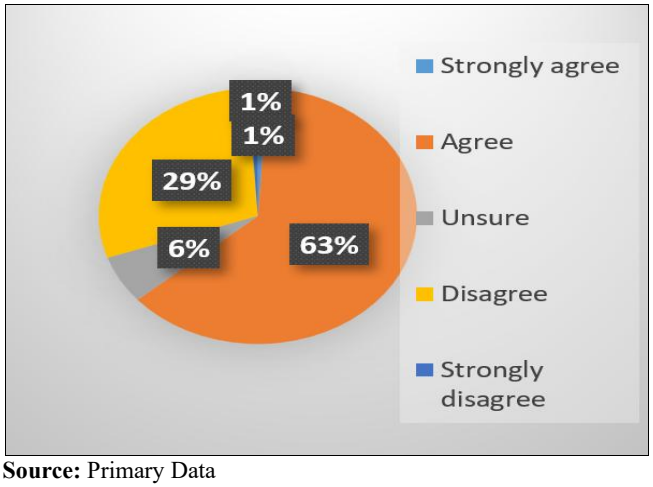
4.1 Characteristics of Respondents (Bio Data)

All the respondents in our research are fully registered SMEs in Lusaka District. However, it is general knowledge that SMEs cut across the various sectors of the economy. The 99 responses received were fairly spread across the wide range of the Zambian economy with the most concentration centered in the Retail and Wholesale industry. This sector alone accounted for 31 of the responses representing 31.31%, then the Retail industry accounted for 26 responses representing 26.26%, Service industry accounted for 16 representing 16.16%, Finance industry accounted for 8 representing 8.08%, Consultancy industry accounted for 4 representing 4.04%, Food industry accounted for 4 representing 4.04%, Wholesale Industry accounted for 2 representing 2.02%, Management and Consultancy accounted for 2 representing 2.02%, Training and Advertising accounted for 1 representing 1.01%, Service and Consultancy accounted for 1 representing 1.01%, Manufacturing Industry accounted for 1 representing 1.01%, Consultancy and Trading accounted for 1 representing 1.01%, Clothing Industry accounted for 1 representing 1.01% then Business advisory accounted for 1 representing 1.01%. On the aspect of capital invested when starting up the business, from the 99 responses the researcher got from the field, 50 respondents invested less than K81, 000 representing 50.02% and then 47 of the respondents invested between K81, 000 – K400, 000 representing 47.96%, and 1 respondent invested above K401, 000 representing 1.02%.

In addition, on the source of the capital invested in their business, 95 respondents stated that their main source of capital was contributions and savings representing 95.95%, 2 of the respondents stated that then obtained a loan from a commercial bank to finance their business representing 2.02%, 1 of the respondents stated that they obtained a loan from a micro finance institution representing 1.01%, 1 of the respondents also mentioned that they obtained a loan from a government agency representing 1.01% and then 1 other respondent stated that their source of capital was contributions from family and friends representing 1.01%.

Furthermore, when asked whether they (SMEs) have bank accounts or not, all the 99 respondents said Yes, representing 100%.

4.2 To establish the effects of interest rates on the profitability of SME in Lusaka district.

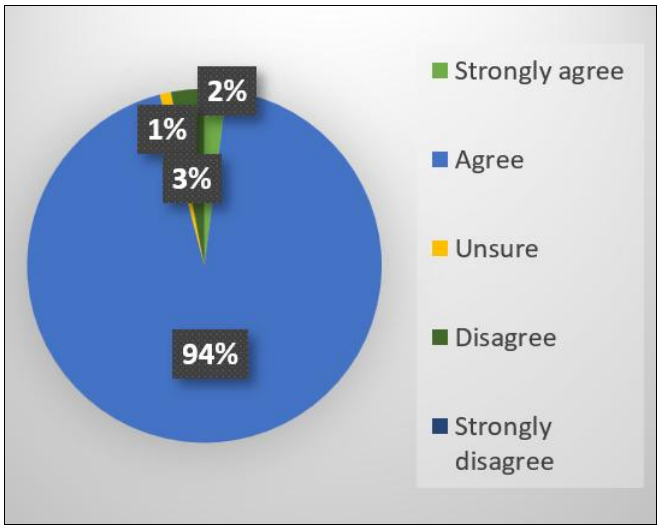


Source: Primary Data

Fig 1.1: There are high charges on deposits in commercial banks

According to the researcher's findings on the aspect whether there are high charges on deposits in commercial banks or

