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Effect of Microfinance Products on Small Business Growth: Emerging Economy Perspective

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Abstract

Small businesses play a significant role in the economic stability and development of emerging economies, and access to financial services is crucial to their growth and performance. This study seeks to ascertain whether microfinance products such as loans, savings, insurance, and education affect small business growth in Ghana. The study uses descriptive and inferential statistics on responses of 248 small business owners for data analysis. Using multiple linear regression analysis, the study found that all the microfinance product or services positively affects small business growth, and the greatest influence is microloans. This study contributes massively to exact literature to the growth of microfinance institutions (MFIs) and small businesses in an emerging economy, Ghana. The study can assist MFIs to assess the effectiveness of their product or services, and can also serve as a guide to effective utilization of available scarce resources leading to the growth of small businesses in emerging economies.

Keywords: Small Business Growth, Microfinance Institutions (MFIs), Entrepreneurs, Ghana

1. Introduction

Small businesses play a significant role in emerging economies (Mead & Liedholm, 1998; Ogunyami & Ojikutu, 2014). For instance, in Ghana, 92 percent of businesses are small businesses, and they contribute 70 percent to GDP and 80 percent to employment. The activities of small businesses to a larger extent creates jobs (Agwu & Emeti, 2014; Boadu, Gabriel, Appiah & Dwomo-Fokuo, 2014; Haider, Asad, Fatima & Abidin, 2017), and government generates a lot of revenue through taxes paid by small businesses which are used to undertake developmental projects in the country (Abor & Quartey, 2010). Due to the

significant role small businesses play, their growth, and sustainability is crucial for economic stability and development. However, many small businesses are unable to grow due to a lack of financial support and assistance from financial institutions (Carpenter, 2001). This is because small businesses are unable to meet the collateral requirements of formal banks as compared to larger firms (Babajide, 2012). They tend to find comfort from the non-bank financial institutions like the microfinance institutions (MFIs) that give credit and other financial services or professional advice that promote their operations.

Microfinance institutions (MFIs) play a major role in the growth of small businesses through the provision of insurance, education, training on financial literacy on working capital management, records keeping, repayment schedule, and inventory management. The activities provided by MFIs help small businesses to reduce the risk of moral hazard and help them to grow. Thus, the significant contributions of MFIs towards small businesses growth made it necessary to examine whether the products or services provided by MFIs affect the growth of small businesses in an emerging market, Ghana where the majority of businesses are small that depend on microfinance for survival.

Prior studies conducted in Ghana normally focus on loans or credits provided by MFIs to ascertain whether it affects small enterprise's growth. To the best of our knowledge, no study has focused on the combination of microfinance products or services that examine its effects on small business growth in Ghana. The researchers felt that there is a need for a study on this area to bridge the gap to find out whether micro-savings, microloans, micro insurance, and education provided by MFIs affect the growth of small businesses in Ghana. Also, the study is of great importance to MFIs in the sense that it can assist them to assess the effectiveness of their product or services and find out the product that contributes massively to the growth of small businesses in an emerging economy and help improve their services. The study can also serve as a guide to effective utilization of available scarce resources leading to the growth of businesses and contributes to the exact literature in emerging economies on the relationship between MFIs and small business growth.

The rest of the paper proceeds as follows. Section 2 reviews the literature. Section 3 discusses the methodology used for the study. Section 4 shows results and discussions. Section 5 concludes the study.

2. Literature Review

2.1 Microfinance Context in Ghana

The term microfinance is the provision of financial services provided to the poor or low-income earners who normally do not have access to formal financial assistance from banks due to lack of collateral, unstable job, and no credit history (Westover, 2008). According to Putzeys (2002), microfinance provides services such as accepting savings, giving loans or insurance, and transfer of money to less endowed individuals. Also, microfinance provides services such as education and professional training on how to invest and how to use loans to increase profitability. Thus, microfinance provides both financial and non-financial services to individuals in the low-income category, and provide managerial services on how to make use of

the funds.

Canadian Catholic missionaries were the first to establish microfinance institutions in the Northern part of Ghana in 1955 to help the poor in the rural areas in Africa. However, some researchers associated the common term "Susu" which originated from Nigeria as the main product that contributes to the emergence of microfinance institutions in Ghana (Asiama & Osei, 2007). Ghana government established variable strategic microfinance interventions program in the olden days to reduce poverty and improve the standard of living of Ghanaians. Among these interventions include the delivery of subsidized microfinance loans formed in the 1950s; the Agricultural Development Bank established in 1965 to ensure the growth of the agricultural sector; the formation of Rural and Community Banks (RCBs) to provide credit to small scale industries in the rural communities and the establishment of non-bank financial institutions like credit unions under the Promulgation of PNDC Law 328 in 1991. The above policies established by various governments created the development of three major types of microfinance institutions in Ghana namely the commercial banks, rural and community banks, and microfinance savings and loans institutions (Asiama & Osei, 2007). They were designed to cater to the poor and enhance their livelihood in terms of job creation and improved economic activities.

