A STUDY OF FINANCE OPTIONS FOR SME'S IN GHANA: THE CASE OF SAVINGS AND LOANS COMPANIES IN THE ASHANTI REGION OF GHANA,

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STATEMENT OF AUTHENTICITY

We have read the university regulations relating to plagiarism and certify that this report is all our own work and does not contain any unacknowledged work from any other source. We also declare that we have been under supervision for this report herein submitted.

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ABSTRACT

The study analysed the financial options for small and medium scale enterprises in Ashanti Region. It specifically identified the role of the non-banking financial institutions as an alternative means for finance for SMEs in Ashanti Region as a whole. It also determine the source of finance for SMEs in Ashanti Region, examine the type of products of the savings and loans companies in Ghana, the challenges that are faced by SMEs and how to improve the lending of money to SMEs by the savings and loans companies.

The survey revealed that SMEs have very limited access to deposit and credit facilities provided by formal financial institutions. A purposive sampling was administered, to seventy five (75) respondents in the study of which sixty seven (67) were fully answered.

The data was analysed and presented in the form of tables and charts. The study revealed that most of the SMEs in the Ashanti Region are dominated by people in their youth age. This was due to the fact that majority of the respondent, that is about 68% were in their youthful age, which is between eighteen to forty years (18-40), and 25% were ranged between 41-50 years and only 7% were above 50 years.

Based on the results obtained in this study, it is recommend that savings and loans companies should make their products relatively flexible to SMEs and there must be other sources of credit to SMEs where collateral security will not be a major demand or challenge to SMEs.

DEDICATION

This piece of work is dedicated to God Almighty for the grace and strength given to us to complete this work, irrespective of the limitations on our part.

Next, we dedicate it to all our families for their support both financially and emotionally.

Also, we dedicate it to all lecturers and friends who made it possible for us to get this far.

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CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

Small and medium-sized enterprises (SMEs) are the backbone of economies in advanced industrialized countries, as well as emerging and developing countries, as they are a key source of economic growth, innovativeness, and poverty reduction. SMEs constitute the dominant form of business organization, accounting for over 95% and up to 99% of enterprises depending on the country (Taddesse, 2010). Small and medium sized enterprises in both developing and developed countries play important roles in the process of industrialization and economic growth, by significantly contributing to employment generation, income generation and catalysing development in urban and rural areas. (Hallberg, 200; Olutunla, 2001; OECD, 2004; Williams, 2006). Haggblade and LIedholm (1991) affirm that Africa and Asia has the majority of their population living in rural areas where small scale enterprises delivers about 20% - 45% of full-time employment and 30% - 50% of rural household income. Latin America, which is more urbanized, has an estimated 50 million micro and small scale enterprises, employing 120 million people (Berger and Guillamon 1996). In Sub-Sahara Africa, the SME sector accounts for over 90% of all enterprises of which 70% - 80% are micro and very small enterprises.

In spite of the significant role SMEs play in socio-economic development of developing countries in general and Ghana specifically, the sector continues to be plagued with a myriad of challenges such unstable government policies, gross under capitalization, high operating costs, lack of clear cut government support and assistance, and difficulty in assessing credit from financial institutions and banks (Aryeteey, 2008). The one most pervasive and predominant challenge which confront SMEs and hinder majority of entrepreneurs from success is the finance factor (UNCTAD, 1995, 2001; SBA, 200). Having access to finance gives SMEs the chance to develop their business and to acquire better technologies for production, therefore ensuring their competiveness. However, there is a huge challenge for SMEs globally when it comes to sourcing for initial and expansion capital funds from traditional commercial banks. The situation is even dire in developing countries and in Ghana in particular where, access to and cost of credit is so prohibitive.

The formal financial sector of the economy constitutes the most reliable source of credit for most SMEs in the advanced countries and some emerging economies in the Far East, than it is for Africa. Even though SMEs account for a large share of enterprises and represents potential employments and economic growth in emerging economies of Africa, they receive a very low share of credit from the formal financial sector. Indeed, most of them are denied access to formal financial markets. The reasons for this scenario are not far-fetched. In Ghana the formal financial institutions led by the commercial banks and other traditional sources of credit have always considered SMEs as a greater risk than larger companies, and respond by adopting anti-risk measures like charging higher interest rates or demanding landed collateral security. This makes it more and more difficult or almost impossible for many SMEs to effectively borrow from banks where the price of credit is too high. If entrepreneurs cannot gain access to finance through the regular system or more 'bigger' banks, they may find it extremely difficult to start up a business or may simply go out of business, which represents a potential loss to the economy. The alternative left for such entrepreneurs may be to abandoned the formal system altogether and operate in the informal economy, and in the process possibly evade taxes and regulations, and thus not making a full contribution to economic growth and job creation. SMEs would therefore have no choice but turn to other sources of credit to finance their business.

1.2 Statement ofthe Problem

Ghana’s economy, like all other developing economies, is dominated by a large proportion of business in the small-scale and self-employed group. These businesses need reliable sources of funds which have not been met by the commercial banks in the formal sector. The emergence and proliferation of several other financial institutions in the formal and informal sector offers opportunities for SME entrepreneurs to address the age old financing battle. These institutions made up of credit unions, financial NGO’s, cooperatives, savings and loans companies, leasing companies, micro-finance and susu companies are potentially good sources of credit for the teeming SMEs who are under served by the ‘big banks’. The questions that comes to mind is whether these institutions have the capacity, resources and scope to serve the huge demand for credit or finance from the SMEs. From the institutions listed, the savings and loans company constitute a potentially major source of finding given their scope, mandate, core functions and their coverage across the country. The focus of this study would specifically be on the savings and loans companies and how they can be relied upon as an alternative source of financing for SME businesses in Ghana. The issue at stake now is whether the savings and loans company are indeed reliable source of funds? What products and services do they offer to potential clients? Do these Savings and Loans Companies have SME lending policies? And if they do, to what extent the policies enhance or improve lending to SME clients. What challenges do SME face in accessing credit from the Savings and Loans Companies? This study would attempt to address some of these questions from the perspective of SME operators and the financial institutions as well.

1.3 Research Objectives

The general objective of this study is to determine whether savings and loans companies can serve as an alternative source of formal finance for small and medium enterprises in the Ashanti Region. The specific objectives of the study include:

i. To determine the sources of finance of the SMEs in the Ashanti Region.

ii. To examine the type of products and services of savings and loans companies in Ashanti Region.

iii. To assess the challenges of SME in lending practices by the Savings and Loans Companies.

iv. To make recommendations on improving lending to SMEs by Savings and Loans Companies.

1.4 Research Questions

This study seeks to address the following questions:

i. What are the sources of finance of the SMEs in the Ashanti Region?

ii. What type of products and services do the Savings and Loans Companies in Ashanti Region offer?

iii. What are the challenges of SMEs in accessing lending by Savings and Loans Companies?

iv. Are there recommendations on improving lending by Savings and Loans Companies to SMEs?

1.5 Significance of the Study

It is undeniable fact that SMEs play a major role in the socio-economic development of the country in promoting economic growth and poverty reduction. Extensive research has been carried out in this area of SME financing because of the peculiar role they play in the economy. Accessing financing through the informal or formal sector has always been a challenge for most SME operators. In the light of the difficulties encountered by entrepreneurs in obtaining credits from especially the commercial banks as indicated by several studies, it would be interesting to investigate how the recent upsurge in financial intermediaries in Ghana; particularly the non-bank financial institutions have served as an alternative source of funding for SME business operations and to what extent they have helped bridged the financing gap for many SMEs. The study is important as it is going to provide valuable information for the consumption and use of SME operators, commercial banks and NBFIs, academia and policy makers. It will also enlighten the public in general and SMEs and banks in particular on whether the NBFIs are truly bridging the financing gab as an alternative to the commercial banks in the Ashanti Region. Although, the study may relate to the Ashanti Region, other regions and cities or urban and rural areas would find the results of the study equally useful in respective operations and for their consumption.

1.6 Limitations of the Study

This study examined the role of Savings and Loans Companies as an alternative or financing option for small and medium enterprises in the Ashanti Region. The researchers were hard pressed with time, resources and funds and as a result only a representative sample of Savings and Loans Companies as well as SME operators was used in obtaining general information. Secondly, the research was limited to Ashanti Region which represents a good sample frame of the SME clients in the Ashanti Region and for Ghana. Some of the problems encountered in data collections were the inability of the respondents to complete or provide full information on some questions posed, especially the few opened ended questions. The low level of literacy among some respondents might have accounted for this trend and thus made the administration of the questionnaire time consuming. The Savings and Loans Companies were unwilling to give out details of statistics and data on performance of their products.

1.7 Organization of the Study

The study is presented in five chapters:

Chapter 1 shows briefly, background and general introduction to the study, the problem statement, objectives and the questions of the study. Chapter 2 takes a look at the theoretical framework and review of literature relevant to objectives and topic of the study, particularly the financial sector in Ghana. The role and the importance of SMEs in Ghana's economy, the formal financial sector of the Ghanaian economy, the role of Savings and Loans Companies, and the issues of financing gap in SME financing.Chapter 3 gives an explanation of the research process and the methodology employed for collecting and analysing data.Chapter 4 deals with analyses and discussion of the data and a presentation of research findings. Chapter 5 presents a summary as well as conclusions and recommendations of the study.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

Small enterprises and most the poor population in sub-Saharan Africa have very limited access to deposit and credit facilities and other financial services provided by formal financial institutions. For example, in Ghana and Tanzania, only about 5-6% of the population has access to the banking sector (Basu et al 2004). Banks are generally reluctant to give credit, especially to those starting a business without proper collateral. Small businesses are being denied credit due to insufficient guarantee or perceived risks. The cost of handling microcredit and the perceived risks associated with them make such poor entrepreneurs 'unbankable' and thus of no interest to the traditional banks (Council, 2002). According to the 2000 Population and Housing Census in Ghana, 80% of the working population is found in the primary informal sector. This group characterized by lack of access to credit, which constrains the development and growth of that sector of the economy. Clearly, access to financial services is imperative for the development of the informal sector and also helps to mop up excess liquidity through savings that can be made available as investment capital for national development (World Bank, 1999). The goal of attaining economic development in many more countries around the world is unlikely to be realized while 1.7 billion working adults make less than US$2 a day and have little or no access to basic financial services. According to Firpo, (2005) the history of financial systems in the United States has shown that providing citizens with capital and the ability to save are key underpinnings of economic growth. Yet between 70% and 80% of the world's population has no access to even the most basic financial services.