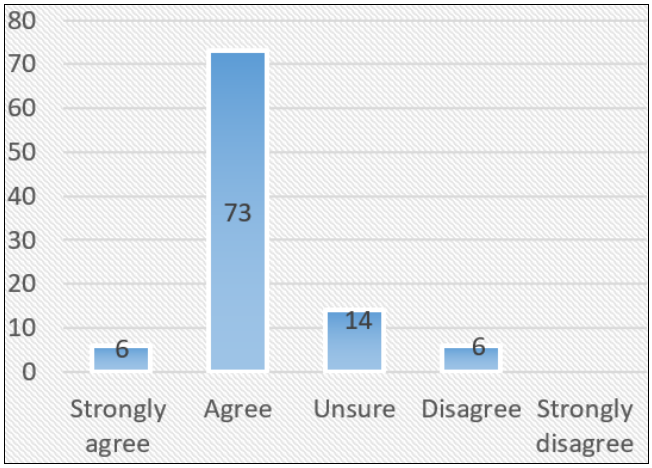
not, 62 respondents agreed to the fact that there are indeed high charges on deposits in commercial banks, representing 63%, 29 respondents disagreed representing 29%, 6 of the respondents were unsure, 1 respondent, strongly agreed and 1 other respondent strongly disagreed.



Source: Primary Data

Fig 1.2: My deposits in terms of savings have helped develop my SME

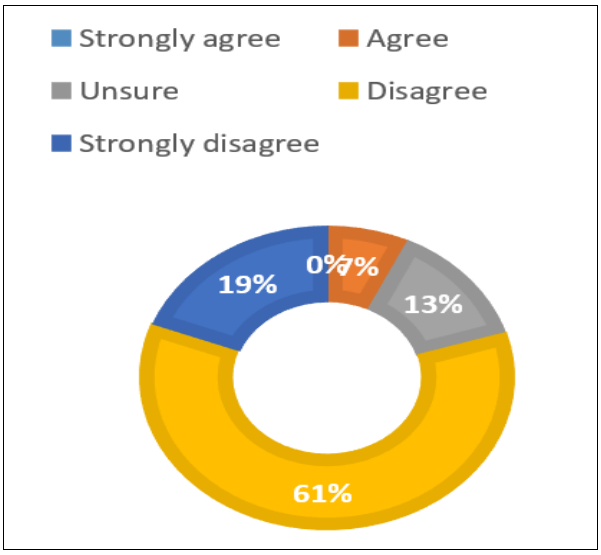
According to our findings on the aspect whether the deposits in terms of savings have helped develop the SMEs or not, 93 respondents agreed that savings have abetted in the development of their SME representing 94%, 3 respondents disagreed representing 3%, 2 respondents strongly agreed representing 2% and 1 respondent was unsure representing 1%.



Source: Primary Data

Fig 1.3: Commercial banks charge high interest rates on the money the lend

Based on our findings on whether commercial banks charge high interest rates on the money they lend, 73 respondents agreed to this facet that indeed commercial banks do charge high interest rates on the money they lend representing 74%, 14 respondents were unsure representing 14%, 6 of the respondents strongly agreed representing 6% and 6 others disagreed representing 6%.



Source: Primary Data

Fig 1.4: Commercial banks charge low interest rates on the money the lend

Based on our findings on whether commercial banks charge low interest rates on the money they lend, 60 respondents disagreed to the assertion that commercial banks do charge low interest rates on the money they lend representing 61%, 19 respondents strongly disagreed representing 19%, 13 of the respondents were unsure representing 13% and 7 others agreed representing 7%.

Regress: What is your firms Gross Profit against Interest rates aspects?