2.2 Small Business in Ghana

Small businesses cover a heterogeneous group of businesses in Ghana, ranging from a single artisan working in a small shop that makes handicrafts for a village market to sophisticated engineering firms selling in overseas markets (Fischer & Reuber, 2003). There are numerous definitions for small businesses based on size, turnover, activity, ownership, and legal status in Ghana. Due to its heterogeneous nature, there is no unified definition of what constitutes a small business. The study adopts the definition given by National Board for Small Scale Industries (NBSSI) that defines small businesses as enterprises with at most nine (9) employees with non-current assets not exceeding GHS 10,000.00.

Scholars have argued that the role played by small businesses cannot be over-emphasized (Snodgrass & Winkler, 2004; Asiedu & Agyei-Mensah, 2008; Okpukpara, 2009; Abor & Quartey, 2010). According to Asiedu and Agyei-Mensah (2008), small businesses contribute significantly to the economic growth, job creation, social cohesion, and development of both developed and developing countries. Poverty minimization is an important role played by small businesses in developing countries (Snodgrass & Winkler, 2004; Abor & Quartey, 2010). Also, in Ghana, 92 percent of businesses are small businesses and they contribute 70 percent to GDP and 80 percent to employment.

However, most small businesses are unable to grow financially due to a lack of credit facilities, inadequate infrastructure, low managerial skills, low technological levels, weak institutional and regulatory framework. In order to have a more vibrant and successful private sector, there should be in place mechanisms that can provide easy credit and other services to small enterprises that cannot be provided by the formal sector (Babajide, 2012). The emergence of microfinance institutions (MFIs) came into being to solve some of these challenges coupled with small businesses. Apart from the credit, MFIs provide other financial services such as

savings, insurance, and educational training to small business owners or associates that the formal financial sector are unwilling to provide. The next section explains the products or services provided by MFI.

2.3 Microfinance Product/Service

2.3.1 Microloan

A microloan is an important aspect of microfinance and it has been described as the premise of microfinance institutions (Alhassan, Hoedoafia & Braima, 2016). These are the funds that are given to small enterprises or individual business owners over a period. It should be noted that the terms microloan and microcredit are used interchangeably by MFIs and consider these as a subset of microfinance. The size of the loan depends on the individual/business character and savings habit. Buyske (2004) asserted that microcredit is between $300 and $1000.

Christen, Lyman, and Rosenberg (2003) postulated that the only upper limit of the size of loans depends on the borrower's character and its cash flows. Ledgerwood argues that MFIs must consider the cash flows of an individual before they are given loans. The loans are granted through microfinance interventions that are used for varying purposes, and in most cases, the loans are used for investment and wealth generations. The provision of microcredit to small businesses helps them meet their basic necessities, reduce risks and improve household economic welfare that increases entrepreneurs or owner's operational growth in terms of profit, sales, and returns on the asset.

2.3.2 Micro Savings

Micro savings includes part of business incomes given to micro- financial institutions or bankers on a daily, weekly, or monthly basis that are accumulated to the bank account. In Ghana, the term "Susu" is predominantly used to refer to micro- savings. Wenner, Alvarado, and Galarza (2003) argue that there is a need for savings facilities for small businesses in emerging economies particularly those in rural communities to save part of their income for future investment. Most emerging economies with some commercial banks have the mandate to mobilize micro-savings, however, they have not fully entered rural markets and the informal sector. The microfinance institutions take care of the micro-savings needs of the small businesses in the rural and informal market to help save, invest and grow their businesses. Also, this service provided by MFIs helps to improve the poor household finance and protects low-income economic agents to accumulate worth for some period that can be used in profitable investment or other important purposes.

2.3.3 Micro Insurance

According to Oscar and Abor (2013), this type of product is very key since it insured microfinance client's activities. Mathur (2010) defines microinsurance as a low-value product that requires different design and distribution schemes like the premium that is based on community risk rate. Microfinance institutions integrate insurance with client's credit and savings activity so that it reduces credit risk on loans (Oscar & Abor, 2013). Micro-insurance

covers life, health, property or agricultural products, and other valuable items of business owners. The services of micro insurance reduce poor and help mitigate risks. The low-income clients buy insurance products to safeguard their assets against theft and fire and also protect them against accidents and ill health. It is usually the poor who suffer the most in the event of misfortune. Micro-insurance enables the poor and low-income earners to insure their assets and operations against any disaster, and also helps small businesses to safeguard the resources that enable them to manage risks and avoid debts.