This lack of access to financial services from the formal financial system is quite striking, when one considers that in many African countries the poor represent the largest share of the population and that the informal sector is an important part of the economy. To meet unsatisfied demand for financial services, a large variety of microfinance institutions (MFI's) has emerged over time in Africa. Some of these institutions concentrate only on providing credit, others are engaged in providing both deposit and credit facilities and some are involved only in deposit collection (Basu et al, 2004).

Traditionally, commercial banks have shunned the microfinance sector, allowing it to be dominated by the 'Alternative Financial Institutions' which consist of small savings and loans companies and susu collectors. The excuse for neglecting the microfinance market is simply that the low-income earners, the main clientele for microfinance service, are not 'bankable' The Consultative Group to Assist the poor (CGAP) has also highlighted the vast potential market for retail financial services to low-income earners. The CGAP reports that as of 2003 there were approximately three billion potential clients worldwide for the microfinance market with only one-sixth of this market being served, mostly by Alternative Financial Institutions. (Boateng, D., 2009). Firpo, (2005) argues that the microfinance industry has proven that the extreme poor are bankable. Not only do they repay loans, but they also do so with very low defaults and relatively high interest rates. Banks and entrepreneurs in developing countries are beginning to realize that there is a viable market for financial products among the vast unbanked populations of the world (Firpo, 2005). According to Appiah, (2008), microfinance has been successful in reaching the poor and helping them gradually escape poverty because of its strong competency in using scare resources to efficiently reach the underserved.

Appiah, (2008) defines microfinance as the provision of financial services and the management of small amount of money through a range of products and a system of intermediary functions that are targeted at low income clients. It includes loans, savings, insurance, transfer services and other financial products and services.

2.2 Meaning and Definition of Small and Medium Scale Enterprise

Different authors have usually given different definitions to this category of business. The most commonly used and now accepted criteria for defining SMEs are the number of employees and the asset value.

The European Commission (EC) defines SMEs largely in term of the number of employees as follows:

- Firms with 0 to 9 employees – micro enterprises;
- 10 to 99 employees – small enterprises;
- 100 to 499 employees – medium enterprises.

Thus, the SME sector is comprised of enterprises (except agriculture, hunting, forestry and fishing) which employ less than 500 workers. In effect, the EC definitions are based solely on employment rather than a multiplicity of criteria. Secondly, the use of 100 employees as the small firm's upper limit is more appropriate, given the increase in productivity over the last two decades (Storey, 1994). Finally, the EC definition did not assume the SME group is homogenous; that is, the definition makes a distinction between micro, small and medium-sized enterprises. Weston and Copeland (1998) hold that definitions of size of enterprises suffer from a lack of universal applicability. In their view, this is because enterprises may be conceived of in varying terms. Size has been defined in different contexts, in terms of the number of employees, annual turnover, industry of enterprise, ownership of enterprise, and value of fixed assets. For example, (Van der Wijst 1989) considers small and medium businesses as privately held firms with 1 – 9 and 10 – 99 people employed, respectively. Jordan et al (1998) define SMEs as firms with fewer than 100 employees and less than €15 million turnover. Michaelas et al (1999) consider small independent private limited companies with fewer than 200 employees and (Lopez and Aybar 2000) considered companies with sales below €15 million as small. According to the British Department of Trade and Industry, the best description of a small firm remains that used by the Bolton Committee in its 1971 Report on Small firms. This stated that a small firm is an independent business, managed by its owner or part-owners and having a small market share (Department of Trade and Industry, 2001).

2.2.1 Alternative Definitions

The United Nation Industrial Department Organization (UNIDO) also defines SMEs in terms of number of employees by giving different classifications for industrialized and developing countries (Elaian, 1996). The definition for industrialized countries is given as follows.

- Large – firms with 500 or more workers;
- Medium – firms with 100 – 499 workers;
- Small – firms with 99 or less workers.

The classification given for developing countries is a follows:

- Large – firms with 100 or more workers
- Medium – firms with 20 – 99 workers
- Small – firms with 5 – 19 workers
- Micro – firms with less than 5 works

It is clear from the various definitions that there is not a general concerncious over what constitutes and SME. Definitions vary across industries and also across countries. It is important now to examine definitions of SMEs given in the context of Ghana.

2.2.2 The Ghanaian Situation

There have been various definitions given for small scale enterprises in Ghana but the most commonly used criterion is the number of employees of the enterprise (Kayanula and Quartey, 2000). In applying this definition, confusion often arises in respect of the arbitrariness and cut off points used by the various official sources. In its industrial statistics, the Ghana Statistical Service (GSS) considers firms with fewer than 10 employees as small scale enterprises and their counterparts with more than 10 employees as medium and large size enterprises. Ironically, the GSS in its national accounts considered companies with up to 9 employees as SMEs (Kayanula and Quartey, 2000).

The value of fixed assets in the firm has also been used as an alternative criterion for defining SMEs. However, the National Board for Small Scale Industries (NBSSI) in Ghana applies both the International Research Journal of Finance and Economics – Issue 39 (2010) 221 "fixed asset and number of employees" criteria. It defines a small scale enterprise as a firm with not more than 9 workers, and has plant and machinery (excluding land, buildings and vehicles) not exceeding 1,000 Ghana Cedis. The Ghana Enterprise Development Commission (GEDC), on the other hand, uses a 1,000 Ghana Cedis upper limit definitions for plant and machinery.

It is important to caution that the process of valuing fixed asset poses a problem. Secondly, the continuous depreciation of the local currency as against major tradition currencies often makes such definitions outdate (Kayanula and Quartey, 2000). In defining small scale enterprises in Ghana (Steel and Webster 1991, Osei et el 1993) used an employment cut off point of 30 employees. (Osei et el 1993), however, classified small scale enterprises into three categories, these are:

(i) Micro – employing less than 6 people;

(ii) Very small – employing 6 to 9 people;

(iii) Small – between 10 and 29 employees.

A more recent definition is the one given by the Regional Project on Enterprise Development Ghana manufacturing survey paper. The survey report classified firms into:

(i) Micro enterprise, less than 5 employees;

(ii) Small enterprise, 5 - 29 employees;

(iii) Medium enterprise, 30 – 99 employees

(iv) Large enterprise, 100 and more employees (see Teal, 2002).

2.3 Features and Characteristics of SMEs in Ghana

SMEs in Ghana can be categorized into urban and rural enterprises. The former can be sub divided into organized and unorganized enterprises; the organized ones tend to have paid employees with a registered office whereas the unorganized category is made up of artisans who work in open spaces, temporary wooden structures, or at home and employ little or in some cases no salaried worker, they rely mostly on family members or apprentices.

Rural enterprises are largely made up of family groups, individual artisans, women engaged in food production from local crops. The major activities within this sector include; manufacturing of soap and mining, making of bricks and cement, beverages, food processing, bakeries, wood furniture, agro processing, chemical based products and mechanism (Liedholm and Mends 1981; Osei et al 199; World Bank 1992, Gray, Cooley and Lutabingwa, 1997). It is interesting to note small scale enterprise make better use of scarce results than large scale enterprise. Research in Ghana and many other countries have shown that capital productivity is often higher in SMEs than is the case with the large scale enterprise (LSEs) (Steel 1977; Child 1971). The reason for this is not difficult to see; SME's are labour intensive with very small amount of capital invested. Thus it has been argued that promoting the SME sector in developing countries will create more employment opportunities, lead to a more equitable distribution of income and will ensure productivity with better technology (Steel and Webster 1991). SMEs howeverhave a crucial role to play in stimulating growth, generating employment and contributing to poverty alleviation, given their economic weight in African countries.

It is estimated approximately 90% of all business units in Ghana are made up of Small and Medium Scale Enterprises (SMEs) who absorb incredibly, 60% of the national work force. SME's also contributes immensely to the gross domestic products to the country. Majority of SMEs are female-owned businesses, which more often than not are home-based compared to those owned by males; they are operated from home and are mostly not considered in official statistics. This clearly affects their chances of gaining access to financing schemes, since such programmes are designed without sufficient consideration of the needs of businesses owned by females. These female entrepreneurs often get the impression that they are not capable of taking advantage of these credit schemes, because the administrative cost associated with the schemes often outweighs the benefits. Prior empirical studies in Ghana have shown that female-owned SMEs often have difficulty assessing finance. Females are mostly involved in sole-proprietorship businesses which are mainly micro enterprises and as such may lack the necessary collateral to qualify for loans (Aryeetey et al, 1994; Abor and Biekpe, 2006).

Measures of enterprise efficiency (e.g. labour productivity or total factor productivity) vary greatly both within and across industry. Firm size may be associated with some other factors that are correlated with efficiency, such as managerial skill and technology, and the effects of the policy environment. Most studies in developing countries indicate that the smallest firms are the least efficient, and there is some evidence that both small and large firms are relatively inefficient compared to medium-scale enterprises (Little et al, 1987). It is often argued that small firms bring innovations to the market place, but the contribution of innovations to productivity often takes times, and large firms may have more resources to adopt and implement them (Acs et el, 1999).

2.4 Importance and Significance of SMEs

Small and medium enterprises contribute greatly to the social and economic development of Ghana. Amongst the several benefits that SMEs bring to the national economy in general society as a whole are the following:

- SMEs have been recognized as the engines through which the growth objectives of developing countries can be achieved. They are potential sources of employment and income in many developing countries, (OECD, 1997). In Ghana they employ an estimated 70-80% of the active labour force, and close to 99% in the rural agricultural sector.
- SME's seem to have advantages over their large-scale competitors in that they are able to adapt more easily to market conditions, given their broadly skilled technologies. They are able to withstand adverse economic conditions because of their flexible nature.
- They also improve the efficiency of domestic markets and make productive use of scarce resource, thus facilitating long-term economic growth (Kayanula and Quartey, 2000).
- SME's are more labour intensive than larger firms and therefore have lower capital cost associated with job creation.

- SME’s contribute to a national product by either manufacturing goods of value, or through the provision of services to both consumers and/or other enterprises. This encompasses the provision of products and, to a lesser extent, services to foreign clients, thereby contributing to overall export performance.
- SME’s provide job opportunities for the people especially the youth within the area in which they operate and therefore minimize social and upheavals and unrest especially among the youth.
- SME’s are likely to succeed in smaller urban centres and rural areas. This helps to slow the flow of migration to large cities.