What is your firms Gross Profit	Coef	S.E	t	P<|t|	95% C.I
There are high charges on deposits in Commercial Banks	28293.85	17475.33	1.62	0.109	-6423.939
My savings in terms of my savings have helped develop my SME	-81001.48	48552.96	-1.67	0.099	-177465.4
commercial banks charge high interest rates	54326.05	38515.27	1.41	0.162	-22191.26
commercial banks charge low interest rates	-16341.17	31028.34	-0.53	0.600	-77984.39
commercial banks interest rates have affected my business expansion	-88678.2	24634.6	-3.61	0.000	-137420.5
_CONS	378827.6	220358.5	1.72	0.89	-58952.8

Source: Primary Data

Using a 95% interval confidence level on this linear regression analysis, the outcome has been shown that the one with the highest likeliness of affecting the gross profit with respect to interest rate is low interest rate charged when SMEs obtain loans from commercial banks which had a probability of 0.600. In this quest, when banks charge low interest rates on the loans, it will enable more SMEs have access to bank credit, thereby investing it in the business, yield high returns and hence affect the gross profit positively. On the other hand, if the interest rates are high, it will mean that only a few firms will be able to obtain loans to finance their businesses.

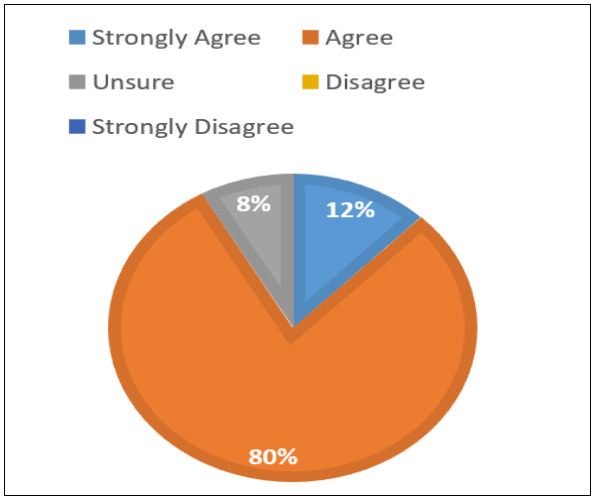
Regress Net Profit with Interest rates aspects

What is your firms Net Profit	Coef	S.E	t	P<|t|	95% C.I
There are high charges on deposits in commercial Banks	16557.97	18588.38	0.89	0.376	-20441.27
My savings in terms of my savings have helped develop my SME	-29672.07	48511.09	-0.61	0.543	-126231
commercial banks charge high interest rates	97864.41	43344.97	2.26	0.027	11588.4
commercial banks charge low interest rates	-14578.87	32494.55	-0.45	0.655	-79257.65
commercial banks interest rates have affected my business expansion	-60248.27	30120.41	-2.00	0.049	-120201.5
_CONS	378827.6	220358.5	1.72	0.89	-58952.8

Source: Primary Data

Using a 95% interval confidence level on this linear regression analysis, the outcome has been shown that the one with the highest likeliness of affecting the net profit with respect to interest rate is low interest rate charged when SMEs obtain loans from commercial banks which had a probability of 0.655. In this quest, when banks charge low interest rates on the loans, it will enable more SMEs have access to bank credit, thereby investing it in the business, yield high returns and hence affect the net profit positively.

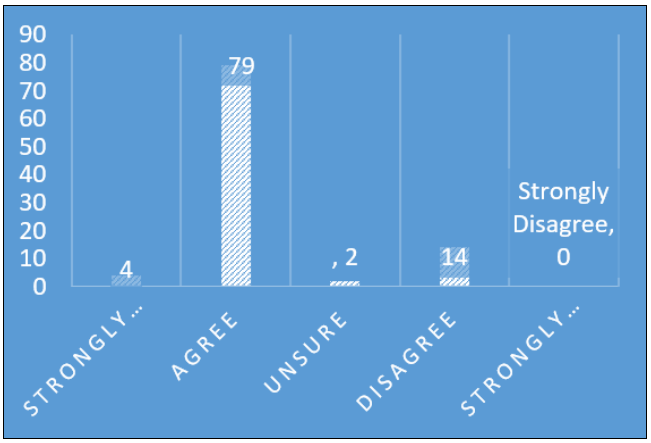
4.3 To analyze commercial banks credit on SME performance in Lusaka district