2.3.4 Education

Microfinance also provides non-financial educational services or professional training to help assist, and improve the activities of small businesses through efficient utilization of resources, inventory management, and other basic accounting methods. Microfinance education usually takes a maximum of 30 minutes in relevant areas to enhance and empower entrepreneur's literacy. Accounting or financial literacy can help business owners or managers to make sound and objective decisions on finance that can help grow their businesses (Sarpong-Danquah, Gyimah, Poku & Osei-Poku, 2018). Usually, most of the microfinance educational services are tailored towards the utilization of microcredit and other social services which are aimed at improving the working capital and the social lives of the beneficiaries to increase productivity (Dunford, 2001). For instance, credit with microfinance education strategy given by Freedom from Hunger Worldwide bring self-help solutions to the fight against poverty, and this was launched in West Africa in 1988. The credit with microfinance education is usually organized weekly or monthly basis to evaluate the individual businesses and also serves as a repayment period of loans. Some solutions are recommended by MFIs to the challenges faced by small businesses through microfinance educational training and workshops.

2.4 Empirical Review

Some researchers have investigated the effects of MFIs products on the growth of small businesses with divergent outcomes. For instance, Thio (2006) investigated the impact of MFIs on the growth of small businesses and the result indicates that microfinance products or services have a positive impact on sales of small enterprises. The result also shows that loan has a negative impact to the performance of small enterprises. However, research conducted by Kisaka and Mwewu (2014) on the effects of MFIs on small businesses in Kenya indicates that microloans and micro-savings positively affect the growth of small firms. Meanwhile, educational training was not statistically significant.

Appiah, Turkson, and Hagan (2009) investigated the role of MFIs from the perspective of small and medium enterprises (SMEs) using empirical data from Ghana among 66 SMEs. From the study, they establish that there is a positive impact of MFIs on poverty reduction, and specifically 85 percent of SMEs admitted that they can access certain facilities from MFIs.

Fauster (2014) researched to find out the effects of MFIs on SMEs in Wa Metropolis. The study reviews that microfinance positively affect the sale revenue of small businesses and

Awuah and Addaney (2016) also researched Multi Credit Savings and Loans Limited products on the performance of SMEs using Sunyani Metropolis as a case study in Ghana. Their study also confirms prior studies in Ghana which conclude that the effect of microfinance on SMEs positively affects the performance such as revenue, profit, and assets turnover due to the patronage of MFIs services.

This current study examines whether the combination of microfinance products or services in terms of microloans, micro-savings, micro-insurance, and education affects positively the growth of small businesses in an emerging economy, Ghana where there is no prior study.

3. Methodology

The study is a descriptive survey that uses quantitative analysis to examine the nexus between microfinance and small business growth in Ghana. The study uses primary data and employs a structured questionnaire to obtained favourable and accurate responses from the entrepreneurs or small business owners in Ghana. Due to unavailable data on registered small businesses in Ghana, the researchers employ purposive sampling to distribute 500 questionnaires across the country. However, only 248 responded to the questionnaires representing a 49.6% response rate.

The questionnaire instrument uses five points Likert scale format and uses indicators strongly agree (a score of 5 points) to strongly disagree (a score of 1 point). We coded and entered the retrieved responses in Microsoft excel according to each responded item of the questionnaire. The coded responses are imported to SPSS 21 to analyze data. Descriptive statistics in the form of standard deviation and mean are used to analyze the product provided by MFIs and small business growth.

The study tests the correlation among the variables, ANOVA, and uses a multiple linear regression model for the available data. The multiple regression model is to examine microfinance effects on the growth of SMEs in Ghana. The model is presented as:

$$GWTH = \alpha + \beta_1 MLOAN + \beta_2 MSAVI + \beta_3 MINSU + \beta_4 MEDUC + e \quad (1)$$

Where:

GWTH = Growth in sales

α = Constant

β = Slope of regression line

MLOAN = Microloan

MSAVI = Microsavings

MINSU = Micro-insurance

MEDUC = Micro education

e = Error term/Stochastic term

The independent variables were measured using the five-point Likert scale from 1 to 5. Finally, the study test 4 hypotheses and they are as follows.

Hypothesis A: Relates to microloans

H_0: Microloan does not have any influence on the growth of small businesses.