The finance needs of a start-up should take account of these key areas:

- Set-up costs (the costs are incurred before the business starts to trade)
- Starting investment in capacity (the fixed assets that the business needs before it can begin to trade)
- Working capital (the stocks needed by the business – e.g. raw material + allowance for amounts that will be owed by customers once sales begin)
- Growth and development (e.g. extra investment in capacity)

2.5 Sources Finance for Small and Medium Enterprises

One way of categorizing the sources of finance for a start-up is to divide them into sources which are from within the business (internal) and from outside providers (external).

2.5.1 Internal Sources of Funds

The main internal sources of finance for a start-up are as follows:

Personal Sources – These are the most important source of finance for a start-up. This can be personal savings or other cash balances that have been accumulated. It can be personal debt facilities which are made available to the business. In particular savings and other “nest-eggs are a form of savings where entrepreneurs will often invest personal cash balances into a start-up. This is a cheap form of finance and it is readily available. Often the decision to start a business is prompted by a change in the personal circumstance of the entrepreneurs – e.g. redundancy or an inheritance. Investing personal savings maximizes the control the entrepreneurs keep over the business. It is also strong signal of commitment to outside investors or providers of finance. Re-mortgaging is the most popular way of raising loan related capital for a start-up. The way this works is simple. The entrepreneurs take out a second or large mortgage on private property then invest some or all of this money into the business. The use of mortgaging like this provides access to relatively low-cost finance, although the risk is that, if the business fails, then the property will be lost too.

Borrowing from Family and Friends - Friends and family who are supportive of the business idea provide money either directly to the entrepreneur or into the business.

This can be quicker and cheaper to arrange (certainly compared with a typical or standard bank loan) and the interest and repayment terms may be more flexible than a bank loan. However, borrowing in this way can add to the stressed face by the entrepreneur, particularly if the business faces difficulties.

Retained Profits – This is the cash that is generated by the business when it trades profitably – another important source of finance for any business, large or small. For example, a start-up sells the first batch of stock for say GH¢12,000.00 cash which it had bought for GH¢10,000.00. This means that retained profits are GH¢2,000.00 which can be used to finance further expansion to pay for other trading cost and expenses.

Share Capital Invested by the Entrepreneur – the founding entrepreneur may decide to invest in the share capital of a company, founded for the purpose of forming the start-up. This is a common method of financing a start-up. The founder provides all the share capital of the company, retaining 100% control over the business. The entrepreneur may be using a variety of personal sources to invest in shares. Once the investment has been made, it is the company that owns the money provided. The shareholder obtains a return on this investment through dividends (payments out of profits) and/or the value of the business when it is eventually sold.

2.5.2 External Sources of Funds

The commonest form of external funds available to businesses is loan capital or debt. This can take several forms, but the most common are a bank loan or bank overdraft.

A bank loan – provides a longer-term kind of finance or a start-up, with the bank stating the fixed period over which the loan is provided (e.g. 5 years), the rate of interest and the timing and amount of repayments.

The bank will usually require that the start-up provide some security for the loan, although this security normally comes in the form of personal guarantees provided by the entrepreneurs.

Bank loans are good for financing investment in fixed assets and are general at a lower rate of interest than a bank overdraft. However, they do not provide much flexibility. A bank overdraft is a more short term kind of finance which is also widely used by start-up and small businesses. An overdraft is really a loan facility the bank less the business "owe it money" when the bank balance goes below zero, in return for changing a high rate of interest. As a result, an overdraft is flexible source finance in the sense that it is only used when needed. Bank overdrafts are excellent for helping a business handle seasonal fluctuations in cash flow or when the business runs into short term cash flow problems.

Business Angels are the other main kind of external investor in a start-up company. Business angels are professional investors who typical invest several thousands of cash funds. They prefer to invest in businesses with high growth prospects. Angels tend to have made their money by setting up and selling their own business – in other words they have proven entrepreneurial expertise. In addition to their money, angels often make their own skills, experience and contacts available to the company. Getting the backing of an angel can be a significant advantage to a start-up, although the entrepreneur needs to accept a loss of control over the business.

Venture Capital – is a specific kind of share investment that is made by funds managed by professional investors. Venture capitalists rarely invest in genuine start-ups or small businesses (their minimum investment is usually over £1m, often much more). They prefer to invest in businesses which have established themselves. Another term you may hear is "private equity" – this is just another term for venture capital. A start-up is much more likely to receive investment from a business angel than a venture capitalist.

2.6 An Overview of the Financial System in Ghana

The financial system in Ghana falls into three main categories: formal, semi-formal and informal.

Formal Sector Financial Institutions – these are those that are incorporated under the Companies Code 1963 (Act 179), which gives them legal identities as limited liability companies, and subsequently licensed by the Bank of Ghana (BOG) under either the Banking Law 1989 (PNDCL 225) or the Financial Institutions (Non-Banking Law 1993) PNDCL 328) to provide financial services under Bank of Ghana regulation. Most of the banks target urban middle income and high net worth clients. Rural and Community Banks (RCBs) operates as commercial banks under the banking law, except that they cannot undertake foreign exchange operations, their clientele is drawn from their local catchment area, and their minimum capital requirement is significantly lower. Some collaborate with NGOs using micro finance methodologies. Among the nine specified categories of Non Bank Financial Institutions (NBFIs), the Savings and Loans Companies (S&Ls), which are restricted to a limited range of services, are most active in micro and small-scale financial intermediation using microfinance methodologies.

Semi-Formal System – the Non-Governmental Organizations (NGOs) an d the Credit (CUs) are considered to be the semi formal system, in that they are formally registered, but are not licensed by the Bank of Ghana. NGOs are incorporated as companies limited by guarantee (not for profit) under the Companies Code. Their poverty focus leads them to relatively deep penetration to poor clients using microfinance methodologies, though mostly on a limited scale. They are not licensed to take deposits from the public and hence have to use external (usually donor) funds for micro credit. Credit Unions are registered by the Department of Cooperatives as cooperative thrift societies that can accept deposits from and give loan to their members only. Although credit unions are included in the NBFI Law BoG has allowed the apex body Ghana Cooperative Credit Union Association to continue to regulate the societies pending the introduction of a new Credit Union Law.

Informal Financial System – the informal financial system covers a range of activities known as susu, including individual savings collectors, rotating savings and credit associations, and savings and credit "clubs" run by an operator. It also includes money lenders, trade creditors, self-help groups, and personal loans from friends and relatives. Money lenders are supposed to be licensed by the police under Money Lenders Ordinance 1957.

The commercial banking system, which is dominated by a few major banks, reaches only about 5% households, most of which are excluded by high minimum deposit requirements. With 60% of the money supply outside the commercial banking system, the rural banks, savings and loans companies, and the semi-formal and informal financial systems play a particularly important role in Ghana's private sector development and poverty reduction strategies. The assets of RCBs are nearly 4% of those of the commercial banking systems, with S &Ls and CUs adding another 2%.

2.7 Financial Sector Reforms in Ghana

Financial Sector Reform in Ghana came as a package with the Economic Recovery Programme (ERP) which was introduced in the country primarily to get the wheels of the economy back on track. This programme was implemented because the economy of Ghana has not been performing to expectation. According to (Owusu T. 1993), the implementation of the Financial Sector Adjustment Programme (FINSAP), under the Economic Recovery Programme (ERP) was aimed at strengthening the overall financial system, including the informal non-bank sector in Ghana. In the late 1980's quite a number of Susu and finance companies sprang up and their objective was to mobilize savings ostensibly for on-lending to their customers. Owusu(1993) states that the generous credit overtures made by these companies enthused many petty traders, mostly women, to make colossal deposits with them. However, it turned out that the companies had fraudulent intentions and the millions of cedis mobilized were misappropriated by the owners and the employees without any recourse to redress by depositors.

In an effort to instill sanity into the system, the Bank of Ghana took steps in 1990 to license the Susu/Finance companies under the classified name of Savings and Loans Companies. The effort being made to regulate and modernize/institutionalize the traditional/informal savings societies is aimed to achieve higher growth in mobilization of savings for supporting economic ventures as a complement to the improvement in the formal banking sector (Owusu, 1993). A new law, PNDCL 328 known as Financial Institution (Non-Banking) Law as to regulate the Non-Bank financial institutions. The non-bank financial institutions, under which the subject of this study falls, form an integral part of the financial system and the fact that they were registered under a different law does not detract from their importance. The distinction is only a means to identify these institutions. The difference lies in the fact that these institutions cannot create money like the banks do (Atta-Bronyah, 1995). The advent of Savings and Loans Companies and their rapid growth followed the passage in 1993 of the Financial Institutions (Non-Banking) law. The Savings and Loans Companies are restricted to a range of services and are most active in micro finance and small scale intermediation using various micro finance methodologies. Savings and Loans Companies are most effective in reaching large numbers of savers due in part to their location in urban and peri-urban area. The Non-Bank Financial Institutions were required to be licensed by the Bank of Ghana to operate as such. A license so issued could be revoked or suspended if the non-bank financial institution.

- Obtained it by fraud or mistake;
- Contravenes any provision of the law or any terms or conditions upon the license is granted;
- Engages in undesirable methods of conducting the business in respect of which the license is issued; or
- Fails to maintain the minimum paid up capital (PNDCL 328)

Savings and Loan associations, building societies and mutual savings banks are also classified as thrift institution. Johnson, (1993) defines a thrift institution as a financial institution that encourages moderate-income workers to save money on a regular basis. Likewise the institution invests in loans to these savers, especially mortgage loans.

2.8 Types of Formal Financial Institutions in Ghana

A financial institution is an institution whose assets are financial assets or financial claims-stocks, bonds and facilitating the accumulation and allocation of capital by channelling individual savings into loans to government and business. The transactions of financial institutions consistof making loans to customers and the purchase of investment securities in the market place. Financial institutions also offer a wide variety of other financial services ranging from insurance protection to the sale of retirement plans and the provision of a mechanism for making payments, transferring funds and storing financial information.

The types of financial institutions we have in Ghana are:

(i) Depository Institutions

(ii) Commercial Banks

(iii) Merchant Banks

(iv) Savings and Loan Companies

(v) Credit Unions

(vi) Non Depository Institutions

(vii) Life Insurance

(viii) Pension Funds

(ix) Mutual Funds

(x) Leasing

(xi) Investment Bankers and Brokerage Companies

Depository institutions raise funds by accepting deposits in the form of current, savings and fixed deposit accounts from households and businesses. Non-depository institutions raise funds either from other financial institutions or by selling securities in the financial markets.