Source: Primary Data

Fig 1.5: Frequency of access to loans helps in the growth of the firm

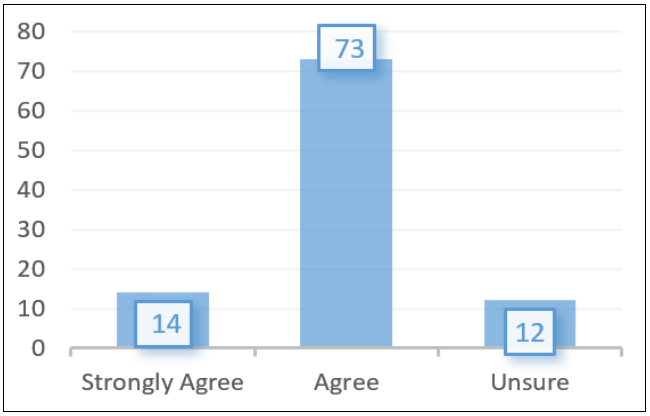
According to our findings on whether the frequency of access to loans helps in the growth of the SME or not that when an SME has frequent access to loans, it aids in the growth and development of the business, 79 respondents agreed representing 80%, 12 respondents strongly agreed representing 12%, and 8 of the respondents were unsure representing 8%.



Source: Primary Data

Fig 1.6: The firm has enough information on credit availability

Based on our findings on whether the firm has enough information on credit availability or not, 79 respondents agreed representing 80%, 14 respondents disagreed, representing 14%, 4 respondents strongly agreed and 2 respondents were unsure.



Source: Primary Data

Fig 1.7: Loans from Banks would greatly increase sales revenue and profits

Based on our findings, 73 respondents agreed that loans from banks increase sales revenue and profits representing 74%, while 14 respondents strongly agreed, representing 14% and then 12 respondents were unsure, representing 12%.

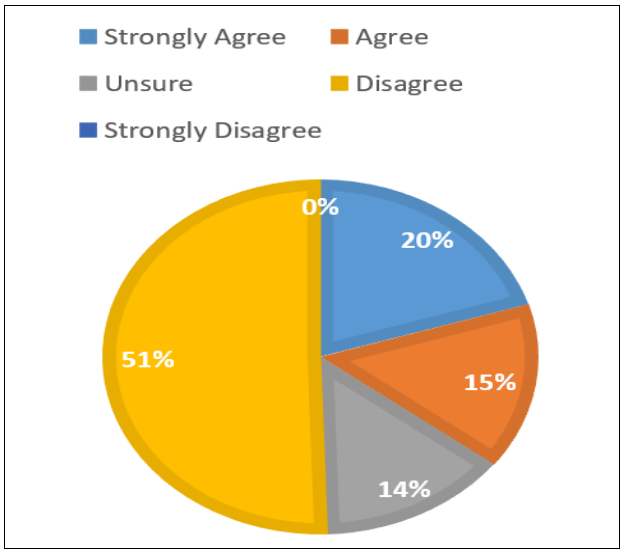
Regress Net Profit with Bank Credit aspects

What is your firms Net Profit	Coef	S.E	t	P<|t|	95% C.I
Frequency of access to loans helps in the growth of the firm	16369.32	42777.92	0.38	0.703	-68778.01
The firm has enough information on credit availability	4417.276	44396.81	0.10	0.921	-83952.36
This firm has reliable security guaranteed to access credit	-40862.11	53259.73	-0.77	0.445	-146872.9
Policies of commercial banks influence the firm's decision to obtain credit	-107294.4	44729.58	-2.40	0.019	-196326.4
Loans from banks would greatly increase sales revenue and profits	52800.54	54345.53	0.97	0.334	-55371.54

Source: Primary Data

Using a 95% interval confidence level on this linear regression analysis, the outcome has been shown that the one with the highest likeliness of affecting the net profit with respect to bank credit is the availability of enough credit information to the firms; which had a probability of 0.921. Thus, this means that if firms have enough information on credit availability, it will enable them to make sane decisions on how they can obtain credit from the bank. When they obtain credit to boost their business, it will contribute positively towards the net profit. Hence, credible information is key to SMEs obtaining credit from commercial banks.