H_1: Microloan influences the growth of small businesses.

Hypothesis B: Related to micro-savings

H_0: Micro saving does not influence the growth of small businesses.

H_1: Micro saving influences the growth of small businesses.

Hypothesis C: Related to microinsurance

H_0: Microinsurance does not influence the growth of small businesses.

H_1: Microinsurance influences the growth of small businesses.

Hypothesis D: Related to Micro education

H_0: Micro education does not influence the growth of small businesses.

H_1: Micro education influences the growth of small businesses.

4. Findings

4.1 Descriptive Statistics and Correlations

Table 1 shows the descriptive statistics and correlations among the variables used for the study. From Table 1, microloan (MLOAN) has the highest effect on the growth of business with the highest average score of 4.73 and standard deviation of 0.76. The implication is that the growth of a small business depends mostly on loans. Micro savings (MSAVI) offered by MFIs record an average score of 4.46 and a standard deviation of 0.91. The result also indicates that the savings made by entrepreneurs or business owners help them to accumulate funds that are plough back to business operations or other profitable investments. Microinsurance (MINSU) records the lowest average of 2.38 with a standard deviation of 1.08 indicating that the majority of entrepreneurs or business owners disagree that insurance services provided by MFIs affect their growth. Micro education (MEDUC) records an average score of 3.06 and a standard deviation of 1.03. The result implies that some business owners agree educational services contribute to the success of their business, others assert otherwise.

From Table 1, the correlation result indicates that there is a strong positive correlation between microloans and small business growth due to the high R-value of 0.82 and the correlation is significant ($p < 0.01$). Also, micro education shows a significant ($p < 0.05$) positive correlation with growth at an R-value of 0.72. Moreover, the result shows that there is a high positive significant correlation between micro-savings and small business growth ($p < 0.05$; R-value = 0.64). Finally, micro- insurance shows a weak positive correlation between growth at a low R-value of 0.47, however, the relationship is significant ($p < 0.01$).

The correlation result reviews that microloan, micro-savings, micro-insurances, and micro education have a significant effect on the growth of small businesses because the significant levels are all less than 0.05.

Table 1. Descriptive Statistics and Correlations (N = 248)

	Variables	Mean	S.D.	1	2	3	4	5
1	GWTH	4.67	0.85	1.00				
2	MLOAN	4.73	0.76	.82***	1.00			
				0.000				
3	MSAVI	4.46	0.91	.64**	.32**	1.00		
				0.042	0.017			
4	MINSU	2.38	1.08	.47***	.13**	.17***	1.00	
				0.000	0.014	0.000		
5	MEDUC	3.06	1.03	.72**	.15*	0.12*	.33**	1.00
				0.040	0.092	0.100	0.042	

Significant level: *** $p < 0.01$

** $p < 0.05$

* $p < 0.10$

4.2 Regressions Results

The results in Table 2 shows that the dependent variable (GWTH) has a strong relationship between the independent variables (MSAVI, MLOAN, MINSU, and MEDUC) because the multiple regression r-square value is 0.87. This implies that 87 percent of the variance in the growth of small businesses is explained by independent variables whereas the remaining 13 percent is explained by other variables that are not in the regression model.

From Table 3, the linear regression equation records p-values less than 0.01 ($p = 0.0002$) and this implies that the independent variables are significant in assessing the growth of small businesses in Ghana. From Table 4, using the beta coefficient of the independent variables, the model is:

$$\text{Growth} = -0.090 + 0.321\text{MLOAN} + 0.283\text{MSAVI} + 0.254\text{MINSU} + 0.272\text{MEDUC}$$

Thus, holding all the independent variables constant, the growth of small businesses can decrease 9 percent without the product or services provided by MFIs. However, holding all the independent variables constant, a unit change in microloans leads to a 32.1 percent increase in growth; a unit increase in micro-savings increases growth by 28.3 percent; a unit increase in microinsurance increases growth by 25.4 percent and finally, a unit increase in micro education results to a 27.2 percent increase in growth.

Also, the regression result in Table 4 shows that at significant level ($p < 0.05$), micro loans ($\beta = 0.321$, $p = 0.000$), micro savings ($\beta = 288$, $p = 0.008$), micro education ($\beta = 0.279$, $p = 0.022$) significantly affect small business growth at a confident level of 95 percent ($p < 0.05$). However, micro insurance ($\beta = 0.254$, $p = 0.087$) is significant at 10 percent. This shows that

microinsurance is the least product that affects the growth of small businesses in an emerging economy, Ghana.