2.9 Origins of Formal Banking in Ghana

Formal banking began in Ghana (then Gold Coast Colony) in 1896 with a branch of the Bank of British West Africa (Fry 1976) followed by Barclays Banks in 1917 (Crossley and Blandford, 1975). Both banks were operated and supervised as branches of their London head officers. The first indigenous bank was the Gold Coast Cooperative Bank, which was established in 1945. Its main business was to support the marketing societies to buy cocoa from the farmers. Its registration was cancelled in 1961 and its operation absorbs into the Ghana Commercial Bank (Republic of Ghana 1970). In 1953, the Bank of Gold Coast was established by statute as the first indigenous commercial with some central bank functions. In 1957, the central bank functions and the commercial bank functions were separated between the bank of Ghana and the Ghana Commercial Bank respectively (Steel and Andah, 2003). At the time of independence, the banking industry in Ghana consisted of three (3) banks. The industry has grown over the years. As at 31 December 2007, there were twenty three (23) banks, one hundred and twenty six (126)

Rural and Community Banks and forty one (41) Non-Bank Financial Institutions, including fourteen (14) Savings and Loans Companies (Bank of Ghana, 2007).

The first formal micro finance institutions in Ghana arose out of the micro savings products of the post office system. The institutions ware upgraded to the post office savings banks under the Savings Bank Act 1962 (Act 129), to operate independently within the post office system. It attained full bank status as National Savings and Credit Bank in 1972 under National Redemption Council (NRC) Decree 38. The new management abandoned the use of the network of the post office system and developed its own, leading to the destruction of the micro savings products (Anim, 2000).

Long before reforms, government and sub Saharan Africa attempted to diversify the institutional structure of the formal financial system. They establish specialized bankingandnon-banking institutions. According to Ayeetey (2008) central bank were challenged to create commercial banks, merchant banks, development financial institutions and a number of non-banking and specialized finance institutions, including insurance institutions and provident funds. For their lending operations, banks have always beencharacterize by relatively high value and longer duration loans which require formal institution that government created and yet they failed to solve the problem of the huge financing gap. Aryeetey, (2008) states that the difficulty of trying to reach small borrowers with large formal institutions, among others, led to poor banking practices that eventually weakened many banks and made reforms necessary. He further argues that in contrast, individual savings collectors known all over West Africa made advances to their regular clients. These advances were usually low value, very short term (less than one month), provided interest free and disbursed immediately. Many analysts were of the view that combing the banks’ capital with the intrinsic advantages of the informal agents could result in solving the financial gap problem (Aryeetey, 2008).

2.10 Savings and Loan Companies

Savings and loans companies (S &Ls) are deposit-taking financial institutions regulated by the Bank of Ghana under the Non-Bank Financial Institution (NBFI) Law 1993 (PNDCL 328), with a minimum capital requirement much lower than that of the universal banks but above that for rural and community banks.

The advent of the NBFI Law has given rise to a rapid growth and transformation of some Financial Non-Governmental Organizations (FNGOs) into savings and loans companies operating in urban and peri-urban areas in the country. They serve mostly the economic active informal unbanked population ns and offer tailored products to suit this category of the population. They are restricted to a limited range of financial services compared to universal banks, mostly mobilizing deposit, provision of credit to low income clients and SMEs, money transfers and financial literacy. They utilize microfinance methodologies to serve most of the clients in the peri-urban areas with an average loan size higher than the other category of microfinance institutions. Savings and Loans companies have seen some tremendous injection of foreign capital and benefited immensely from technical assistance from institutional investors. This has boosted operations and increased their competitiveness.

Initial licensing of the new S & L category was difficult and long-delays, as the BOG grappled with how to implement the new law. The required minimum capital (GH¢100 million or US$150,000) initially posed a hurdle, but its real value was eroded by rapid inflation, and the number of S &Ls grew from three in 1995 to seven by 1998. Mum capital requirement in 1998 and 200By 2002 the eight S &Ls had over 160,000 depositors and 10,000 borrowers. Increases in the minimum capital requirement in 1998 and 2000 restored the dollar value through a ten-fold increase in the nominal value, which stalled the rate of new entry. As of June 1999, all of the five outstanding applications for S & L licenses lacked adequate capital to comply with the increase minimum which was raised further in 2001 to about US$2 million.

Nevertheless, the Savings and Loans category has proven to be a flexible means of regularizing three types of MFIs through:

- Transformation of NGOs into licensed financial intermediaries;
- Formalization of actual or potential informal money – lending operations;
- Establishment of small private banking operations serving a market niche

The first license as an S & L went to Women's World Banking Ghana (WWBG) in 1994, representing the first transformation of an NGO into a licensed financial institution. Its success, however, was limited by different views of its mission and commercial orientation between its Board and management and by its failure to establish a high-performing, growing loan portfolio, and it is likely to have difficult complying with the minimum capital and prudential requirementestablished in 2001. EMPRETEC, an NGO providing training for micro and small scale businesses, is also trying to meet the paid-up capital requirement for an S & L. Some of the S &Ls that have become licensed fall into a category that might be termed potential moneylender who wishes to enter the formal financial system to be able to mobilize savings as an additional source of funds. The principle promoters or shareholders of such S &Ls are entrepreneurs with little experience in financial services but who have surplus funds and high motivation. Among the S &Ls, First Allied has become one of Ghana's largest RMFIs, reaching 51,049 depositors with GH¢25.5 billion (US$3.4 million) and 2,820 borrowers with a total loan portfolio of GH¢10.3 billion (US$1.4 million) in 2001, although it serves only the local market around Kumasi, the second largest city in Ghana.

The S & L category has also made possible the entry of private investment to serve a particular market niche on a smaller scale than would be required for a commercial bank. The first in this category was Citi S & L, established in 1994 on commercial banking principles but based in local markets with traders and susu collectors as the main depositors. While Citi was an innovator in its linkages with susu collectors and especially susu clubs, its financial performance has been constrained by earlier problems with its loan portfolio. It represents both an interesting success in applying commercial principles to microfinance and innovating in commercial-informal financial linkages; and a challenge to the supervisory authorities in applying the regulatory guidelines to ensure discipline as well as innovation.

The advantage of having a regulatory niche suitable for specialized MFIs is also apparent in the establishment of Sikaman S & L Company Ltd., promoted by InternationaleProjekt Consult of Germany, which is designed to apply international best practices in microfinance to reach profitable operation in less than two years. Sikaman began operations in 2002 with a staff of 24 as the only S & L whose shareholders are entirely corporate bodies (all but one foreign).

The increased paid-up capital requirement diluted the local ownership from 30% to 2.5% when one local partner institution dropped out and the other could not raise the additional funds. Sikaman later became known as Pro Credit Savings and Loans Company.

2.11 Products and Practices of Savings and Loans Companies

Savings and Loans Companies like most formal final institutions in Ghana are mandated by BoG to deal in specific products and services and are regulated by law to comply in that respect. The commonest products offered include deposits taking – namely current accounts, ordinary savings, fixed deposits accounts, group or susu savings, micro-finance savings. Some also provide local and international money transfer for clients and non-clients. Credit and loan products include personal loans, payroll loans, commercial loans, SME loans, agriculture loans, and micro-finance or group loan. Savings and Loans generally use the loan products described above under RCBs. For example, First Allied S & L uses a group and individual savings with credit scheme with exist, registered occupation-based groups such as butchers, kente weavers, carpenters, and other association (Chord 2000). S &Ls have also been leaders in innovating. Citi S & L uses Susu clubs or any other economic association for their group loan product, with joint group guarantee and savings bank balance up to 5% of loan amount. It has pioneered linkages with susu collectors as well as clubs, including through other forms of individual loan products. Citi also has a micro-leasing product available to clients with at least two successful loan terms (Anin 2000).

2.12 Operations of Savings and Loans Companies in Ghana

Aryeetey, (2008) state that long before reforms, governments in sub-Saharan Africa attempted to deal with the problem. One outcome of reforms is the graduation of Savings and Loans Associations from informal organizations to formal financial institutions, yet retaining most of the characteristics of the former. The mode of operations of savings and loans companies appears to be modelled largely along the lines of the Susu system. Susu is said to have originated in Nigeria and spread to Ghana from the early 1900s. In the market places of West Africa, individual 'mobile bankers' help traders and others accumulate savings through small daily deposits. A market woman in Ghana typically sees her 'bankers' help traders and others accumulate savings through small daily deposits. A market woman in Ghana typically sees her 'banker' everyday to deposit as little as 25 cents. At the end of the month, she gets back her accumulated savings, with which she replenishes her stock or buys something that she could not afford out of one day's profits. She often requests an advance on the month's expected proceeds, but her banker may avoid lending because he lacks cash reserves or access to credit in case repayment is delayed. This 'banker' is an informal savings collector, known in Ghana as susu collector (Aryeetey, 1994).

Savings and loans companies have utilized the traditional susu methodology of daily or weekly deposit collection to raise their savings mobilization and to provide lower-income households with greater access to financial services (Steel and Andah, 2003). They have provided convenient transactions for urban commerce and households through adaptations of traditional susu and money lending methodologies.

Savings and Loans companies make use of microfinance strategies which are highly innovative in reaching relatively poor clients with very small, short-term transactions but which remain both costly and risky (GHAMFIN). The interest rates of these institutions are therefore higher than the traditional banks. However clients place greater value on ready access to funds than interest charges. The modes of frequent small payments (weekly, fortnightly and monthly) make it easier for clients to bear. A saving orientation that develops provides a useful strategy for screening and selection. Savings and Loans companies also demand that potential clients save with them before applying for loans. This aids in the selection of clients with discipline to pay off loans and to eliminate those who are unlikely to be able to bear the debt burden (GHAMFIN). The companies employ both individual and group lending strategies.

The clients of Savings and Loans companies are essentially urban-based and largely female (Goldstein et al, 1999). Savings and Loans companies deal with clients who are able to contribute to their strategy of savings mobilization. The clients made up of people with peculiar financial needs. These are people with relatively low social status and low income. Also a comparatively large number of the clients need to be served for the operations to be profitable. There is a high risk of default which needs to be well managed (Boateng, 2009).

2.13 Differences in Service delivery between Traditional Banks and Savings and Loans Companies

Traditional commercial banking approaches to microfinance delivery often do not work. According to traditional commercial banking principles, the credit methodology requires documentary evidence, long-standing banker-customer relationship and collateral, which most micro and small businesses do not possess. The commercial banking system reaches only about 5% of households and captures 40% of money supply (Bank of Ghana, 2007). Personal guarantors have proven to be relatively effective and enforceable as security for loans in Ghana. Savings and Loans companies tend to rely relatively heavily on personal guarantees of the borrowers while banks often insist on third party guarantors who are in a strong financial position and clearly understand their obligations (Steel &Andah, 2003).