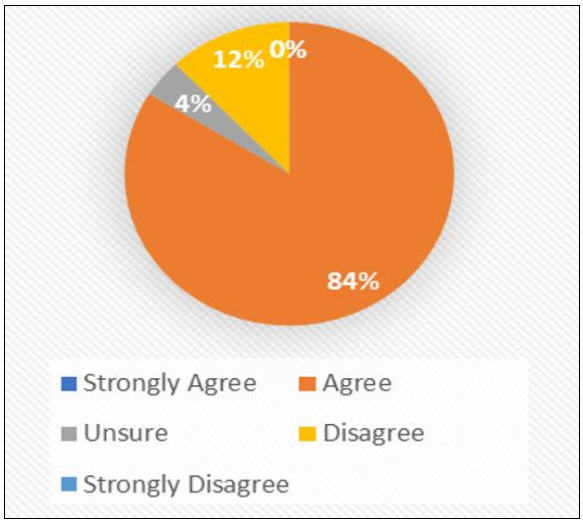
4.4 To Establish credit terms influence on SME performance in Lusaka district



Source: Primary Data

Table 1.2: This firm feels interest rates charged are reasonable

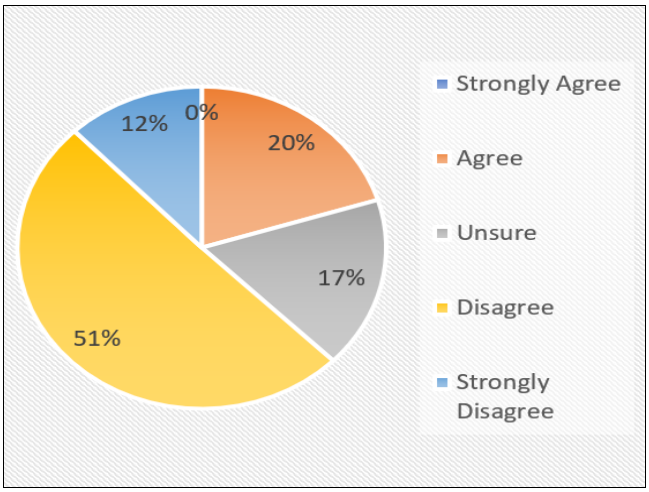
According to our findings shown in the pie chart above, 51% of respondents disagreed to the assertion that firms feel interest rates charged are reasonable, then 20% of respondents strongly disagreed, 15% of respondents agreed, and then 14% of respondents were unsure.



Source: Primary Data

Table 1.3: This firm has sufficient collateral to obtain credit from commercial banks

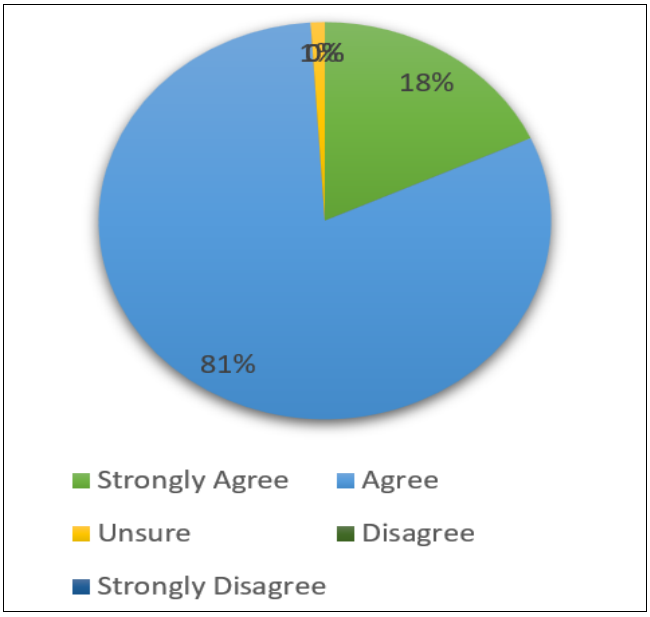
According to our findings, 84% of respondents stated that they have enough collateral to obtain credit from commercial banks, then 12% of the respondents disagreed and 4% respondents were unsure.



Source: Primary Data

Table 1.4: The loan repayment period given to this firm is convenient

Based on our findings, 51% of respondents disagreed that the loan repayment period given was not convenient, then 20% of respondents agreed that the loan repayment period given was convenient, then 17% of respondents were unsure and 12% of respondents strongly disagreed.