Table 2. Model summary

Model	R	R-Square	Adjusted R-Square	Standard Error of the Estimate
1	0.91 (a)	0.87	0.84	0.23

(a) Independent Variables: MLOAN, MSAVI, MINSU, MEDUC, (Constant).

Table 3. ANOVA

Model		Sum of	Squares	Degree of Freedom	Mean Square	F	Significant level
1	Regression	86.22		2	43.11	301.76	0.0002(a)
	Residual	12.28		246	0.049		
	Sum	98.50		248			

(a) Independent Variables: MLOAN, MSAVI, MINSU, MEDUC, (Constant).

Table 4. Coefficients of Independent Variables

Model		Unstandardized Coefficients Beta	Standard Error	Standardized Beta	T	Significant level
1	(Constant)	-0.090	0.007		-12.866	0.003
	MLOAN***	0.321	0.020	0.308	16.048	0.000
	MSAVI***	0.283	0.017	0.441	16.641	0.008
	MINSU*	0.254	0.015	0.290	16.933	0.087
	MEDUC**	0.272	0.016	0.432	17.008	0.022

(a) Independent Variables: MLOAN, MSAVI, MINSU, MEDUC, (Constant).

Dependent Variable: Growth in sales

Significant level: *** $p < 0.01$;

** $p < 0.05$;

* $p < 0.10$.

5. Discussion

From the analysis, microloans report an R-value of 82 percent at significant at 0.01. This shows that it affects the growth of small businesses in Ghana. The regression model result shows a positive significant coefficient ($\beta = 0.321$, $p = 0.000$) for microloans. The finding is consistent with a study done by Fauster (2014) who found that microloans positively contribute to the growth of small enterprises. However, the findings contradict the study done by Thio (2006) who asserts that microloans negatively affect the growth of small enterprises.

Also, micro-savings report an R-value of 64 percent at 0.05 significant level, and the model result gives a significant positive coefficient ($\beta = 0.283$, $p = 0.008$). This shows that there is a positive

relationship between micro-savings and small business growth. The finding is consistent with Awuah and Addney (2016) who postulate that micro-savings positively affect the growth of small businesses.

Another surprising finding is the low R-value of 47 percent for microinsurance but its p-value is 0.000 ($p < 0.01$). The regression model result shows that microinsurance is not highly significant ($p = 0.087$) as compared to the other variables that recorded a significant level less than 0.05. Thus, at a 10 percent significant level, micro-insurance also affects small business growth in Ghana.

The final product, micro education reports an R-value of 72 percent at 0.05 significant level and the regression model result shows that there is a strong relationship between micro education and small business growth ($\beta = 0.272$, $p = 0.022$). The finding agrees with the results of Fauster's (2014) study that found that micro education has a positive effect on small business growth. However, the result disagrees with Kisaka and Mwewu's (2014) study that found that micro education or training services provided by MFIs do not have any significant effect on small enterprises in Kenya.

6. Conclusion

The purpose of the study is to find out the effect of microfinance products or services on small businesses in an emerging economy, Ghana. The result indicates that at a 1 percent significant level, microloans increase the growth of small businesses in Ghana since we recorded p-values less than 0.01. Therefore, the study rejects the null hypothesis (H_0) that micro-savings have no significant effect on small business growth. The study also rejects the null hypothesis ((H_0) for micro-savings and micro education that report a p-value less than 0.05. Micro-insurance reports a p-value of 0.087 ($0.10 < p > 0.05$), indicating that at 90 percent confidence level, the null hypothesis (H_3) for microinsurance is rejected, and conclude that there is a partial positive correlation between micro-insurance and small business growth in Ghana.

In conclusion, the MFIs products or services affect the growth of small businesses in Ghana, and the greatest influence product is microloans due to high R-value of 82 percent and significant p-value less than 0.01 ($p = 0.000$). This is followed by micro education with a high R-value of 72 percent and the coefficient in the regression model is significant at 0.05 ($p = 0.022$). Micro savings follow with an R-value of 64 percent significant at 0.01. Micro-insurance is the least influence on the growth of small businesses with a low R-value of 47 percent. Thus, the study recommends that MFIs should increase the insurance services to entrepreneurs to have confidence for some assurance of funds in case of any occurrence of operational misfortune. This can also increase the saving rate of business owners for the benefit of MFI's growth. Also, MFIs should continue to provide educational or entrepreneurial training regularly that can gear toward the growth and profitability of small businesses in emerging economies. Finally, MFIs should increase their asset credits or loans duration and spread loan reimbursement over long periods to enable businesses owners to have greater use of credit over a long period for the acquisition of capital assets and technology that can help them grow.

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