Formal financial institutions have to their advantage extensive infrastructure and systems, funds and opportunities for portfolio diversification which allows them to present a wide range of services to their clients. However, they are mostly accessible to populations in the upper and middle income strata and very often inaccessible to rural and the urban low income population (Aryeetey, 2008). In contrast, Aryeetey (2008) states that informal financial institutions (to which Savings and Loan companies belong) operate close to rural populations and have information on their clients which enables them to conduct their operations productively. However, given their mode of operations they are unable to offer services beyond a small geographical area, resulting in highly concentrated loan portfolios (Aryeetey, 2008). Aryeetey (2008) argues further that the informal financial institutions have much better information about small borrowers than formal institutions. Informal lenders are often able to build a personal relationship with their borrowers that can ensure an extremely low loan default rate (Aryeetey, 2006).

The savings and loans companies are not directly included in the clearing and payments system. This is part of the trade-off that allows the entry of specialized financial institutions with lower minimum capital than commercial banks, and is intended to mitigate the risks of relatively weak internal controls. Bank of Ghana considers that Savings and Loans Companies are licensed to operate as savings institutions and not as general deposit institutions, and is not in favoiur of them issuing their own cheques (Steel and Andah, 2003).

Savings and loans companies rely very little on external funding, and do not have access to refinancing by the Bank of Ghana. Client savings make up nearly the entirely of their financial resources. There is therefore a great deal of competition among institutions to capture savings which has led some savings and loans companies to set up alliances with informal mechanisms, such as susu collectors, in order to increase their funding base (Goldstein et al, 1999).

CHAPTER THREE

METHODOLOGY

3.1 Introduction

This chapter explains how questions of the research were answered, methods that were employed in the study, the target population, sample size and sampling techniques as well as the various and appropriate sources of data and how the data were collected.

3.2 Target Population

The population for this study included sampled Savings and Loans Companies and SME's operating in the Ashanti Region. A total of seven Savings and Loans Companies and seventy five SME operators all in the Region were selected for the research. The SME's were engaged in various activities including manufacturing, wholesaling, retail trade, services, transport, agribusiness, construction etc.

3.3 Sample Size

A total of 75 SME entrepreneurs operating in the Ashanti Region were contacted and selected for the research work. In all 67 out of the 75 questionnaires distributed were retrieved and used for the analysis. The SME operators were not necessarily clients of the specific Savings and Loans Companies. For the Savings and Loans Companies, seven (7) were sampled for the interview. There are currently about 19 registered Savings and

Loans Companies in Ghana, most of which are located in the regional capitals and some major towns. Therefore using seven in the Ashanti Regionwas quite representative of the industry size.

3.4 Data Sources

Information from both primary and secondary sources was collected. The primary sources of data were obtained through questionnaire administered to respondents. Questionnaires were administered to SME operators across the metropolitan, municipal and districtsof the Ashanti Region - notably Adum, Abuakwa, Offinso, Obuasi, and Kejetia areas. Another set of questionnaire administered to the seven Savings and Loans Companies selected from the Region. In addition to the questionnaires, interviews were also conducted with the savings and loans companies' officials- branch managers and operations managers. Other data were obtained from brochures of the Savings and Loans Companies as well as their official website.

3.5 Methods and Procedures Used For Obtaining Data

Purposive sampling was employed in this study as the researchers were constrained by resources and time. Questionnaires were administered over a period of seven working days - from 8th-16th January, 2013 to customers of the Savings and Loans Companies who had come to the banking premises to conduct business. Some questionnaires were also administered to other SME operators who were not necessarily customers of Savings and Loans Companies interviewed.

3.6 Data Collection

Data for the research was collected mainly through the administration of well-structured questions to obtain adequate information to tackle the objectives set for the research.

Most of the questions were the closed-ended type designed to obtain accurate responses and make it easier for respondents to fill. Two types of questionnaire were administered. One was administered to the SME operators and the other to the Savings and Loans Companies.

3.7 Data Analysis

Data collected from the field was analysed using simple statistical tools including descriptive statistics. Microsoft Excel software was used to generate statistical data including percentages, bar charts and pie charts.

CHAPTER FOUR

RESULTS AND DISCUSSION

4.1 Introduction

This chapter focuses on the presentation of data analysed. The discussion focuses on the analysis of data collected from the field results. The highlights include the demographic characteristics of SME operators, the business experiences, and their degree of awareness of the formal financial institutions. It will also discuss the type of financial products offered by the savings and loans companies, an analysis of the lending process for SME loans and the challenges in lending to SME's by the savings and loans companies including loan recovery efforts.

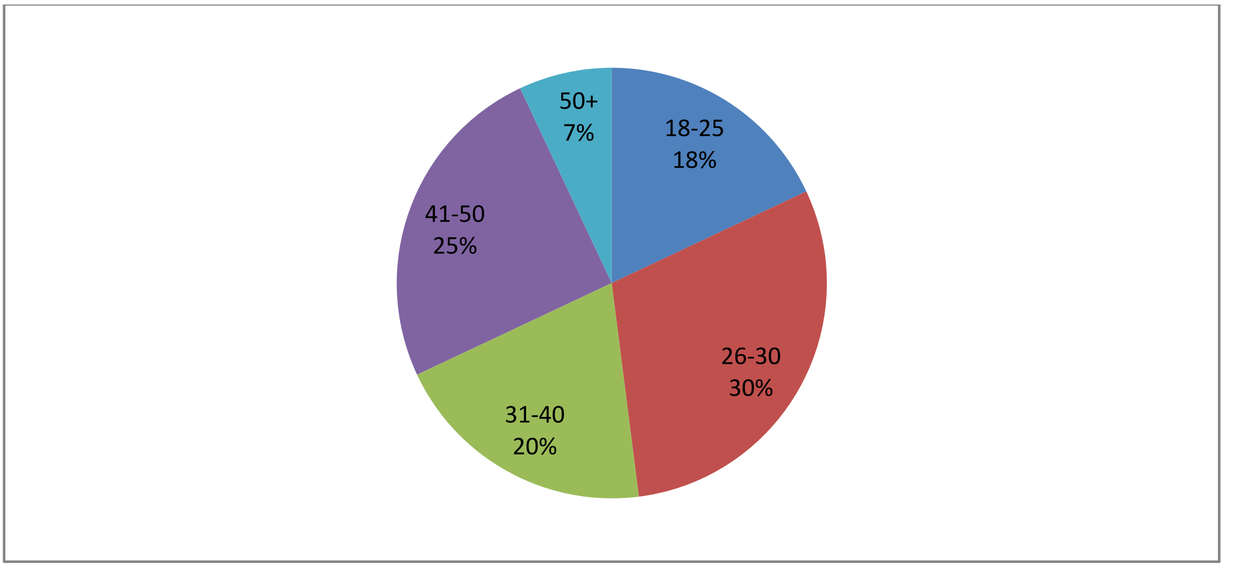
A total of 75 questionnaires were distributed to SME operators in the Ashanti Region and 67 fully answered questionnaires were retrieved and used for the analysis. The SMEs interviewed included those who are in the hospitality industry, trading, manufacturing, transportation, agri-business, engineering, general merchants, importers and exporters. And a total of seven savings and loans companies were also interviewed and offered questionnaires to complete as part of the data collection exercise.

4.2 General Characteristics of SME Entrepreneurs in the Ashanti Region

The demographic characteristics discussed here include the age, gender, educational level and literacy status of entrepreneurs.

From Figure 4.1, we can say that most the SME's in the Region is dominated by people in their youthful age. Majority of respondents, about 68% were in their youthful age between 18 – 40 years old; 25% were in the 41 – 50 year range and only 7% were above 50 years. This indicates that entrepreneurship requires some amount of youthfulness and energy to be able to handle the difficult task in building businesses.

Figure 4.1: Age of SME Operators Surveyed in Ashanti Region

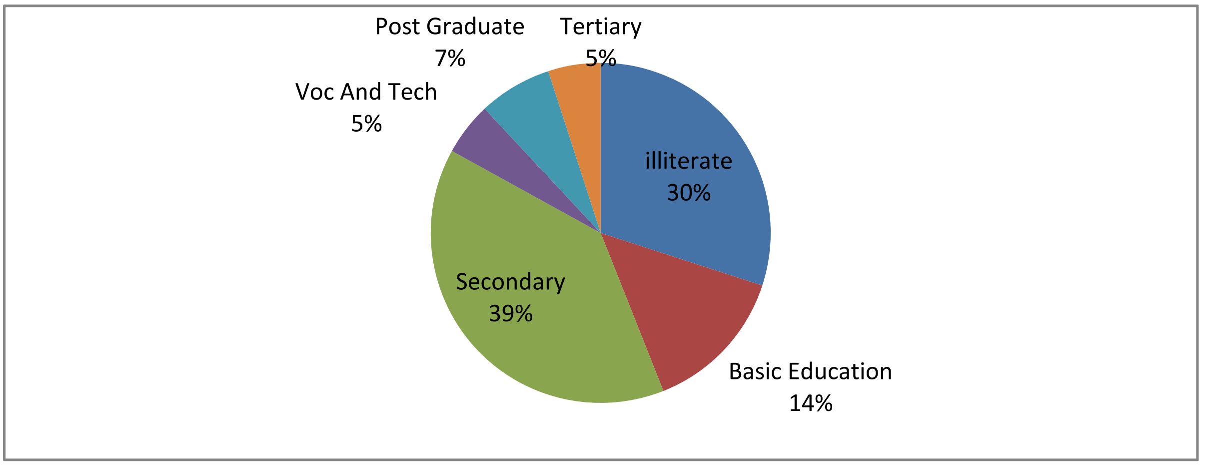


Source: field study, January 2013

Most of the SME operators also happened to be males, who constituted about 71% of the respondents and females formed 29%. The SME sector in the metropolis, from our research findings was dominated by males.

The research findings as shown in Figure 4.2 also revealed that close to 30% of SME operators were illiterates, that is had no formal education whiles the remaining 70% had some level of education.

Figure 4.2: Educational Background of Respondents



Source: field study, January 2013

The educational training ranged from the basic school certificate (14%), secondary (39%), vocational and technical (5%), tertiary education (5%) and post-graduate (7%). Thus while majority had some level of education, there were still a sizeable illiterate business operators. The illiteracy level can have an effect on the performance, management and financial management skill of entrepreneur and also loan acquisition from banks.

4.3 Business Operating Experience of SME Operators Surveyed in Ashanti Region

From Table 4.1, it can be seen that majority of SME operators surveyed were sole proprietors (75%), followed by partnerships (13%) and the limited liability companies (12%). This result is typical of most SME in Ghana, where sole-proprietorship dominates.