Source: Primary Data

Table 1.5: Lack of credible information on the part of SMEs creates a barrier to obtaining credit from the bank

As shown the pie chart above, 81% of respondents agreed that lack of credible information on the part of SMEs creates a barrier to obtaining credit from the bank, then 18% of respondents strongly agreed and then 1% of respondents were unsure.

A Linear regression analysis of credit terms against net profit to establish the performance of the firm. Using a 95% interval confidence level on this linear regression analysis,

the outcome has been shown that the one with the highest likeliness of affecting the net profit with respect to credit terms is lack of information on the part of the SME which creates a barrier to obtaining credit from the commercial bank; it had a probability of 0.884. Thus, this means that if firms do not have adequate information on credit disposal and requirements for attaining credit, it would be a barrier for them to successfully obtain credit from the bank and this would affect the net profit negatively. But if they have the right information, it would be easy for them to obtain credit and this would affect the net profit positively. Hence, credible information is key to SMEs obtaining credit from commercial banks.

4.5 SME Financial Performance

The researcher is trying to analyze the financial performance of the firms. However, the researcher will firstly present a mean estimation of the gross profit, net profit and net sales. Then present the findings on a pie chart and further present chi-square plots on both net profit and gross profit.

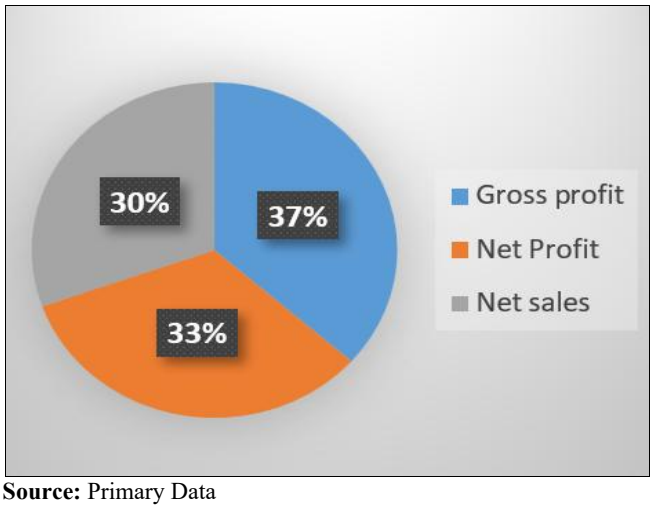
Mean estimation Number of Obs =62

	Mean	Std. Er.	(95% Conf Interval)
Gross Profit	151096.8	21892.97	107319.1 194874.5
Net Profit	136571	20694.65	95189.45 177952.5
Return on sales	125837.1	19766.9	86310.74 165363.5

Source: Primary Data

According to our findings on the mean estimation of the three financial indicators of a business, Gross profit was estimated at 15109.8, then Net profit was estimated at 136571 and then Returns on sales were estimated at 125837.1. Thus, with a 95% confidence level, the gross profit was the highest with 107319.1, then the net profit at 95189.45 and then the returns on sales at 86310.74.

See the distribution of the three indicators of financial performance (Gross profit, net profit and returns on sales) on the pie chart below:



Source: Primary Data

4.6 Discussion of Results

This section addresses some of the key or major findings of the study and briefly gives an analysis to the study in line with the research question and objectives.

The following are some of the major findings of the study;

In trying to ascertain the effects of Interest rates on the profitability of the SMEs, a linear regression analysis was implored and the results showed that low interest rates have a positive effect on the profitability of the business. With a 95% confidence level, the probability of low interest rates affecting the gross profit was 0.66 and the probability of affecting the net profit was 0.655. In most cases, low interest rates will attract more people to obtain loans to boost their business which would in turn increase profits, unlike when there are high interest rates, firms find it difficult to get loans.