Table 4.1: Ownership Structure/Legal Status

Ownership Structure	**Frequency**	**Percentage**
Sole Proprietorship	50	75%
Partnership	9	13%
Limited Liability	8	12%
Total	**67**	**100%**

Source: Field study, January 2013

Our research findings also showed that most of the respondents who had 2-5 years business or working experience were in the majority (48%), followed by 6-10 years of operation (24%) and 11-20 years (15%). Only 3% of the respondents indicated they had operated as SME's entrepreneurs for more than 20 years.

Table 4.2: Number of Years of Operation or Experience of Sampled SMEs

Years	Frequency	Percentage
0 – 1	7	10.4%
2 – 5	32	47.8%
6 – 10	16	23.9%
11 – 20	10	14.9%
20+	2	3.0%
Total	**67**	**100%**

Source: Field study, January 2013

The nature of businesses that SME operators were engaged in was also analyzed, and the research revealed that the retail trade (34%), services (27%), wholesale trade (24%) and manufacturing (15%) sector dominated the SME sector in that order. The result is not surprising as it conforms to the characteristics of many SMEs in typical urban areas. The manufacturing sector was made up mostly of the limited liability companies.

Figure 4.3 Nature of the Business of SMEs in the AshantiRegion

Source: field study, December 2012

One of the important roles that SME's play in the economy is the job creation and employment offering opportunities especially for the youth. Our research findings indicated that all SME operators employed at least one hand to assist with their operations. Majority of the respondents (60%) indicated that they employed between 1 – 10 extra hands, 27% said they employed 11 – 30 staff and 5 of the medium sized firms employed well over 100 staff. This result supports the numerous research findings that SME's are indeed job creation avenues for many people and the Region is not an exception.

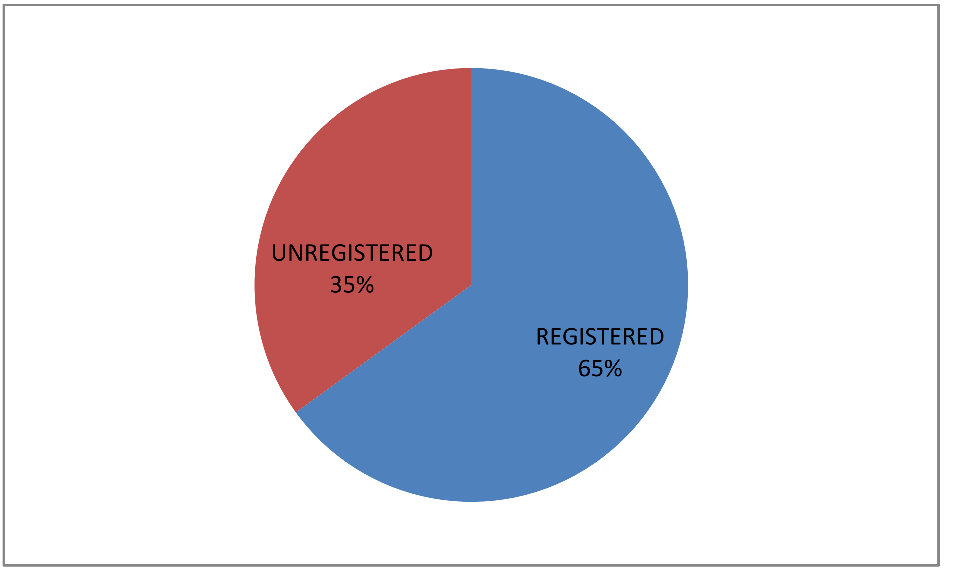
Table 4.3: Number of Employees hired by SMEs in Ashanti Region

No. of Employees	Frequency	Percentage
1-10	40	60%
11-30	18	27%
31-42	2	3%
41-100	2	3%
101-500	5	7%
Total	**67**	**100**

Source: Field study, January 2013

Small and medium enterprise in most developing countries operate within the informal sector and therefore are mostly not captured in national data as far as activities like tax return, business operating permits etc are concerned. This can affect their relationship with the formal financial institutions when it comes to funding. The results from the field as presented in figure 4.4 indicated that about 58% of business surveyed in the metropolis had some form of business registration or the other, whiles 42% were not registered. Evidence of business registration was in the form of certificates, licenses or permits from the Registrar Generals Department or the Metropolitan Assembly etc. Business registration status of SME's in the Region was generally good.

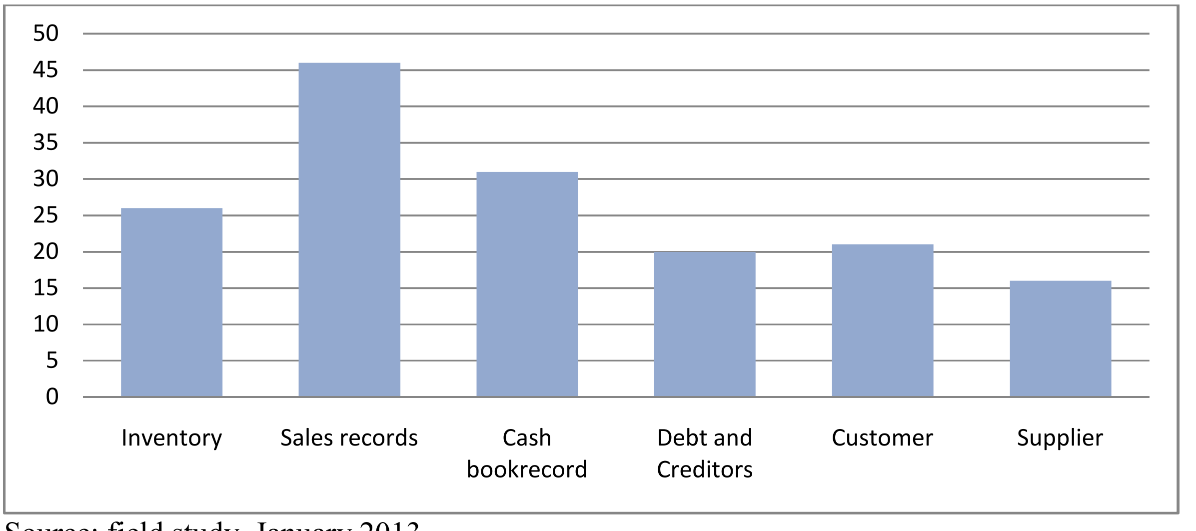
Figure 4.4 Business Registration Status of SME's surveyed in the Ashanti Region



Source: field study, January 2013

Record keeping is also an important management consideration that was checked in the survey. Almost all the SME respondents indicated that they kept one form of records or the other. The most widely reported form of records kept from our survey, as shown in figure 4.5 was sales records, cash book records and inventory records in that order.

Figure 4.5: Record Keeping Status of SME Operators in Ashanti Region



Source: field study, January 2013

Record keeping is an important component of any business activity. It is important for management decisions including finance and loan acquisition from the banks. It is expected that good business records can improve the chances of accessing credit from the formal sector.

4.4 Sources of Finance for SME's in the Ashanti Region

Finance is very important for SME businesses all over the world. However this has always been a challenge for most SME's especially in the developing countries. As a result many operators depend almost entirely on their own sources throughout the life span of the business, which makes them show slowed growth and sometimes total collapse. Research findings from the field as shown in Table 4.4, indicated that majority of SME operators in Ashanti Region (47%) used their personally savings as the major source of financing their businesses at the start-up stages, 10% depended on credit unions, 9% depended on banks and micro-finance institutions, whiles 7.5% looked up to family members for support. Only 4.5% indicated that they looked for financial help from money lenders.

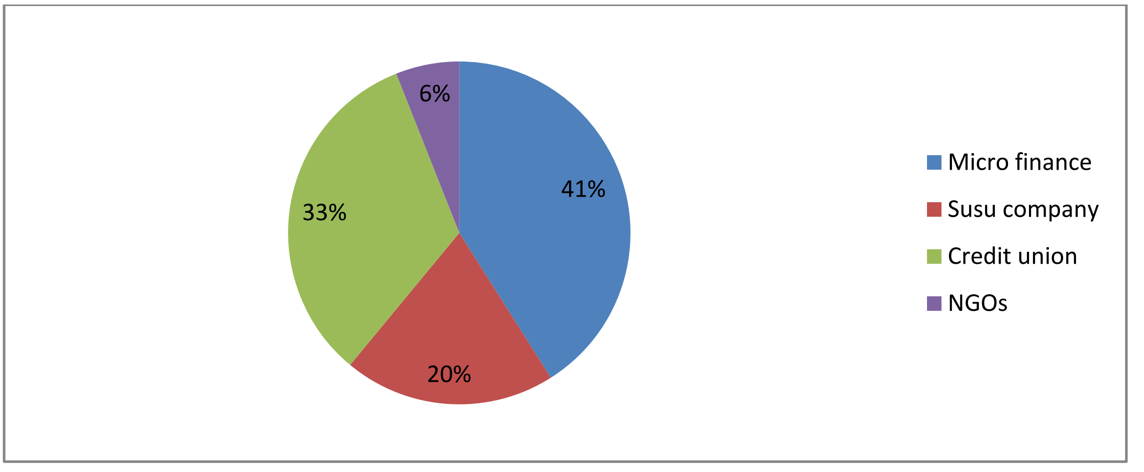
Table 4.4: Various Sources of Funds of SMEs

Source	Frequency	Percentage
Personal	36	54
Family	5	7.5
Business partners	4	6
Money lender	3	4.5
Bank	6	9
Micro finance	6	9
Credit union	7	10

Source: Field study, January 2013

Apart from personal sources of finance, we tried to find out the other sources that SME operators went to seek for funds. As deposited in Figure 4.6, it was realized that the other most important sources of funds for most SME operators were the micro-finance institutions including savings and loans companies (41%), Credit Unions (33%), Susu Companies (20%) and NGO’s (6%).

Figure 4.6: Other Sources of Funds by SME's



Source: field study January 2013

We can conclude here that Savings and Loans Companies can therefore be a good and reliable alternative for SME financing

4.5 Types of Products and Services Delivered by Savings and Loans Companies

The focus of this research work was on how Savings and Loans Companies in the Ashanti Region were serving as an alternative source of financing for SME's in the metropolis. The Savings and Loans Companies surveyed, seven in all, had a variety of products and services. These deposit products included current accounts, ordinary savings account, fixed deposit accounts and susu savings accounts. These four products were offered by all the banks surveyed, as indicated in Table 4.5.

The other most commonly occurring products included micro-finance group savings and other forms of savings products nicked named 'Boafo' account, 'Anidaso' account etc.

Table 4.5: Products and Services of Savings and Loans Companies in Ashanti Region

Products/Services	Frequency	Percentage
Current Account	7	100%
Ordinary Savings	7	100%
Fixed Deposits	7	100%
Susu Savings	7	100%
Money Transfer – Western Union	5	71%
Others	7	100%
SME Loan	7	100%
Payroll Loan	7	100%
Commercial Loan	5	71%
Susu/Micro-Finance Loan	5	71%
Personal Loans	7	100%

Source: Field study, January 2013

The credit or loan types offered by these institutions included personal loans, payroll loans, commercial loans and SME loans. All the S & L companies surveyed indicated that they offered these types of loan products. Five of the S & L firms indicated they provided 'susu' and micro-finance loans to individual and groups members. The provision of micro-credit in the form of susu loans or micro-finance loans is common feature of most S & L Companies. This is usually offered to micro-enterprises and SME's often in the rural communities.

From this we can ascertain that S & L Companies offered products and services that are similar to those provided by the commercial banks.

4.6 SME Financing Needs and Types of Loans Provided by Savings and Loans Companies

Small and medium enterprises require credit to run and operate their businesses at the start-up and most importantly the expansion state. Our research work examined the types or kinds of credit needs of most SME's when they applied for loans from the S&L companies. From Table 4.6; it was realized that all the 67 respondents (100%) mentioned working capital needs as need. This type of credit is required for stock purchases or inventories, payment of suppliers, fuels, utility, salaries of workers etc. Thirty of the respondents (45%) also mentioned that they needed credit to purchase capital assets like working tools, equipment and machinery. Twenty of the SME's also stated that they needed overdraft facility to meet immediate and urgent transaction needs. Overdrafts are faster or quicker to source as they may not require detailed collateral requirements.

Table 4.6 Finance and Credit Needs of SME'S

Type	Frequency	Percentage
Working capital	67	100%
Assets base capital	30	45%
Short term capital	11	17%
Overdraft	10	15%

Source: Field study, January 2013

4.7 Challenges of Lending to SME'S by savings and Loans Companies

Financial institutions have always regarded SME's as very risky due to a number of reasons. Poor information asymmetry, the highly informal nature of business ownership, poor business and financial management ability of SME operators are some of the common reasons. SME's also view the requirements for accessing loans from financial institutions as very complicated and tasking. Our research work examined the challenges that SME's and the S & L Companies face when it comes to providing credit. First we considered the requirements that the S & L Companies demanded from SME operators as part of their loan application process. All the six (100%) of financial institutions required their SME clients to submit or make provide some form of collateral security as part of loan application process. The reason was more to check for risk of SME not being able to repay loan. As indicated in Table 4.6, six of the seven banks represents 86% of the banks indicated that they required some level of business information from their SME clients in approving loans. The information included basic business information like sales records, receipts, invoices, location of business, years of operations, VAT payments, contract letters, loan purpose etc. Since most SME could not provide audited financial statements, the S & L Companies demanded these documents to help them assess the SME applicants' capacity to repay loan.

Table 4.7 Demands or Requirements for SME Loan by S & L Companies

Category	Frequency	Percentage
Financial statement	4	57%
Business plan	2	29%
Business registration	6	86%
Business information	6	86%
Collateral security	7	100%

Source: Field work, January2013

Six of the S & L Companies also stated that business registration was considered as part of their loan assessment procedures for SME applicants. SME's that are registered are considered to be more formal and may operate within a more transparent system than unregistered firms. The S & L Companies did not consider business plan from SME's as an important requirement since most clients could not prepare bankable business proposals.

When the SME's asked to indicate the requirements they had the meet in applying for credit from the S & L Companies, as shown in Table 4.7, they listed collateral security requirement as the most prevalent. All the sixty seven respondents indicated that collateral security was a requirement, 67% stated business registration as a requirement and 67% stated their bankers needed financial statements as a proof of their financial performance. This can also be usd to determine loan repayment ability of applicants.

Table 4.8 Requirements for Applying SME Loan by Applicants

Category	Frequency	Percentage
Financial statement	45	67%
Business plan	20	30%
Business registration	40	60%
Collateral security	67	100%

Source: Field work, January 2013

The SME operators in their loan application process encountered some difficulties which can be considered as a hindrance to access to finance. As shown in Table 4.8 some these included the high interest rate charges (100%) by S & L Companies, the need for collateral security (100%), delays in processing loans (60%) and cumbersome procedures recorded 54%.

About 45% of clients also indicated that they did not receive the exact amount of loan requested for. Only 20 (30%) of the 67 respondents mentioned bureaucratic procedures as major problem.

Table 4.9 Challenges in Loan Acquisition Process from S & L Companies in the Ashanti Region

Category	Frequency	Percentage
Collateral security	67	100%
Cumbersome procedure	36	54%
Delays in loan approvals	40	60%
Bureaucratic procedures	20	30%
High interest rate	67	100%
Loan amount not granted	30	45%

Source: Field work, January 2013

The savings and loans companies like most formal financial institutions in Ghana, are required to adopt anti-risk measures in managing their portfolio's to reduce the default and bad loans. They therefore put in place mechanism to minimize this risk and this can be seen by SME applicants as hindrances or difficulties in accessing loans.

4.9 Suggestions for Improving Loan Access by Savings and Loans Companies to SME Clients in Ashanti Region

Another objective of this study was to offer suggestions and recommendations on how improve access to credit from savings and loans companies to SME's.

The suggestions made here are basically those offered by the SME operators in the research. In order to improve access to credit from the Savings and Loans Companies, the SME operators made the following suggestions:

- The S & L Companies should reduce interest rate charges on SME loans
- The procedures for loans application should be made less cumbersome
- The S & L Companies should accept other forms of collateral security other than landed collateral
- The S & L Companies should fast-track and improve loan approval process.
- The S & L Companies should improve offering other short term loans like overdraft facilities.

The Savings and Loans Companies also offered the following suggestions for lending SME operators as follows:

- SME clients should improve their business management skills including basic record keeping, marketing etc.
- SME clients should enhance their financial and credit management skills

- SME operators must make regular cash lodgement into their business accounts and use the banks transaction systems such as cheques for payments. This would give the banks a better appreciation of financial transactions.
- SME businesses should formalize their business operations registering and using VAT invoices, paying taxes etc.
- Lastly SME’s should be assisted to prepare financial statements and business plans.

CHAPTER FIVE

SUMMARY OF FINDINGS, CONCLUSION, AND RECOMMENDATIONS

5.1 Introduction

This part of research consists of conclusions and recommendations. The findings were those important issues about SME financing that were discovered through the analysis of the field data captured through the questionnaires administered. The conclusion deals with a summary of the entire research work. The recommendation was based on objectives set for this research and issues that were identified during the field work.

5.2 summaries of findings

In spite of the large employment and job creation capabilities, SME's are saddled with difficulties of financial crisis. It is the financing options that prompted this research. Fund has been hampering the operations of SME's in the Ashanti Region, leaving some of them completely out of business or stagnant in growth. Some of them simply do not get the necessary support from lenders and even those who get it complain of limited fund.

The research was conducted to determine the role of Savings and Loans Companies as financing options for SME's in Ashanti Region. Four specific objectives were set to determine the outcome of the research topic. Generally it can be stated that SME's are very important to the economic and social development of Ashanti Region and Ghana for that matter.

Access to finance forms a very important means to improve the performance of businesses in the SME sector.

Results and analysis of our research findings from the Savings and Loans Companies and SME's in the Ashanti Region indicated enabled us to draw the following conclusions:

- SME's in the Ashanti Region is dominated by sole proprietors (75%); most operators are males and are in the youthful age of 18-40 (80%).
- Most of the SME operators have between 2-10 years of business experience; more than 60% had registered their businesses and therefore are considered to be relatively formal.
- The major businesses SME operators were engaged were the retail, services, wholesale and manufacturing in that order.
- The main source of finance for most SME in the Ashanti Region was personal finance. The alternative sources of funding for most operators were the S&L Companies that provided similar products as those offered by the micro-finance institutions. They also depended on the credit unions as a good source of credit.
- The major products offered by the S&L Companies were similar to those the traditional banks. Theyincluded ordinary savings, current and fixed deposits accounts. They also provided micro-finance and susu savings accounts of various kinds.
- The credit facilities offered by S&L Companies included SME loans, commercial loans, salaried loans, personal loans, micro-credit or susu loans.
- The major challenges that S&L Companies encountered in their lending programs to SME included lack of securable collateral by SME's, absence of business

registration certificates, poor business information and management records keeping leading to information asymmetry and inability of SME's to provide good financial statements.

- The SME's on the other hand encountered some problems in loan acquisition from S&L Companies. These included high interest rate charges by S&L Companies, cumbersome procedures, delays in loan approvals, and demand for landed collateral security.

5.3 Conclusion

SMEs are the aggressive catalyst to the growth and the development of the Region and the Nation as a whole. As such, all efforts must be made to assist them in terms of finance.

The government should provide access to capital through banks at preferential terms

The government should serve as a security on behalf of SMEs in terms of sourcing for finance from the S & L; since new entrant finds it difficult to provide collateral security.

5.4 Recommendation

Based on the conclusions drawn from the research work, we make the following recommendation for the use of SME operators, S&L Companies, other financial institutions, policy makers and government.

- SME's should be assisted to explore other sources of funding like the S&L Companies where loan products and services tend to be relatively flexible.

- Other sources of credit, like government finance schemes, where collateral security is not a major demand, should also be explored by SME's
- To minimize risk and loan default from SMEs, it is recommended that S&L Companies consider providing group lending to SMEs who agree to do so.
- SME clients should improve their business management skills including basic record keeping, marketing etc.
- SME clients should enhance their financial and credit management skills
- SME operators must make regular cash lodgement into their business accounts and use the banks transaction systems such as cheques for payments. This would give the banks a better appreciation of financial transactions.
- The S & L Companies should reduce interest rate charges on SME loans
- The procedures for loans application should be made less cumbersome
- The S & L Companies should accept other forms of collateral security other than landed collateral
- SME businesses should formalize their business operations registering and using VAT invoices, and paying taxes.
- Lastly SME's should be assisted to prepare financial statements and business plans.

The relationship between the two can be enhanced if the Savings and Loans Companies can support the SME's clients by building long term business relations, offer training services in credit management and improve on service delivery such as faster loan approval times, lessened collateral requirement and much simpler loan procedures.