In addition, it was found that most SMEs do not have sufficient information on the services that banks offer. Issues ranging from Interest rates on the loans, collateral, the loan repayment period. However, the banks should not just be theoretical but be practical in ensuring that they help SMEs understand better what they are doing and hence give them a way to benefit from the products and services the bank is offering. When collecting data from the bank, the researcher came to learn that ZANACO has financial literacy programs running of which most SMEs don't know about. Hence the bank should focus on inclusivity and engage more SMEs in their training programs so that the positive effect of the bank on SMEs can be felt. The researcher believes that it is only when SMEs are educated enough on how to conduct business and on how to understand market dynamics that they can build viable and sustainable businesses and then contribute positive to the growth of the local economy.

However, in analysing the impact of commercial bank credit on SME the findings showed that more than 80% of the respondents agreed that frequency of access o loans affects the business growth positively and more than 80% agreed that they had enough information on credit availability. In addition, after performing the linear regression analysis on bank credit and Net profit in order to ascertain the performance of the firm, the results showed that one aspect that would affect the net profit was the availability of information on credit. This clearly shows that if their sufficient information on credit and firms are able to understand, it would push them to obtain loan that would in turn boost their business and affect their profits and improve its performance. Further, as explained by the respondent from ZANACO, most SMEs would obtain loans from the bank and divert their use to intended purpose, hence they fail to actualize and boost their production and surely even generating profits. Thus, the most cardinal thing is to help SMEs understand the kind of financial services that the bank is offering and other services too apart from the loan that could help them carry out their day-to-day operations effectively.

Furthermore, Credit terms are central to firms successfully obtaining loans from commercial banks. If the firm does not have enough collateral, they cannot be given a loan, the loan repayment period, interest rates and others. From our findings, 83% of the respondents have enough collateral to obtain loans, then more than 50% of the respondents mentioned that the loan repayment period given was not enough. From the results of the linear regression analysis, it showed that lack of information on the part of the SMEs creates a barrier for the SME to obtain credit from the commercial can affect the net profit negatively with a probability of 0.844. However, SMEs have been unable to obtain finance from financial institutions, due to an

information gap, which prevents them from knowing how and where to obtain this finance on acceptable terms, and the risk associated with their failure to pay back funds. The implication is that small businesses face funding limit, and are discriminated against in credit markets, which leads to large firms crowding out smaller firms in the market. The lack of adequate funding means that SMEs will experience low incomes, low profits and low capital formation.

In understanding the financial performance of the SMEs under study, the researcher implored a mean estimation of the three indicators of financial performance (gross profit, net profit and sales turn over), the results showed that most SMEs gross profit and net profit was below the threshold. The reason to this would have been high interest rates that would have deterred SMEs from obtaining credit and a lack of credible information on credit availability and on the requirements needed to obtain credit on the part of SMEs.

All in all, both SMEs and Commercial banks lay a very significant role in the economic development of a country. More so, Commercial banks such as ZANACO should ensure that their products are accessed by all SMEs as they play a huge role in the growth of the SMEs. Through, loan services, overdrafts, financial education, online banking services, PayFlex services, mobile banking services, business development education and many other services, the researcher is very confident that the SME sector may expand and thereby create a positive impact on the country's economic development.

5. Conclusion

There is no doubt that small and medium scale enterprises (SMEs) are a source of development and an engine of growth. SMEs should therefore, immediately become the economic policy priority of government because of their potentials if they have to address our economic ills. Our track record in Zambia in the management of SMEs has proved unsatisfactory. Even now, many of such enterprises cannot pass the test of efficient and effective management. Many have collapsed while many are still grappling with problems that could have been avoided if they had the right information, conducive business environment and the right skill set.

However, the objective of the study was to assess the effectiveness of commercial banks capital financing in the performance of SMEs in Lusaka district. Thus, the study concludes that commercial banks do indeed lay a major role in the effective performance of SMEs. As such, SMEs should be sensitized about the many products and services that commercial banks offer and that commercial banks should journey through with SMEs in their business by providing the right tools to help them grow. This study also concludes that commercial bank loans contribute to increased production and growth in profits for business. This study also concludes that SMEs play a major role in the economic development of a country, ranging from job creation, manufacturing and industrialization, improving the quality of life of people in the community, and influencing policies for rural development and decentralization

Lastly, the present study was confined to SMEs in Lusaka. For further research, it would be useful to carry out a similar study across all the provinces in Zambia and beyond and see whether the same results would be replicated.

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