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APPENDIX – 1

QUESTIONNAIRES FOR SME's

A. GENERAL CHARACTERISTICS / BACKGROUND INFORMATION

1. Name of the venture/business……………………………………….....................

2. Location: ………………………Tel number: …………………………………

3. Number of branches/outlets …………………………………………………….

4. Age of Entrepreneurs

   18-25 Yrs [ ]

   26-30 Yrs [ ]

   31-40 Yrs [ ]

   41-50 Yrs [ ]

   50 Yrs + [ ]

5. Gender of entrepreneur

   [ ] Males Female [ ]

6. What is your educational background?

   [ ] Illiterate [ ] Basic Education [ ] Secondary

   [ ] Vocational, Technical [ ] Tertiary [ ] Post-graduate

B. Business Operation – General Characteristics and Experience

7. What is the ownership structure or legal status of this business/enterprise?

   [ ] Sole-proprietorship [ ] Partnership

   [ ] Limited Liability Company

8. How many years have you operated this particular business?

   [ ] 0-1 yr [ ] 2-5 yrs [ ] 6-10 yrs [ ] 11-20 yrs [ ] 20yrs+

9. What is the ownership structure of venture/enterprise?

[ ] Ghanaian owned [ ] Foreign owned [ ] Mix – Ghanaian and Foreign

10. What is the type/nature of your business?

[ ] Manufacturing [ ] Wholesale [ ] Retail [ ] Service

11. What specific products or services do you deal in? ....

12. How many employees do you have?

[ ] 1-10 [ ] 11-30 [ ] 31-40 [ ] 41-100 [ ] 101-500

13. Is your business registered?

[ ] Yes [ ] No

14. If yes, what kind of registration or by which agency? …..........…………..

15. Which of these management records do you keep for the business?

[ ] Inventory Records [ ] Sales Records

[ ] Cash Book Records [ ] Debtors and Creditors Records

[ ] Customer Records [ ] Suppliers Records

16. What is your main source of finance to start-up your business? Tick those that apply

[ ] Self [ ] Friends [ ] Family

[ ] Business Partner [ ] Money lender [ ] Bank

[ ] Micro-Finance Company [ ] Credit Union

17. What is your main source of credit/finance as you expand your business?

[ ] Plough back profit [ ] Friends [ ] Family

[ ] Business Partner [ ] Money lender [ ] Bank

[ ] Micro-Finance Company [ ] Credit Union

18. Have you ever sourced for credit/finance from the formal financial institution?

[ ] Yes [ ] No

19. If yes, which source did you approach for finance? Tick all that apply

[ ] Universal Banks [ ] Rural Banks

[ ] Savings & Loans Companies [ ] Leasing Company

[ ] Venture capital firm [ ] Discount House

[ ] Government Sources

20. Which other sources of finance apart from the above have you accessed or tried to access credit?

[ ] Micro-Finance Company [ ] Susu Company [ ] Credit Union

[ ] NGO funds

22. What factors influenced your choice of selection of this particular financial institution?

[ ] Recommendation by friend [ ] Advert on media

[ ] Range of products [ ] To secure a loan

[ ] Have flexible/better terms

23. Which kind of products or services did the financial institution provide?

[ ] Current Accounts [ ] Savings Accounts [ ] Fixed Deposits

[ ] Susu Savings [ ] Money Transfer

24. Have you applied for a loan from the commercial banks before?

[ ] Yes [ ] No

25. Was your application granted?

[ ] Yes [ ] No

26. If no, were you told the reasons for non-approval?

[ ] Yes [ ] No

27. If yes, tick the reason given for rejecting your application?

[ ] Unable to provide landed collateral [ ] No proper financial records kept

[ ] Low turnover

29. Do you know about the lending policy of savings and loans companies?

[ ] Yes [ ] No

30. What loan types do they usually offer to you?

[ ] Working Capital [ ] Asset based capital

[ ] Short term capital [ ] Overdraft

31. What three major problems do you encounter with savings and loans companies?

[ ] Cumbersome procedures [ ] Delays in loan approval

[ ] High interest rate [ ] Loan amount not granted

[ ] Bureaucratic procedures

32. What do you suggest the company must do to improve their services?

[ ] Less cumbersome procedures for loan approval [ ] Easy access to loan

[ ] Attractive interest rate [ ] Fast - track and improve loan approval

APPENDIX – 2

QUESTIONNAIRES FOR SAVINGS AND LOANS COMPANIES

A. General Profile of Financial Institution

1. Name of Financial Institution:…………………………………………………

2. What are the major investment or deposit products?

[ ] Savings Accounts [ ] Current Accounts [ ] Fixed Deposits

[ ] Treasury Bill [ ] SME Account [ ] Salaried Accounts

[ ] Susu Savings [ ] Group Savings

[ ] Others ……………………………………………………………………

3. What are the types of credit products on offer to customers? Please tick where applicable

[ ] Commercial bank [ ] SME Loan [ ] Payroll loan

[ ] Micro finance/Group loan [ ] Overdraft

[ ] Personal/Consumer loan

[ ] Others ………………………………………………………..........………

4. Does the bank have an SME lending Policy?

[ ] Yes [ ] No

5. If yes, to what extent do you think your customers are aware of this policy?

[ ] Very much aware [ ] Fairly good knowledge [ ] Low awareness

6. Do you provide any form of training for your SME clients?

[ ] Yes [ ] No

7. If yes, what kind of training do you usually offer?

[ ] Business management [ ] Credit management

[ ] Financial statements preparation [ ] Records keeping

8. Which category of SME constitutes your major clients, in terms of numbers and value of portfolio? Rank them as 1, 2, 3 and 4

[ ] General Merchants - Traders, wholesalers, retailers

[ ] Manufactures

[ ] Service Providers

[ ] Importers & Exporters

9. How long should an SME customer operate an account before a loan can be granted?

0-3 months [ ] 6-12 months [ ] 12 months+ [ ]

10. How would you generally rate the financial literacy capacity of most of your SME clients?

[ ] Excellent [ ] Very Good [ ] Good

[ ] Average [ ] Below average [ ] Very Poor (None at all)

11. SME applicants usually apply for loans for which of the following purposes? Please rank them

For start-up [ ]

For expansion [ ]

As working capital [ ]

Capital expenditure [ ]

Others (state) ……………………………………………………………………

12. What range of loan does your financial institution give to SMEs?

[ ] GH¢1,000 – GH¢5,000

[ ] GH¢10,000 – GH¢20,000

[ ] GH¢30,000 – GH¢50,000

[ ] GH¢50,000 – GH¢100,000

[ ] Above GH¢100,000

13. Which of these business-related requirement and risk-mitigation tool are necessary conditions in your SME lending? Tick as many as apply

[ ] Collateral security [ ] Credit history

[ ] Business plan [ ] Audited financial statements

[ ] Asset turnover [ ] Cash lien / Guarantor

[ ] Business records

[ ] Business records – Inventory, sales, cash book, debtors and creditors etc

14. Which of these categories constitute tour largest categories of borrowers?

[ ] SME's [ ] Payroll workers [ ] Micro-finance groups

[ ] Corporate bodies [ ] Petty traders [ ] Others

15. Does the bank use interest rate charge as a risk mitigation tool for SME loans?

[ ] Yes [ ] No

16. What challenges does the bank encounter in lending to SME customers?

[ ] Poor asymmetry of information

[ ] Poor business and financial management ability

[ ] Lack of proper business plan

[ ] High informal nature of business owner ship

17. SME's are considered to be generally risky. What do you think needs to be done to make them more attractive to work with?

[ ] Provision of collateral security [ ] Provision of business information

[ ] Provision of proper financial statement [ ] Business registration

First of all, the government and the regulatory agencies such as the State Bank of Pakistan need to provide a conducive and enabling environment for SMEs to operate. This requires that the macroeconomic policies are sound, the regulatory regime is supportive and the legal system is able to enforce contracts and property rights. There ought to be a level playing field for both the small and large entrepreneur and there is no preferential treatment for any particular class. In the past the SROs were being used to favour certain individuals or tariffs were raised to protect selective groups or banks loans were given to supporters of the ruling parties. In the past five years, however, these practices have been done away and a level playing field now exists for all businesses – small or large – in the economy.

The second player in this process is the Provincial and the local Governments. They have to allocate and earmark land for setting up industrial estates and deliver the infrastructure facilities in these estates. The economies of agglomeration dictate that if clusters of same industries are relocated in the same vicinity the suppliers of raw materials and components, and providers of services and marketing of output also move to the same areas. The logistics management and reduction in transportation cost reduce the unit cost of production and distribution for a single enterprise and also improve the reliability and timeliness in the delivery of products. In many countries such zones and clusters have worked very well and helped small and medium enterprises to become more competitive.

Thirdly, organizations such as SMEDA have to play a critical role in the business developments support, advisory services and managerial training of SMEs. For example, most small enterprises do not maintain proper accounting of their operation and do not have a trained accountant on their staff. This impedes their ability to access credit from commercial banks. SMEDA can organize training courses in accounting and assign these certified trainees to work on a part–time basis with a number of enterprises. Simple

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accounting software packages are now available for small businesses and these can be profitably used in a large number of SMEs. SMEDA can design simplified standardized book keeping, inventory management and ledger forms which can aid in the preparation of financials.

The SME Bank, which was established in the public sector in 2002 to provide financing to the SME sector, is another important player in the sector. However, it alone cannot cater to the needs of the entire sector but it could develop a prototype of program lending, credit appraisal and delivery methodology, standardized documentation, monitoring mechanisms, which can be replicated and followed by other commercial banks. The SME Bank can produce experienced and skilled professionals who are specialists in the SME credit for the whole industry.

The commercial banks, leasing industry, modarabas themselves have to develop dedicated groups for servicing the SMEs. They should establish their presence and branches at the clusters and places such as Daska, D.I.Khan, Wazirabad, Khairpur, Kotri, Gwadur which have large untapped potential. If the SME branches of the banks remain limited to a few big cities you will never be able to make a profitable business out of the SME sector. The balance sheet, cost of funding, the geographical spread do confer a big advantage to the big banks and if they do not make innovative use of technology, skills, systems and procedures to capitalize on this advantage they will soon be marginalized by the intrusion of more agile and nimble small private banks. The banking industry has to invest in people, processes and systems to minimize their risks and enhance their returns on the SME segment.

Besides banks and DFIs, Leasing Companies and Modarabas are also the right vehicles for delivery of credit to the SME sector. Unfortunately with the exception of one or two leasing companies they have limited their activities so far to large urban areas and have not opened up their doors for business